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The SECURE Act 2.0: What's In It For You?

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On December 29, 2022, President Biden signed into law the Omnibus Appropriation Act, 2023, which includes the SECURE 2.0 Act of 2022 (the "SECURE Act 2.0"). The Setting Every Community Up for Retirement Act of 2019 (the "original SECURE Act") included a number of legislative changes designed to encourage retirement savings and expand employee participation in retirement plans. The SECURE Act 2.0 again modifies the Internal Revenue Code (the "Code") and the Employee Retirement Income Security Act of 1974 to further these objectives and to address some new areas. This *Legal Update* highlights some key changes under the SECURE Act 2.0. Please note that implementing these changes often will require plan amendments.

Changes Effective Beginning in 2023

Required Minimum Distribution Age. The original SECURE Act increased the required minimum distribution ("RMD") age from 70-1/2 to 72 for those reaching 70-1/2 after 2019. The SECURE Act 2.0 again increases the RMD age as follows:

- The RMD age is 73 for individuals who reach age 72 after December 31, 2022 and age 73 before January 1, 2033; and
- The RMD age is 75 for those who reach age 74 on or after December 31, 2032.

Note: A technical correction likely will be needed for this change because an individual could both turn age 73 before January 1, 2033 and age 74 after December 31, 2032.

Missed RMD Excise Tax Reduction. Previously, an individual who failed to take their RMD from a retirement plan timely would be subject to an excise tax of 50% of the RMD amount that should have been distributed. The individual who should have received the RMD can request a waiver of this penalty if the failure to take the RMD was due to a reasonable error and the individual was taking reasonable steps to remedy the shortfall.

Effective beginning in 2023, the excise tax is reduced to 25%. In addition, if the individual receives all of their past-due RMDs and files a tax return paying the tax within two years after the year of the missed RMD **and** before receiving notice from the Internal Revenue Service ("IRS") of assessment

of the RMD excise tax, the excise tax is further reduced to 10% of the missed RMD. A question now arises as to whether the lower tax on missed RMDs will make it less likely that the IRS will grant waivers of the tax.

Hardship Withdrawals. In a change that should simplify the administration of hardship withdrawals significantly, an employer may rely on an employee's certification both as to the occurrence of a hardship event and as to the amount needed to address the hardship. Previously, the employer could rely only on the employee's certification that they did not have sufficient other liquid assets to satisfy the hardship.

De Minimis Incentives for Making Elective Deferrals. Under current law, an employer cannot provide a benefit, other than matching contributions, that is contingent upon an employee making elective deferrals to a 401(k) plan. Beginning with the 2023 plan year, an employer now may provide additional de minimis financial incentives, such as low-dollar gift cards, to encourage employees to enroll to make elective deferrals.

Employer Roth Contributions. Beginning in 2023, 401(k), 403(b) or government 457(b), and other qualified defined contribution plans may allow an employee to elect to have employer matching and non-elective contributions made to the plan as Roth contributions. The election will be permitted, however, only if these employer contributions are immediately vested. The change allows a plan to include Roth contributions (and, if it does, in-plan Roth rollovers/conversions) whether or not the plan permits employee elective deferrals.

Previously, a plan only could allow an employee to elect to contribute their salary reduction elective deferrals as Roth contributions. If the plan did allow this election, then the plan, by its terms, could permit the employee to elect to convert other non-Roth balances, including amounts attributable to employer matching and non-elective contributions, to Roth amounts through an in-Plan Roth rollover/conversion.

Changes Effective Beginning in 2024

Increased Automatic Small Benefit Cash-Out Limit. Effective beginning January 1, 2024, a qualified retirement, 403(b), or government 457(b) plan is permitted to provide that a participant's benefit will be cashed out automatically upon termination of employment (i.e., without their consent) if their vested benefit does not exceed $7,000. Under current law, the limit on automatic cash-outs is $5,000.

Age-50 Catch-Up Contributions. Starting in 2024, a 401(k), 403(b), or government 457(b) plan must treat age-50 catch-up contributions made by a participant who received compensation greater than $145,000 (as indexed for inflation) in the preceding year as Roth contributions.

No Mandatory RMDs from Roth Accounts. For RMD distribution years beginning after 2023, a participant will not be required to take RMDs from a designated Roth account under a 401(k), 403(b), governmental 457(b), or other qualified defined contribution plan during their lifetime. The RMD rules applicable at death continue to apply to a designated Roth account.

Matching Student Loan Payments. Currently, an employer may choose to make an employer contribution based on student loan payments. This contribution is treated as an employer non-elective contribution, which presents some testing issues for a plan.

Beginning with the 2024 plan year, a 401(k), 403(b), or government 457(b) plan may permit an

employer to make matching contributions on certain qualified higher education loan repayments made by its employees. For testing purposes, these employer contributions will be treated as matching contributions and the employee loan repayments will be treated as elective deferrals, which should simplify administration significantly.

Emergency Savings Account. Beginning in 2024, a 401(k), 403(b), government 457(b), or other qualified defined contribution plan may permit participants who are not highly compensated to make deposits to an emergency savings account within the plan. The plan also may enroll eligible participants automatically to contribute to that account at a contribution rate of not more than 3% of pay. All employee contributions to the account must be Roth after-tax contributions and capped so that the employee's emergency savings account balance does not exceed $2,500 (indexed for inflation). The deposits must be invested in cash, an interest bearing account, or a fund designed to preserve principal. Employees may make monthly withdrawals from the account. For purposes of matching contributions, the employer must treat the amount contributed to the emergency savings account the same as matched employee elective deferrals.

Expanded In-Service Withdrawal Options for Emergencies or Domestic Abuse. Beginning in 2024, a 401(k), 403(b), government 457(b), or other qualified defined contribution plans may permit a participant to take a withdrawal for a personal or family emergency and/or in response to domestic abuse. These withdrawals will not be subject to the 10% penalty tax generally applicable to distributions taken prior to age 59-1/2 and will not be subject to 20% income tax withholding. The plan sponsor may rely on the employee's certification that they have suffered a personal or family emergency or that they have been the victim of domestic abuse. Certain limits apply.

Changes Effective Beginning in 2025

Automatic Enrollment. If an employer establishes a 401(k) or 403(b) plan on or after the effective date of the SECURE Act 2.0 (i.e., December 29, 2022), then, beginning in 2025, the plan generally must provide for automatic enrollment of newly eligible employees at a rate of at least 3% of pay, and provide an annual automatic increase of at least 1% until the participant reaches a contribution level of at least 10% (but not more than 15%) of pay. In addition, the automatic enrollment arrangement must qualify as an eligible automatic contribution arrangement ("EACA") under which employees can withdraw automatic enrollment contributions within 90 days of initial automatic enrollment.

Additional Catch-Up Contributions. Beginning in 2025, the catch-up contribution limit for a participant who is age 60, 61, 62, or 63 will be the greater of $10,000 (indexed for inflation) or 150% of the regular age-50 catch-up dollar limit.

Part-Time Employees. The law previously required that, beginning in 2024, defined contribution plans (other than collectively bargained plans) permitting employee elective deferrals allow part-time employees who complete at least 500 hours of service in each of *three* consecutive years to participate in the plan as to elective deferrals. Effective beginning with the 2025 plan year, a part-time employee must be permitted to make elective deferrals under such a plan if they have *two* consecutive years in which they perform at least 500 hours of service.

Employee Stock Ownership Plans. Code section 1042 provides that a shareholder owning stock of a C corporation that is not publicly traded may sell stock to the corporation's ESOP and elect to defer the recognition of gain on the sale provided that, following the sale, the ESOP owns at least 30% of the corporation's outstanding stock. The gain deferral applies only to the extent the selling shareholder invests the proceeds of the sale in qualifying replacement property (i.e., securities issued by a domestic operating corporation). Certain other requirements also must be satisfied. Effective for

stock sales occurring after 2027, the Code section 1042 option to elect to defer recognition of gain is extended to S corporation shareholders who sell stock to an ESOP. This option to defer gain recognition for S corporation shareholders is limited, however, to 10% of the proceeds of the sale.

Defined Benefit Plans.

1. Lump Sum Window Notice Requirements. Increasing interest rates have made lump sum windows a popular tool for employers to reduce the funding risk of defined benefit pension plans. If an employer intends to offer a lump sum window to participants or beneficiaries new notice requirements will apply. The employer must provide (i) written notice, at least 90 days before the first day that a window lump sum can be elected, to eligible individuals setting forth specified information regarding the window and comparing the lump sum to annuity options, (ii) written notice, at least 30 days before the first day that a lump sum can be elected, to the Department of Labor ("DOL") and the Pension Benefit Guaranty Corporation ("PBGC") describing the window and lump sum calculation and providing a copy of the notice provided to eligible individuals, and (iii) written notice to the DOL and PBGC, within 90 days after the close of the lump sum window, reporting how many individuals took the lump sum option. These notice requirements will not be effective, however, until final regulations are issued.

2. Annual Funding Notice. Currently, a defined benefit pension plan must provide participants an annual funding notice that discloses, among other items, the plan's funding target attainment percentage. Starting with the 2024 plan year, the notice must disclose different information, including the percentage of plan liabilities funded, the average return on assets for the plan year, and whether the assets are sufficient to fund liabilities not guaranteed by the PBGC.

3. PBGC Variable Rate Premium No Longer Indexed. Starting with the 2024 plan year, the PBGC variable rate premium for underfunded defined benefit pension plans will be fixed $52 per $1,000 of unfunded vested benefits and will no longer be indexed for inflation.

Plan Corrections. The IRS is directed to issue updated Employee Plans Compliance Resolution System ("EPCRS") procedures by December 29, 2024. Among other changes, the new EPCRS procedures will allow an employer to correct inadvertent qualification errors in its 401(k), 403(b), or other qualified retirement plan *at any time* under the Self-Correction Program ("SCP") without needing to submit the correction to the IRS for approval. The time limit on correcting "significant errors" applicable previously under SCP will be eliminated. The employer simply must complete the correction within a reasonable period after it identifies the error. Self-correction under SCP will not be available, however, if the IRS identifies the error before the employer has taken action that demonstrates a specific commitment to correct the error.

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