SECURE 2.0 Act Update

On December 29, 2022, as part of a government funding bill, President Biden signed into law the *SECURE 2.0 Act of 2022* ("SECURE 2.0"). This legislation builds upon 2019's *Setting Every Community Up for Retirement Enhancement Act* (the "SECURE Act").

SECURE 2.0 contains 90 provisions aimed at modernizing the retirement system, encouraging additional retirement savings, and easing administrative requirements. The changes will have at least some impact on most plans, potentially as soon as this year.

Below, we review the provisions we believe may be most relevant to you.

Plan Design Provisions

Expanding automatic enrollment in retirement plans. SECURE 2.0 makes automatic enrollment mandatory for new 401(k) plans established after the date of enactment of SECURE 2.0 (December 29, 2022). This means that plans established in 2023 and thereafter must adopt automatic enrollment effective for plan years beginning after December 31, 2024.

Exemptions to this rule:

- Plans established prior to December 29, 2022,
- Plans sponsored by employers that normally employ fewer than 11 employees
- New businesses (exempt during the first three years of existence of the business or a predecessor business).

The initial automatic deferral percentage must be at least 3% but no more than 10% of the employee's compensation, with automatic annual increases of 1% until the deferral amount is at least 10% but no more than 15%. Participants may opt out and the plan must allow permissible withdrawals up to 90 days after the first auto deferral.

Note to MEP Sponsors: an adopting employer must be treated as a separate entity for this rule.

Increase in age for required beginning date for mandatory distributions. The SECURE Act of 2019 increased the required minimum distribution ("RMD") age to 72. SECURE 2.0 further increases the required minimum distribution age to 73 starting in 2023 and to 75 starting in 2033.

Small immediate financial incentives for contributing to a plan. This provision permits employers to offer de minimis financial incentives (for example, low-dollar gift cards), not paid for with plan assets, to encourage employees to participate in workplace retirement plans. This change is effective for plan years beginning after enactment of SECURE 2.0.

Improving coverage for part-time workers. The SECURE Act of 2019 is currently in effect and requires employers to allow long-term, part-time (LTPT) workers to participate in 401(k) plans when the employee has attained age 21 and completed three consecutive years of service with at least 500 hours of service per year starting with the 2021 plan year. Effective January 1, 2024, plans may see their first LTPT workers become eligible to participate. Under the SECURE Act of 2019, years of service prior to 2021 are disregarded for determining eligibility and vesting under the plan.

SECURE 2.0 reduces the three-year service requirement to just two years, and the first time a LTPT worker will be eligible to participate in the plan under SECURE 2.0 will be on January 1, 2025. Under SECURE 2.0, years of service prior to 2023 are disregarded for determining eligibility and vesting under the plan.

401(k) plans are only required to offer to LTPT workers the opportunity to defer. Employer contributions, including safe harbor contributions, are not required. Further, participants classified as LTPT are excluded from nondiscrimination testing and are not required to receive top-heavy minimum contributions.

Contribution & Investment Provisions

Higher catch-up limit to apply at age 60, 61, 62, and 63. SECURE 2.0 increases and indexes to inflation catch-up contribution limits for individuals between ages 60 and 63. The catch-up contribution limit for 2023 is $7,500. Beginning in 2024, SECURE 2.0 increases these limits to the greater of $10,000 or 50% more than the regular catch-up amount in 2024 for individuals who have attained ages 60, 61, 62 and 63. The increased amounts will be indexed for inflation after 2024.

Treatment of student loan payments as elective deferrals for purposes of matching contributions. This highly anticipated provision permits an employer to make matching contributions under a 401(k) plan with respect to "qualified student loan payments" that an employee makes outside the plan. A qualified student loan payment is broadly defined as any indebtedness incurred by the employee solely to pay qualified higher education expenses of the employee. This provision is effective for contributions made for plan years beginning after December 31, 2023.

Elective deferrals generally limited to regular contribution limit. Under current law, catch-up contributions to a qualified retirement plan can be made on a pre-tax or Roth basis (if permitted by the plan). Effective for plan years beginning after December 31, 2023, SECURE 2.0 requires all catch-up contributions to qualified retirement plans to be made on a Roth after-tax basis. An exception is provided for employees with compensation of $145,000 or less (indexed for inflation).

Optional treatment of employer matching or nonelective contributions as Roth contributions. Under current law, matching contributions made by an employer must be on a pre-tax basis only. Effective immediately following enactment of SECURE 2.0, defined contribution plans may provide participants with the option of receiving matching contributions on a pre-tax or Roth after-tax basis.

Distribution & Withdrawal Provisions

Withdrawals for certain emergency expenses. SECURE 2.0 provides an exception to the 10% early withdrawal penalty for certain distributions used for emergency expenses. Emergency expenses are defined as unforeseeable or immediate financial needs relating to personal or family emergency expenses.

One distribution of up to $1,000 is permissible per year, and a taxpayer has the option to repay the distribution within three years. This provision is effective for distributions made after December 31, 2023.

Exemption for certain automatic portability transactions. SECURE 2.0 marks a significant change in the existing practice of "cashing out" terminated employees' sub-$5,000 retirement account balances. This provision permits a retirement plan service provider to provide employer plans with automatic portability services. Such services involve the automatic transfer of a participant's default IRA (established in connection with a distribution from a former employer's plan) into the participant's new employer's retirement plan, unless the participant affirmatively elects otherwise. This provision is effective for transactions occurring on or after December 29, 2023.

Emergency savings accounts linked to individual account plans. SECURE 2.0 permits employers to offer short-term emergency savings accounts ("ESAs") to non-highly compensated employees as part of a defined contribution plan. ESAs must be funded with Roth contributions, and participants may be automatically enrolled at a rate of up to 3% of compensation. Contributions must be capped at $2,500 (indexed for inflation) or a lower amount determined by the sponsor, and there cannot be minimum contribution or balance requirements. Participants must be allowed to take at least one withdrawal from the ESA each month, and the first four withdrawals of each year cannot be subject to fees. This provision is effective for plan years beginning after December 31, 2023.

Reduction in excise tax on certain accumulations in qualified retirement plans. Existing law imposes an excise tax on an individual if the amount distributed to an individual during a taxable year is less than the RMD under the plan for that year. The excise tax is equal to 50% of the shortfall (that is, 50% of the amount by which the RMD exceeds the actual distribution). SECURE 2.0 reduces the excise tax rate from 50% to 25%, and further reduces the rate to 10% if the individual corrects the shortfall during a two-year correction window. This provision is effective for taxable years beginning after enactment of SECURE 2.0.

Updating dollar limit for mandatory distributions. SECURE 2.0 increases the involuntary cash-out limit for terminated employees from $5,000 to $7,000, effective for distributions after December 31, 2023.

Repayment of qualified birth or adoption distribution limited to three years. The SECURE Act of 2019 created qualified birth or adoption distributions. SECURE 2.0 clarifies that qualified birth or adoption distributions may be recontributed to the plan only within three years of the distribution in order to qualify as a rollover contribution. This provision is effective for distributions made after enactment of SECURE 2.0.

Employer may rely on employee certifying that deemed hardship distribution conditions are met. SECURE 2.0 provides that, under certain circumstances, employees are permitted to self-certify that (1) they have had an event that constitutes a hardship for purposes of taking a hardship withdrawal, (2) the distribution is not in excess of the amount required to satisfy the financial need, and (3) the employee has no alternative means reasonably available to satisfy the financial need. This provision is effective for plan years beginning after enactment of SECURE 2.0.

Penalty-free withdrawal from retirement plans for individual in case of domestic abuse. SECURE 2.0 allows retirement plans to permit participants who self-certify that they experienced domestic abuse to withdraw the lesser of $10,000 (indexed for inflation), or 50% of the participant's account balance. A distribution made under this section is not subject to the 10% early withdrawal penalty. Additionally, a participant has the opportunity to repay the withdrawn money from the retirement plan over three years. This provision is effective for distributions made after December 31, 2023.

Roth plan distribution rules. Under current law, required minimum distributions rules do not apply to a Roth IRA prior to the IRA owner's death, but they do apply to Roth amounts in an employer retirement plan. SECURE 2.0 eliminates the pre-death distribution requirement for Roth accounts in employer plans, effective for taxable years beginning after December 31, 2023.

Exception to penalty on early distributions from qualified plans for individuals with a terminal illness. SECURE 2.0 creates an exception to the 10% early withdrawal penalty for distributions to individuals whose physician certifies that they have an illness or condition that is reasonably expected to result in death in 84 months or less. This provision is effective upon enactment of SECURE 2.0.

Surviving spouse election to be treated as employee. This provision allows a surviving spouse to elect to be treated as the deceased employee for purposes of the required minimum distribution rules, effective for calendar years beginning after December 31, 2023.

Special rules for the use of retirement funds in connection with qualified federally declared disasters. In recent years, Congress has eased plan distribution and loan rules in cases of disaster on a case-by-case basis. SECURE 2.0 provides permanent special rules governing plan distributions and loans in cases of qualified federally declared disasters:

- Up to $22,000 may be distributed to a participant per disaster;
- The amount is exempt from the 10% early withdrawal fee;
- Inclusion in gross income may be spread over a three-year period;
- Amounts may be recontributed to a plan or account during the three-year period beginning on the day after the date of the distribution;
- Certain home purchase distributions may be recontributed to a plan or account if those funds were to be used to purchase a home in a disaster area and were not so used because of the disaster; and
- Increased loan maximums and extended repayment terms.

Long-term care contracts purchased with retirement plan distributions. SECURE 2.0 permits retirement plans to distribute a certain amount per year for certain long-term care insurance contracts. The amount permitted to be distributed is the lowest of: (1) the amount paid by or assessed to the employee during the year for long-term care insurance; (2) 10% of the employee's vested accrued benefit in the plan; or (3) $2,500 (indexed for inflation beginning in 2025). Distributions from plans and IRAs are exempt from the 10% early withdrawal penalty when used to pay premiums for high quality, long-term care insurance. This provision is effective as of December 29, 2025.

Plan Administration Provisions

Recovery of retirement plan overpayments. Under current law, fiduciaries for plans that have mistakenly overpaid a participant must take reasonable steps to recover such overpayment, such as collecting the overpayment from the participant, or having the employer reimburse the plan. SECURE 2.0 allows fiduciaries the discretion to decide not to recover inadvertent overpayments made to participants. This provision is effective upon enactment of SECURE 2.0, with retroactive relief for prior good faith interpretations of existing guidance.

Expansion of Employee Plans Compliance Resolution System ("EPCRS"). SECURE 2.0 expands EPCRS to (1) allow more types of errors to be self-corrected, (2) apply to inadvertent IRA errors, and (3) exempt certain failures to make required minimum distributions from the otherwise applicable excise tax. This provision is effective upon enactment of SECURE 2.0, and the IRS is required to issue implementing guidance by December 29, 2024.

Amendments to increase benefit accruals under plan for previous plan year allowed until employer tax return due date. SECURE 2.0 allows plans to make discretionary plan amendments to increase benefits until the employer's tax filing deadline (including extensions) for the immediately preceding taxable year in which the amendment is effective. This provision is effective for plan years beginning after December 31, 2023.

Eliminating unnecessary notice requirements for unenrolled participants. Under current rules, employees who are eligible but choose not to participate in a plan ("unenrolled participants") are still required to receive numerous plan notices and disclosures. SECURE 2.0 amends notice requirements for unenrolled participants to consist solely of an annual notice of eligibility to participate. This provision is effective for plan years beginning after December 31, 2022.

Requirement to provider paper statements in certain cases. SECURE 2.0 updates the existing requirements to provide paper benefit statements to participants. Defined contribution plans will be required to provide a paper benefit statement at least once annually, unless participants have affirmatively elected electronic delivery in accordance with applicable DOL requirements. The DOL must update the relevant sections of their regulations and corresponding guidance by December 31, 2024, and the annual paper statement is effective for plan years beginning after December 31, 2025.

Safe harbor for correction of employee elective deferral failures. SECURE 2.0 provides a grace period after the end of the existing EPCRS automatic enrollment and automatic escalation safe harbor that expires on December 31, 2023. Under this grace period, employers are allowed to correct, without penalty, reasonable errors in administering automatic enrollment and automatic escalation features. Errors must be corrected prior to 9 ½ months after the end of the plan year in which the mistakes were made. This provision is effective for errors after December 31, 2023.

Other Provisions

Retirement savings lost and found. SECURE 2.0 directs the DOL to create an online searchable "Lost and Found" database by December 29, 2024, which will collect information on benefits owed to missing, lost or non-responsive participants and beneficiaries in tax-qualified retirement plans, and will be used to assist such plan participants and beneficiaries in locating those benefits.

Plan document amendments for these provisions must be adopted by December 31, 2025.

This summary is being provided for informational purposes only and is not designed to be complete in all material respects. As additional guidance is released, we will attempt to provide further information on items that we deem of interest to you.