

SECURE 2.0 MAKES NUMEROUS CHANGES TO RETIREMENT PLAN RULES

Hodgson Russ Employee Benefits Alert
January 12, 2023

Building on the changes made by the Setting Every Community Up for Retirement Enhancement Act (“SECURE Act”) enacted in 2019, the SECURE 2.0 Act of 2022 (“SECURE 2.0”), which was included in the Consolidated Appropriations Act, 2023 and signed into law on December 29, 2022, enacts dozens of new rules regulating retirement plans. SECURE 2.0, in broad terms, enacts changes that are intended to expand retirement plan coverage and increase retirement savings, preserve income, and simplify and clarify certain retirement plan rules.

This alert highlights many of the more significant SECURE 2.0 rule changes that will be of interest to sponsors of virtually all types of retirement plans – it does not attempt to describe each and every rule change. Additional SECURE 2.0 rule changes, as well as any new guidance issued by the IRS regarding the SECURE 2.0 rule changes, will be addressed in future alerts.

Many SECURE 2.0 changes will not be effective until after 2023 or later. Nonetheless, employers and plan sponsors should begin to familiarize themselves with the rule changes, and plan for the implementation of plan changes that must be made as well as optional plan changes they wish to make to their existing plans.

Expanding Savings Opportunities

Expanded Automatic Enrollment After 2024. New 401(k) and 403(b) plans will be required to automatically enroll employees (unless the employee opts out) when they become eligible for the plan. Employees must be automatically enrolled at a contribution percentage of at least 3%, but not more than 10%. Those employees also will be subject to automatic escalation provisions that automatically escalates their deferral percentage (unless the employee opts out) by 1% each year until the deferral percentage reaches at least 10%, but not more than 15%. Exceptions to these automatic enrollment/escalation rules are available for small businesses (10 or fewer employees), new businesses (in business for fewer than three years), church plans, and governmental plans. The new automatic enrollment/escalation rules apply to any 401(k) or 403(b) plan established after SECURE 2.0’s date of enactment, and will only apply for plan years beginning after December 31, 2024.

Attorneys

Peter Bradley
Michael Flanagan
Richard Kaiser
Ryan Murphy
Amy Walters

Practices & Industries

Employee Benefits

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Long-Term Part-Time Employee Eligibility – Modified Coverage Rules. The original SECURE Act requires 401(k) plans to allow employees who have at least 500 hours of service in each of *three* consecutive years to make elective deferrals (without requiring the plan to offer matching or other employer contributions). Effective for plan years beginning after December 31, 2024, SECURE 2.0 shortens the eligibility requirement from three years to two years. SECURE 2.0 also provides that 403(b) plans covered by ERISA will be subject to those same long-term part-time coverage rules.

Matching Contributions on Student Loan Payments. SECURE 2.0 permits 401(k), 403(b), SIMPLE IRA and nongovernmental 457(b) plan sponsors to make matching contributions on behalf of employees who make “qualified student loan payments” for higher education expenses (instead of making retirement plan contributions) and to have these matching contributions treated as regular matching contributions for discrimination testing purposes. This new rule is effective for plan years beginning after 2023.

“Starter K” Plans for Employers Without Any Retirement Plan. SECURE 2.0 permits employers with no retirement plan to establish a starter 401(k) deferral-only plan (or safe harbor 403(b) plan). Under such a plan, an employee would be enrolled automatically at a qualified deferral percentage of not less than 3% and not more than 15% of pay (unless the employee opts out), with contributions capped at \$6,000 (indexed for inflation) and a right to make annual additional \$1,000 (indexed for inflation) catch-up contributions upon attainment of age 50. The starter deferral-only plan rules are effective for plan years after December 31, 2023.

New Savings Incentives

Small Employer Tax Credits - 100% Tax Credit for the Start-Up of New Retirement Plans Among Small Businesses. Previously, employers with no more than 100 employees who received at least \$5,000 of compensation from the employer were entitled to claim a tax credit, in each of the first three years of a newly established plan, equal to 50% of the eligible startup costs associated with establishing and administering a new SEP, SIMPLE IRA or qualified plan, up to \$5,000 per year. SECURE 2.0 increases the 50% to 100% for employers with no more than 50 employees and also establishes a new tax credit for contributions made to a newly established retirement plan, other than a defined benefit plan. The new credit is a specified percentage of the contribution made by the employer, up to a per-employee cap of \$1,000. The specified percentage begins at 100% for the first two years the plan is established and then decreases by 25% in each subsequent year. The full credit is available to employers with no more than 50 employees and gradually phases out for employers with 51 to 100 employees. The new small employer tax credits are effective for taxable years beginning after December 31, 2022.

Saver’s Credit - Replaces the Current Saver’s Credit with a Matching Type of Contribution. Current law provides for a nonrefundable tax credit for certain individuals making contributions to an IRA or workplace retirement plan. Effective for taxable years beginning after December 31, 2026, certain lower-income retirement savers will be eligible for a government-provided matching contribution to their IRA or retirement plan. The matching contribution will generally equal 50% of the individual’s contributions, capped at \$2,000 per individual. The match gradually phases out based on income levels. Given the administrative complexity associated with the new saver’s credit, the delayed effective date is likely merited, though if the new saver’s credit proves to be too administratively burdensome, it appears that retirement plans would not be required to accept any government-provided matching contributions.

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RMD Rule Changes

Further Increasing the Required Beginning Date for RMDs from Age 72 to 75. Until the SECURE Act was enacted in 2019, the age at which individuals had to begin taking required minimum distributions (“RMDs”) from their retirement plans generally was 70½. The SECURE Act raised this age to 72 for people who reached that age on or after January 1, 2020. Now, this age is increasing again. SECURE 2.0 raises the required beginning date to 73 years old for individuals who turn 72 after December 31, 2022 and 73 before January 1, 2033. Additionally, the required beginning date will increase to 75 years old for individuals who reach the age of 74 after December 31, 2032.

Reduced Penalty for Failure to Take RMDs. Prior to SECURE 2.0, if a person required to take a RMD did not take the RMD or did not distribute the full RMD amount, that person would be subject to an excise tax of 50% of the amount by which the RMD exceeds the amount actually distributed. SECURE 2.0 reduces the RMD shortfall excise tax to 25%. In addition, the excise tax is reduced to 10% if the person corrects the shortfall within 2 years of the failure. These changes apply for tax years 2023 and thereafter.

Pre-Death RMD Exemption Extended to Roth Accounts in Employer Plans. Under prior law, only Roth IRAs were exempt from the pre-death RMD rules. Roth accounts in employer plans, such as a 401(k), were subject to the RMD rules when the account owner reached his or her required beginning date. SECURE 2.0 extends the pre-death RMD exemption to Roth accounts in employer plans, so that they are treated the same as Roth IRAs when it comes to pre-death RMDs. This change applies for the 2024 tax year and thereafter - RMDs are still required from employer Roth accounts for 2022 and 2023.

Catch-up Contribution Changes

Higher Catch-Up Contribution for Individuals Age 60-63. Participants in certain qualified retirement plans (i.e., 401(k), 403(b), and 457 plans) are subject to annual dollar limits on elective deferrals. However, participants who are at least 50 years old may contribute additional amounts each year. For participants age 50 and older, the 2023 catch-up contribution limit is \$7,500. SECURE 2.0 raises catch-up contribution limits for some participants and requires some catch-up contributions to be Roth contributions (i.e., after-tax contributions). Effective for 2025, the catch-up contribution limit for participants who are ages 60 through 63 will be raised to the greater of \$10,000 (indexed for inflation), or an amount equal to 150% of the standard catch-up amount.

Mandatory Roth Treatment for Certain Catch-Up Contributions. Effective for 2024, SECURE 2.0 requires all catch-up contributions for participants earning more than \$145,000 during the previous year to be deposited into a Roth account.

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403(b) Plan MEPs and PEPs

Under the original SECURE Act, pooled employer plans (PEPs) were introduced as a new type of retirement plan that allowed unrelated employers to participate in a single 401(k) retirement plan. This single employer plan would be sponsored by a “Pooled Plan Provider” and could ease administrative burdens (and expenses) by bundling several plan service providers, such as record-keepers, independent fiduciaries, and investment advisors. Multiple employer plans (MEPs) are similar to PEPs, but allowed for related businesses to join together to participate in a single retirement plan. Effective January 1, 2023, SECURE 2.0 expands these arrangements to also include 403(b) plans.

In-Service Distributions

Emergency Withdrawals from Eligible Retirement Plan. SECURE 2.0 permits one distribution per calendar year up to \$1,000 from an applicable eligible retirement plan in the event of an “unforeseeable or immediate financial needs relating to personal or family emergency expenses.” Such distributions are not subject to the 10% tax under Code Section 72(t) on early distributions, and may be repaid within 3 years. However, no further emergency distributions are permitted during the 3-year period after the distribution unless, either (1) the distribution is fully repaid, or (ii) the participant’s subsequent deferrals or contributions to the plan exceed the amount of the distribution. The provision applies to an “applicable eligible retirement plan” other than a defined benefit plan, including IRAs, tax qualified retirement plans (e.g., profit sharing and 401(k) plans), 403(a) plans (e.g., qualified annuity contracts), 403(b) plans, and government-sponsored 457(b) plans, but not a 457(b) plan sponsored by a nongovernmental organization. The adoption of this provision is optional, and effective for distributions made on or after December 31, 2023.

Pension-Linked Emergency Savings Accounts. SECURE 2.0 amends ERISA to add a new kind of short-term savings account that plan sponsors may offer in tandem with a traditional defined contribution “individual account” retirement plan (an “Emergency Savings Account”). Separate recordkeeping is required for the Emergency Savings Account and the participant’s other account(s) under the plan. The Emergency Savings Account is funded solely with participant-made Roth contributions, provided that plan sponsors may choose to automatically enroll participants at a contribution rate of up to 3% of compensation. Contributions to the Emergency Savings Account are limited to a maximum of \$2,500 (indexed), or a lesser amount set by the plan sponsor. Highly compensated employees are not eligible to make contributions to an Emergency Savings Account, but may take withdrawals from such accounts accrued before they attained HCE status.

Participants are permitted to take one withdrawal per month from the Emergency Savings Account, and the plan may not impose fees on the first four withdrawals in a plan year. Such distributions are not subject to the 10% tax under Code Section 72(t) on early distributions. The plan sponsor may choose to have the Emergency Savings Accounts invested in cash, interest-bearing deposit accounts, or investment products designed to preserve principal and provide a reasonable rate of return. Notably, contributions to an Emergency Savings Account are treated as if they were elective deferrals made to the non-Emergency portion of the plan and are matched in accordance with the plan’s formula up to the maximum amount of Emergency Savings Account contributions permitted under the plan. The implementation of segregated account recordkeeping, while requiring integration of the accounts for purposes of allocating matching contributions may create administrative challenges. The Emergency Savings Account provision

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expressly pre-empts state anti-garnishment laws. The adoption of this provision is optional, and effective for plan years beginning after December 31, 2023.

Repayment of Qualified Birth or Adoption Distribution Limited to Three Years. The original SECURE Act did not limit the time period over which a Qualified Birth or Adoption Distribution (“QBAD”) may be repaid to an eligible retirement plan to qualify as a rollover contribution. SECURE 2.0 provides that QBADs are required to be recontributed within three years of distribution to qualify as a rollover contribution. The limitation is effective for distributions after the date of enactment. For prior distributions, the repayment period ends December 31, 2025.

Employer May Rely Upon Employee Certification that Deemed Hardship Conditions Are Satisfied. Prior to SECURE 2.0, for 401(k) and 403(b) plans providing for hardship distributions on account of an immediate and heavy financial need, the plan administrator was permitted to rely upon the written representation of the participant that s/he lacked sufficient cash or other liquid assets reasonably available to satisfy the need, so long as the plan administrator did not have actual knowledge to the contrary. SECURE 2.0 now allows the plan administrator to rely, in addition, upon an employee’s certification that they have experienced an event of a type that is a deemed hardship under the applicable regulations. Sponsors of governmental 457(b) plans are also permitted to rely upon a participant’s certification that an event constituting an unforeseeable emergency has occurred, and that the participant has no alternative means reasonably available to satisfy the emergency need. This provision is applicable for plan years beginning after the date of enactment.

Penalty Free Withdrawals In Cases of Domestic Abuse. SECURE 2.0 permits distributions to a domestic abuse victim, in an amount not to exceed the lesser of \$10,000 (indexed) or 50% of the value of the participant’s vested account under the plan. The distributions may be made during the one year period beginning on any date the individual is a victim of domestic abuse by a spouse or domestic partner. Domestic abuse is broadly defined to include physical, sexual, emotional and economic abuse. Such distributions are not subject to the 10% tax under Code Section 72(t) on early distributions, and may be repaid using rules similar to those applicable to QBADs, including the requirement that repayment occurs within 3 years. The provision applies to an “applicable eligible retirement plan” other than a defined benefit plan and plans subject to Code Sections 401(a)(11) and 417, including IRAs, tax qualified retirement plans (e.g., profit sharing and 401(k) plans), 403(a) plans (e.g., qualified annuity contracts), 403(b) plans, and government-sponsored 457(b) plans, but not a 457(b) plan sponsored by a nongovernmental organization. The plan administrator may rely upon the certification of the participant that the amount requested constitutes an eligible distribution to a domestic abuse victim. The adoption of this provision is optional and effective for distributions after December 31, 2023.

Distributions of Small Account Balances

Mandatory Cash-Out/Automatic Rollover Thresholds Increase from \$5,000 to \$7,000. Under current mandatory cash-out and automatic rollover rules, a retirement plan benefit of \$5,000 or less generally may be automatically cashed out by the plan and transferred to a designated individual retirement plan unless the participant elects otherwise. For a retirement plan benefit of \$1,000 or less, a mandatory cash-out may simply be distributed in cash. Effective for distributions after December 31, 2023, SECURE 2.0 increases the \$5,000 mandatory cash-out/automatic rollover threshold to \$7,000.

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Prohibited Transaction Exemption for Certain Automatic Portability Transactions. SECURE 2.0 creates a prohibited transaction exemption for retirement plan service providers that are paid to provide services in connection with automatic portability transactions. Subject to certain conditions and the timely delivery of prescribed notices, an “automatic portability transaction” generally is a transfer of an automatic rollover amount from the default IRA established to hold an individual’s automatic rollover into an employer-provided defined contribution plan that covers the individual, provided the individual does not opt out of the transfer. These automatic portability provisions facilitate an automatic transfer of an automatic rollover amount into the retirement plan of the individual’s new employer without the individual’s consent. The new exemption is effective for transactions occurring on or after the date which is 12 months after the date of enactment.

Plan Corrections

Expansion of Self-Correction (Inadvertent Violations) under EPCRS. The IRS maintains its Employee Plans Compliance Resolution System (“EPCRS”) under which plan errors can be corrected. Under EPCRS, certain errors must generally be corrected within three years. In general, SECURE 2.0 now provides that any inadvertent failure to comply with the plan qualification rules will be eligible to be self-corrected at any time. The expansion of self-correction under the IRS’s EPCRS correction program is effective immediately.

Safe harbor for Corrections of Employee Elective Deferrals Failures. The IRS’s EPCRS correction program currently allows certain automatic enrollment and automatic escalation errors to be corrected without the employer being required to make a corrective contribution for any missed elective deferrals attributable to the error, though a corrective contribution for any employer matching contribution may still be required. The relevant provisions in EPCRS were scheduled to sunset after December 31, 2023. SECURE 2.0 generally codifies the existing provisions in EPCRS and is effective with respect to errors after December 31, 2023 (i.e., when the relevant provisions in EPCRS were scheduled to sunset).

Recovery of Plan Overpayments. SECURE 2.0 provides that plan fiduciaries will not be considered to have breached their fiduciary duties merely because they determine not to seek recovery of an inadvertent overpayment from a plan. If the fiduciary does seek recovery of any inadvertent overpayment from a participant or beneficiary, SECURE 2.0 places several conditions on the fiduciary’s ability to do so, including but not limited to not charging interest or lost earnings on the overpayment and not seeking to recover overpayments made to a participant from the participant’s beneficiary. However, these safeguards do not apply where the participant or beneficiary was responsible for the overpayment (e.g., through a misrepresentation in requesting a hardship distribution) or the participant or beneficiary otherwise knew the benefit payment was materially in excess of the correct amount. The overpayment provisions of SECURE 2.0 are effective immediately.

Missing Participants

Establishment of a Retirement Savings Lost and Found. SECURE 2.0 directs the DOL within 2 years to create an online, searchable database of information on lost, missing or non-responsive participants with accrued benefits in defined benefit or defined contribution retirement plans subject to ERISA’s vesting rules. The database will include the latest contact information for plan administrators to assist participants in making claims for benefits.

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Plan Administration

Requirement to Provide Paper Statements in Certain Cases. ERISA requires plan administrators to furnish participants with statements describing the person's benefit under the plan. For individual account plans, a benefit statement must be provided at least once every calendar quarter. For defined benefit plans, this statement must be provided at least once every 3 years. DOL regulations provide safe-harbors permitting electronic disclosure of these notices in the following situations:

1. The participant has work-related computer access;
2. The participant does not have work-related computer access, but consents to receiving electronic notices;
3. The plan administrator posts the notice on an internet website and furnishes a notice of internet availability to participants; and
4. The plan administrator delivers the notice to an email address provided by the participant.

SECURE 2.0 amends these rules by requiring plan sponsors to provide at least 1 paper benefit statement annually for defined contribution plans and at least 1 paper statement every 3 years for defined benefit plans. This change is effective for plan years beginning after December 31, 2025.

Consolidated Defined Contribution Plan Notices. Within 2 years, the DOL and Treasury are required to adopt regulations that will permit, but not require, defined contribution plans to consolidate certain automatic enrollment related notices.

Defined Benefit Annual Funding Notices. SECURE 2.0 amends existing defined benefit plan notices to require additional funding information be disclosed. The additions include information regarding the average return on assets for the plan year, and, for single employer plans, a statement as to whether the plan's funded status for the plan year to which the notice relates and for the two preceding plan years, is at least 100%, and if not, the actual percentage. The aim is to identify defined benefit pension plan funding issues more clearly on a plan's annual funding notice. This section is effective for plan years beginning after December 31, 2023.

Development and Release of the Sample Forms for Direct Rollovers/Trustee-to-Trustee Transfers. SECURE 2.0 directs the Treasury to simplify and standardize the rollover process by issuing sample forms for direct rollovers and trustee-to-trustee transfers that may be used by both the incoming and outgoing retirement plan or IRA. Development and release of the sample forms must be completed no later than January 1, 2025.

Changes to Family Attribution Rules. When determining whether two or more businesses must be aggregated for certain non-discrimination tests, ownership by family members may be attributed to other family members. SECURE 2.0 modifies these attribution rules by disregarding community property laws and changing the attribution of stock between parents and minor children. The modifications are effective for plan years beginning after December 31, 2023.

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Plan amendments required by SECURE 2.0 must be made on or before the last day of the first plan year beginning on or after January 1, 2025 (2027 in the case of governmental plans) as long as the plan operates in accordance with such amendments as of the effective date. This new amendment deadline also applies to amendments required under the SECURE Act, CARES Act, and Taxpayer Certainty and Disaster Relief Act of 2020.

If you have any questions regarding how this legislation may impact your plan, please contact any member of our [Employee Benefits Practice](#).