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Key considerations to retirement amendments under Secure 2.0 | VIEWPOINT

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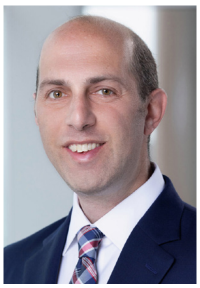
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On December 29, 2022, President Joe Biden signed into law a massive spending bill, the Consolidated Appropriations Act, 2023 (the "CAA"). Lodged towards the end of the CAA, the Secure 2.0 Act of 2022 ("Secure 2.0") ushered in a host of changes to the qualified retirement plan landscape. To some extent, a continuation of a process that started with the original SECURE Act (Secure 1.0), Secure 2.0 is arguably the most significant modification to qualified retirement plans in a generation. Secure 2.0 impacts plan sponsors, participants, service providers and even the government.

After fits and starts and volumes of Internal Revenue Service ("IRS") guidance, plan amendments to comply with Secure 2.0 must be made by December 31, 2026 for most plans. Amendments to Individual Retirement Accounts (IRAs), Roth IRAs, SIMPLE IRAs and Simplified Employee Pensions (SEPs) must be made by December 31, 2027, and amendments to collectively bargained plans must be made by December 31, 2028. Meanwhile, the deadline for governmental plans and public school-sponsored 403(b) plans is December 31, 2029. It is worth noting that many of the changes were required to be implemented at various points between 2023 and the present, resulting in a possible disconnect between plan operations and plan documents.

As the first of a two-part series examining key mandatory and optional amendments, this analysis will deal with some of the more significant mandatory amendments, and Part II will cover some of the more significant optional amendments. Both parts will focus primarily on 401(k) plans but will touch on other types of plans as well.

MANDATORY AMENDMENTS

Required Minimum Distributions (RMDs)

The changes to RMD rules have garnered a tremendous amount of attention, and rightfully so. Briefly, a participant must start receiving benefits by April 1 of the year following the year in which the participant attains a certain age, although employed older participants (other than 5% owners) can delay taking RMDs until after they retire. That certain age had been 70 ½ for decades. Secure 1.0 changed the age to 72 (for people born between July 1, 1949 and December 31, 1950), and Secure 2.0 changed the age to 73 (for people born between January 1, 1951 and December 31, 1959) and to 75 (for people born on or after January 1, 1960).

This change recognizes that Americans are living longer (life expectancy is approaching 80) and working longer. This change is a tremendous boon for participants—an extra three to five years of tax-deferred growth may well result in thousands more to be used in retirement.

Secure 2.0 made other changes to the RMD rules, most notably that Roth IRAs and in-plan Roth amounts are exempt from the RMD rules, and that a spousal beneficiary (assuming the sole beneficiary) can elect to be treated as the deceased participant for RMD purposes.

Long-term part-time employees

Historically, most 401(k) plans have excluded part-time employees, either directly by plan design or indirectly by imposing service requirements that would be impossible for part-time employees to meet. This problem is particularly acute for part-time employees who have worked for the same employer for many years (think seasonal workers).

Secure 2.0 addressed this issue head-on (for 401(k) plans and 403(b) plans that are subject to the Employee Retirement Income Security Act (ERISA)). Employees who work at least 500 (but less than 1,000) hours in two consecutive years for the same employer will be eligible to participate in the plans, with the important caveat that service for that employer before 2021 does not count for these purposes. Employers can restrict long-term, part-time employees from receiving employer contributions and can decide whether to include in certain nondiscrimination tests.

Roth catch ups for high earners

Many (although not all) plans offer participants over age 50 the ability to contribute several thousand dollars more than the statutory limit that applies to participants under age 50. These contributions are known as "Catch-Up Contributions." Under Secure 2.0, for participants who earn more than the $150,000 Federal Insurance Contributions Act (FICA) wage threshold (indexed for inflation), any Catch-Up Contributions must be Roth contributions (broadly speaking, post-tax contributions that, pursuant to certain requirements, are not subject to tax upon distribution).

This new rule only applies to plans that allow Catch-Up Contributions. If the plan does not currently permit Roth contributions, it must either be amended to permit Roth contributions (for all participants) or prohibit high earners from making Catch-Up Contributions. From a recruiting and retention standpoint, prohibiting high earners from making Catch-Up Contributions seems like a suboptimal choice.

PRACTICAL IMPLICATIONS

The above discussion represents a high-level overview of some of the more significant mandatory amendments to 401(k) and other plans. Of course, like any IRS rule, these changes are laden with details and nuance.

What does this mean for plan sponsors? Operationally, sponsors will need to ensure that the relevant stakeholders—HR, payroll, recordkeepers and trustees—are trained and aligned with new policies and procedures. From a document standpoint, for sponsors who adopted a pre-approved/volume submitter plan, there is likely little to do—the document providers (Fidelity, Voya, Vanguard, Schwab, Empower, etc.) have generally either put the amendments directly into the plan or have incorporated them through amendments and/or addenda. In many instances, sponsors will not even have to sign the amendment/addenda. For sponsors using an individually designed plan, ERISA counsel (or, although less frequently, other third-party advisors) will need to draft amendments and related documents.

All in all, Secure 2.0 presents a brave new world for retirement plans, with increased opportunities for participants to save and grow accounts and with increased compliance challenges for plan fiduciaries and other service providers.

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