THOMPSON HINE

SECURE ACT 2.0

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SECURE 2.0 Secures Enactment at the Last Minute

2022 Year-End Legislation Brings Numerous Retirement Plan Changes in 2023 and Beyond

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Introduction to SECURE 2.0

On December 29, 2022, President Biden signed the Consolidated Appropriations Act, 2023 (Funding Bill) before government funding was set to expire. Nestled in the 4,000+ page Funding Bill is the SECURE 2.0 Act of 2022 (SECURE 2.0).

- **SECURE 2.0 Purpose**: Congress determined that many Americans reach retirement age with little to no savings. Consequently, SECURE 2.0 seeks to (1) increase opportunities to participate in employer-sponsored retirement plans; (2) incentivize employers to sponsor retirement plans; (3) ease the regulatory burden of sponsoring retirement plans; and (4) better educate Americans about retirement plans and saving for retirement.
- **Effective Dates**: Each of SECURE 2.0's provisions has its own effective date. The effective dates range from the date of SECURE 2.0's enactment (December 29, 2022) to 2028 and beyond, with the bulk of the provisions taking effect in 2024.
- **Amendment Deadline**: Amendments for SECURE 2.0 generally must be made by the last day of the first plan year beginning on or after January 1, 2025 (i.e., December 31, 2025, for calendar year plans). The deadline for governmental plans and collectively bargained plans is the last day of the first plan year beginning on or after January 1, 2027 (i.e., December 31, 2027, for calendar year plans). These deadlines also generally apply to SECURE and CARES Act amendments due to a helpful provision in SECURE 2.0.

Many of SECURE 2.0's provisions solely apply either to defined contribution plans, such as 401(k) and 403(b) plans, (DC Plans) or defined benefit plans, such as traditional pension and cash balance plans (Pension Plans). There are also a handful of provisions that apply to both types of retirement plans. Brief summaries of select SECURE 2.0 provisions are set forth below.

Select Provisions Specific to Defined Contribution Plans (DC Plans)

Match for Student Loan Repayments

SECURE 2.0 permits employers to make matching contributions to a DC Plan on qualified student loan payments by treating such payments as elective deferrals or elective contributions, as applicable, for purposes of nondiscrimination testing and safe harbor rules. Plan sponsors can rely on an annual certification from a participant that eligible student loan payments have been made and are permitted to perform the actual deferral percentage (ADP) test separately on employees who receive matching contributions on qualified student loan payments.

Effective for plan years beginning on or after January 1, 2024.

Emergency Savings

- **Emergency Savings Accounts**: SECURE 2.0 permits employers to establish emergency savings accounts (ESAs) within a DC Plan to which non-highly compensated participants may separately contribute. Key terms of ESAs include:
  - participants must be able to take an ESA withdrawal at least monthly with the first four ESA withdrawals per year being free from additional fees;
  - the ESA balance is capped at $2,500 (subject to annual inflation adjustments) or a lesser amount selected by the plan sponsor, but cannot be subject to minimum contribution or balance requirements;
  - ESA contributions are treated as Roth contributions (and the employer generally is required to make matching contributions to a non-ESA account at the same rate that would otherwise apply to elective contributions, not to exceed the ESA balance maximum); and
  - participants may be automatically enrolled to contribute up to 3% of compensation to an ESA.

Effective for plan years beginning on or after January 1, 2024.

- **Emergency Expense Withdrawals**: SECURE 2.0 permits a participant to take a distribution of up to $1,000 (or if the participant's vested account is less than $2,000, the amount in excess of $1,000 in the participant's vested account) from the participant's DC Plan account to address unforeseen emergency expenses without being subject to the 10% additional tax that would otherwise apply to early withdrawals. Participants can repay an emergency distribution within three years and cannot take an additional emergency distribution during the corresponding three-year repayment period unless the emergency distribution is repaid.

Effective for distributions made on or after January 1, 2024.

Automatic Enrollment

- **Automatic Enrollment Required for New Plans**: SECURE 2.0 generally mandates that any newly adopted DC Plan include automatic enrollment provisions no later than January 1, 2025 (or, if later, the first day of the plan's 2025 plan year). Importantly, most plans adopted prior to December 29, 2022, are exempt from this requirement. There are also exceptions for certain small and new businesses, church plans, and governmental plans.

Effective for plan years beginning on or after January 1, 2025.

- **EPCRS Safe Harbor Correction Made Permanent**: The Employee Plans Compliance Resolution System (EPCRS) currently contains a temporary "safe harbor" correction provision that provides relief to DC Plans with automatic enrollment and escalation features by permitting correction of elective deferral errors that are corrected within 9½ months of the plan year following the plan year in which the error occurred at QNEC rates, provided certain notice requirements are met. As included in EPCRS, this temporary safe harbor would expire on December 31, 2023. SECURE 2.0 extends this safe harbor correction permanently.

Effective for any failures or corrections occurring on or after January 1, 2024.

Roth and Catch-Up Contributions

- **Roth Matching and Nonelective Contributions**: SECURE 2.0 provides that DC Plans may permit participants the option to elect to receive employer matching and nonelective contributions on a Roth after-tax basis.

Effective for any employer matching contribution or nonelective made after December 29, 2022.

- **Mandatory Roth Catch-Up Contributions**: Under current rules, a participant can make catch-up contributions on a pre-tax or Roth after-tax basis. SECURE 2.0 requires that a participant whose compensation exceeds $145,000 (indexed) for any plan year can only make catch-up contributions on a Roth after-tax basis.

Effective for taxable years beginning on or after January 1, 2024.

- **Increased Catch-Up Contribution Limit**: SECURE 2.0 increases the limit for catch-up contributions for participants ages 60-63 to be the greater of $10,000 and 150% of the general catch-up limit for the applicable calendar year. This increased limit will be adjusted for inflation annually beginning in 2026.

Effective for taxable years beginning on or after January 1, 2025.

Hardship Distributions

- **Hardship Self-Certification**: SECURE 2.0 expands the availability of self-certification for hardship distributions.

Effective for plan years beginning on or after December 29, 2022.

- **403(b) Plans**: SECURE 2.0 conforms the hardship distribution source eligibility provisions for 403(b) plans to match that of 401(k) plans to permit 403(b) plans to distribute QNECs, QMACs, and earnings.

Effective for plan years beginning on or after January 1, 2024.

Reduced Service Period for Long-Term Part-Time Employees

"SECURE 1.0" (prior retirement plan legislation passed in 2019) generally requires non-collectively bargained DC Plans to allow long-term part-time employees to participate for employee contribution purposes effective for plan years beginning on or after January 1, 2024, if they complete a minimum of 500 hours of service per year for three consecutive years. SECURE 2.0 reduces this requirement to 500 hours of service per year for two consecutive years (counting only service during and after 2023). Pre-2023 service is also disregarded for vesting purposes, and for purposes of compliance with the SECURE 1.0 version of this provision, pre-2021 service is disregarded for vesting purposes (this service was already disregarded for eligibility purposes under SECURE 1.0). In addition, SECURE 2.0 extends the long-term part-time employee requirement to 403(b) plans.

Effective for plan years beginning on or after January 1, 2025, except as otherwise noted where impact is retroactive.

Financial Incentives to Encourage Plan Participation

SECURE 2.0 alters the prohibition against conditioning any benefit (other than matching contributions) on whether an employee elects to participate in a DC Plan to allow employees to receive de minimis financial incentives to participate in the plan but only if plan assets are not used to pay the incentive. SECURE 2.0 does not offer a bright line to determine when an incentive is nominal; however, something along the lines of a "low-dollar gift card" should now be permitted under this provision.

Effective for plan years beginning on or after December 29, 2022.

Permanent Disaster Relief Rules

SECURE 2.0 provides special rules permitting distributions of up to $22,000 to participants who reside within an area designated within a qualified federally declared disaster area or who suffered an economic loss because of the disaster that are exempt from the 10% additional tax that would otherwise apply to early withdrawals. Participants can include a disaster distribution in income over a three-year period and can repay the distribution within three years after the date the distribution occurred. Loans taken by participants from their DC Plan accounts relating to a disaster can have more generous terms than otherwise permitted – specifically, participants can borrow higher amounts and have longer periods to repay the loan.

Effective for any disaster declared on or after January 26, 2021.

Penalty-Free Early Plan Distributions

In addition to emergency withdrawals and disaster distributions, SECURE 2.0 adds several other exceptions to the 10% additional tax that generally applies to early distributions:

- Participants who are terminally ill (effective for distributions after December 29, 2022)
- Participants who are victims of domestic abuse (effective for distributions on or after January 1, 2024)
- For the payment of long-term care insurance premiums (effective for distributions after December 29, 2025)

Required Minimum Distributions

SECURE 2.0 makes a series of changes to the required minimum distribution (RMD) rules, with most taking effect in 2023. The changes include:

- increasing the age at which the RMD rules apply from 72 to 73 (January 1, 2023) and then to 75 a decade later (January 1, 2033);
- reducing the penalty if an individual fails to take any RMD, including an extra reduction if the individual timely corrects the failure;
- exempting Roth contributions in an individual’s DC Plan account from the RMD rules prior to the participant’s death;
- allowing a DC Plan participant’s surviving spouse-beneficiary to elect to be treated as the participant for purposes of the RMD rules;
- mitigating the RMD rules’ negative effects on “qualifying longevity annuity contracts” and adding provisions to encourage the sale of such contracts; and
- addressing how the RMD rules can deter the use of annuities in connection with a retirement account.

Reduced Notice Requirements for Non-Participants

SECURE 2.0 simplifies a DC Plan’s obligation with respect to eligible employees who choose not to participate in the DC Plan to only require providing (1) an annual notice of the individual’s eligibility to participant in the DC Plan and (2) any document requested by the individual that the individual would have been entitled to receive in the absence of SECURE 2.0’s reduced notice requirements. This simplification applies only with respect to those non-participating eligible employees who, in connection with their initial eligibility to participate, received all notices required to be furnished at that time, including the plan’s summary plan description.

Effective for plan years beginning on or after January 1, 2023.

Saver’s Matching Contribution

Currently, the Internal Revenue Code of 1986, as amended (Code), assists lower-income taxpayers by offering a tax credit, called the Saver’s Credit, if they make contributions to a retirement plan. SECURE 2.0 provides that the federal government will make a matching contribution to a DC Plan selected by the taxpayer that will accept the contribution in lieu of providing a tax credit. This “Saver’s Match” is treated as a pretax contribution to the receiving DC Plan. The maximum Saver’s Match is $2,000 per year and a taxpayer does not qualify if their income exceeds $35,500 if filing as single and $53,250 if filing as head of household. Single taxpayers with income less than $35,500, but more than $20,500, or head of household taxpayers with income less than $53,250, but more than $30,750, are eligible for a reduced Saver’s Match amount.

Effective for taxable years beginning on or after January 1, 2027.

Select Provisions Specific to Defined Benefit Plans (Pension Plans)

More Detailed Annual Funding Notices

SECURE 2.0 expands the information required to be included in annual funding notices to include (1) financial information with respect to the two plan years prior to the applicable plan year, (2) breakdowns of the Pension Plan’s participant population, and (3) the Pension Plan’s average return on assets.

Effective for plan years beginning on or after January 1, 2024.

Information for Lump Sum Offers

SECURE 2.0 mandates that participants receive specific information in connection with a lump sum payout, including (1) the methodology for calculating the lump sum amount, (2) the other benefit options offered by the Pension Plan, (3) the consequences of selecting the lump sum payment (e.g., loss of some federal protections), and (4) general tax rules applicable to the lump sum distribution. SECURE 2.0 directs the U.S. Department of Labor (DOL) to create a model notice.

Effective no earlier than the later of December 29, 2023, or the date on which DOL issues regulations, and no later than one year following the issuance of such regulations.

Variable Rate PBGC Premiums Frozen

SECURE 2.0 removes inflation-indexing from variable rate PBGC premiums and locks in the 2023 rate announced by the PBGC prior to SECURE 2.0's passage, which is generally $52 per every $1,000 of unfunded plan liabilities.

Effective December 29, 2022.

Overfunded Plans and Retiree Health and Life Insurance Benefits

Currently, if a Pension Plan is overfunded, certain Pension Plan assets can be used for retiree health and life insurance benefits. SECURE 2.0 extends the expiration of this provision from 2025 until 2032.

Effective with respect to any transfer of surplus Pension Plan assets occurring after December 29, 2022.

Fix for Market Rate of Return Cash Balance Plans

SECURE 2.0 includes a change to the highly complex backloading rules to overturn prior interpretations of the rules that have disallowed more favorable treatment of longer-service workers under a cash balance plan that provides interest credits using the rate of return on plan assets or other market variable interest crediting rate. This change would permit employers to provide cash balance benefits that include a permissible amount of backloading (similar to what is allowed under all other Pension Plans) while essentially avoiding most investment return risk to which employers are typically exposed under a Pension Plan.

Effective for plan years beginning after December 29, 2022.

Select Provisions Applicable to Both DC Plans and Pension Plans

Increased Ability to Self-Correct Plan Failures

SECURE 2.0 codifies provisions of EPCRS:

- The ability to self-correct is expanded to generally encompass all "eligible inadvertent failure[s]," which generally are failures that occur even though the plan sponsor has preestablished "practices and procedures" designed to facilitate compliance with the Code. Self-correction is not available if:
  - the IRS identifies the failure before the plan sponsor does;
  - the failure is not corrected within a reasonable time period after discovery;
  - the failure is "egregious";
  - the failure relates to the diversion or misuse of plan assets; or
  - the failure relates to an "abusive tax avoidance transaction."
- Self-corrections for failures relating to participant loans from a DC Plan require DOL to consider any corresponding fiduciary duty breach as corrected under DOL's voluntary fiduciary correction program. DOL is authorized to implement reporting requirements if a plan sponsor intends to use EPCRS self-correction for a breach of fiduciary duty.
- As directed by SECURE 2.0, the IRS will issue guidance to provide specific correction methods for certain failures and general correction principles for failures without a specific correction method.

Effective December 29, 2022.

Government deadline: The IRS must provide updated EPCRS guidance by December 29, 2024.

Flexibility in Recouping Overpayments

SECURE 2.0 grants plan fiduciaries more latitude in determining whether a plan should seek recoupment of overpayments from plan participants, including the ability to determine not to recover an overpayment. Fiduciaries are still permitted to seek recoupment, but SECURE 2.0 applies restrictions to recoupment efforts (e.g., inability to seek interest on an overpayment or costs related to recovery efforts, extremely limited ability to use a collection agency, no recoupment if the first overpayment occurred more than three years before notice of the overpayment is provided to the participant in the absence of the participant's fraud or misrepresentation). SECURE 2.0 also authorizes DOL to issue regulations further restricting overpayment recoupment measures.

Effective December 29, 2022.

Increased Mandatory Cash-Out Limit

SECURE 2.0 increases the mandatory cash-out limit from $5,000 to $7,000, meaning that employers may transfer former employees' retirement accounts from the employer-sponsored plan into an IRA without the employee's consent if the account balance is between $1,000 and $7,000.

Effective for any distribution made after December 31, 2023.

Extended Deadline for Discretionary Plan Amendments

The deadline for certain discretionary amendments is extended to the employer's tax return filing deadline (including extensions) with respect to the tax year in which the amendment takes effect if such amendment provides increased benefits to participants.

Effective for plan years beginning on or after January 1, 2024.

Retirement Savings Lost and Found Database

Frequently, employer-sponsored retirement plans are unable to pay benefits to participants for whom the plan no longer has current contact information (e.g., if the participant moved after employment termination and did not provide updated contact information to the plan). Likewise, participants may be unable to locate the plan sponsor to receive their benefits (e.g., if the plan sponsor was acquired and the plan under which benefits accrued is merged into another plan with an unfamiliar name). SECURE 2.0 directs the DOL to create a national "lost and found" database that individuals can use to find contact information for the plan applicable to the individual's benefit.

- SECURE 2.0 creates a database intended to assist employees looking for former employers. The database is not intended to assist employers in locating missing participants.
- Retirement plans will have a reporting obligation to DOL to facilitate creation and maintenance of the database. DOL regulations will specify the time, manner, and form of the reporting.

Effective for plan years beginning on or after January 1, 2025, for plan reporting requirements.

Government deadline: DOL must have the database established by December 29, 2024.

Paper Benefit Statements

The Employee Retirement Income Security Act of 1974, as amended, imposes a requirement to provide plan participants with written benefit statements and SECURE 2.0 makes two changes:

- DC Plans must provide one paper benefit statement per year and Pension Plans must provide one paper benefit statement every three years. SECURE 2.0 permits an exception to this requirement under certain circumstances (e.g., the employee opts *in* to electronic delivery).
- As directed by SECURE 2.0, DOL will revise the electronic delivery regulations to provide participant protections (e.g., participants must be alerted to the ability to request paper statements).

Effective for plan years beginning on or after January 1, 2026.

We Can Help

Our employee benefits attorneys have supported employers through decades of legislative and regulatory evolution of the legal rules applicable to employer-sponsored retirement plans – and we will continue to do so for SECURE 2.0 and beyond.

We are committed to understanding your business and benefit plans so we can provide individualized advice with respect to SECURE 2.0's provisions.

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FOR MORE INFORMATION

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