STRADLEY RONON

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Key Takeaways of the SECURE 2.0 Act

On Dec. 29, 2022, President Biden signed into law H.R. 2617, the "Consolidated Appropriations Act, 2023." The legislation contains significant retirement provisions in what is called the "SECURE 2.0 Act of 2022." SECURE 2.0 expands upon 2019's Setting Every Community Up for Retirement Enhancement Act (SECURE Act) and adds a number of new concepts.

SECURE 2.0 contains dozens of provisions that are aimed at encouraging retirement savings. Certain provisions are immediately applicable, and others become applicable in 2024 and beyond. We will issue more detailed analyses of SECURE 2.0 in a series of releases in the coming weeks.

For now, some key takeaways for immediate consideration are:

Mandatory "Rothification" of Certain Catch-Up Contributions

- Effective for tax years beginning after 2023, catch-up contributions to 401(k), 403(b), and governmental 457(b) plans by employees whose wages exceed $145,000 (as indexed) must be made on a Roth basis. This is mandatory for any plan that makes catch-up contributions available. This provision does not apply to SIMPLE IRAs or to SEP plans.

Optional Roth Employer Matching and Nonelective Contributions

- Effective for contributions made after the date of enactment of SECURE 2.0, plans may offer employees the ability to elect for some or all of the matching or nonelective employer contributions made to them under the plan to be characterized as Roth contributions, provided that the contributions are fully vested at the time they are made.

Required Automatic Enrollment and Automatic Escalation Provisions for New Plans

- 401(k) and 403(b) plans established after the date of enactment of SECURE 2.0 must, for plan years beginning after Dec. 31, 2024, contain an enrollment provision that automatically enrolls employees into the plan and an escalation provision that automatically escalates participants' deferral percentages. These requirements are subject to the employee's right to opt out of both automatic enrollment and automatic escalation.

- Specifically, employees must be automatically enrolled at a contribution percentage of at least 3%, but not more than 10% and their contribution percentage must automatically increase by 1% on the first day of each plan year following the completion of a year of service until the contribution is at least 10%, but no more than 15%.

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- Employers should understand the increased costs that will arise as a result of the automatic enrollments if their plans include matching contributions.
- Governmental plans, church plans and plans sponsored by new and small businesses are excepted from these general requirements.

Employer Match for Student Loan Payments Permitted

- Effective for plan years beginning after 2023, plan sponsors of 401(k) plans, 403(b) plans, SIMPLE IRA plans, and governmental 457(b) plans will be allowed to make matching retirement contributions for certain "qualified student loan payments" made by the employees for higher education expenses.
- Employers may rely on an employee's annual certification of the amount of their "qualified student loan payments."
- Essentially, this means that young employees who may not be able to afford to participate in the plan because of high student loan payments may nevertheless receive the matching contribution and begin to save for retirement.
- Employees' "qualified student loan payments" are not elective deferrals or contributions to a plan, but a plan may treat the payments as such for purposes of certain safe harbor requirements. Additionally, employers' matching contributions are treated as regular matching contributions for discrimination testing purposes. Further, a plan may treat all employees who receive employer matches for student loan payments as a separate group for purposes of actual deferral percentage testing in any one plan year.

Automatic Portability of Default IRAs Permitted

- Effective 12 months after the enactment of Secure 2.0, default IRA service providers will be allowed to make default IRAs portable. This would allow, after notice and opportunity to opt out, the transfer of the amounts in a default IRA account for an individual (usually placed there because the individual is entitled to a distribution of a small dollar cash out from a qualified plan or a distribution upon a qualified plan termination) to a new employer's plan when the employee changes jobs. These automatic portability services are aimed at limiting "leakage" from retirement accounts. SECURE 2.0 creates a new prohibited transaction exemption covering the receipt of fees and compensation by an automatic portability service provider in connection with automatic portability transactions. The Department of Labor is directed to issue guidance and studies in connection with the exemption.

Limits, Indexing and Penalties Changes

- *IRA Catch-Up Contributions Indexed:* Effective for tax years beginning after Dec. 31, 2023, IRA catch-up contributions will be indexed in $100 increments in the same manner as the indexing for regular IRA contributions.
- *Increase in Catch-Up Contributions for Ages 60-63:* Effective for tax years beginning after Dec. 31, 2024, catch-up contributions limits to non-SIMPLE plans will be increased to the greater of $10,000 or 150% of the "regular" inflation-adjusted limit for 2024 for employees who reach ages 60, 61, 62, or 63 during the year. For SIMPLE plans, the catch-up limit will be increased to the greater of $5,000 or 150% of the "regular" inflation-adjusted limit for 2025 for employees who reach ages 60, 61, 62, or 63 during the year.
- *Increase in Small Benefit Cashout Limit:* Effective for distributions after Dec. 31, 2023, absent a participant's election otherwise, a retirement plan benefit of $7,000 or less (previously $5,000 or less) may be automatically cashed out and transferred to an IRA with a default IRA provider.

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- *Penalties and Excise Taxes Reduced:* Effective for tax years after the date of enactment:
    - Corrective distributions and corresponding earnings from an IRA are exempted from the 10% early withdrawal penalty.
    - The excise tax for failure to take RMDs is reduced from 50% of the shortfall to 25%. The excise tax is further reduced to 10% if the individual corrects the shortfall during a two-year correction window.

PEP and MEP Provisions

- *Contribution Collection for PEPs:* Beginning in 2023, PEPs are allowed to designate any named fiduciary (other than a participating employer) as the entity responsible for contribution collections. Such designated fiduciary must implement written contribution collection procedures that are reasonable, diligent, and systematic.
- *Multiple Employer 403(b) Plans:* Starting in 2023, certain 403(b) plans will be able to operate as MEPs and PEPs and will be subject to registration and reporting requirements. The Department of Treasury is directed to issue regulations providing relief from the “one bad apple” rule for 403(b)s and to issue model plan language.

Other Highlights

Additional Nonelective Contribution to SIMPLE Plans: Effective for tax years beginning after Dec. 31, 2023, an employer may make additional contributions to each employee of a SIMPLE plan in a uniform manner, provided that the contribution does not exceed the lesser of 10% of compensation or $5,000 (indexed for inflation).

Required Minimum Distribution (RMD) Age Increase: The age for commencing required minimum retirement plan distributions increases to age 73 starting on Jan. 1, 2023, and then further increases to age 75 starting on Jan. 1, 2033.

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