Insights

The Setting Every Community Up for Retirement Enhancement (SECURE) Act

February 26, 2020

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On December 20, 2019, the Setting Every Community Up for Retirement Enhancement (SECURE) Act was signed into law by President Trump as a part of a larger budget appropriations bill. Many who have commented on the SECURE Act believe it is the most significant retirement legislation in more than a decade, and some of the changes provided for by the Act are effective immediately. It should be no surprise then that important considerations must be given to the new law by retirement plan sponsors. This Alert summarizes the major provisions of the Act and also provides some insights into its impact on retirement plan sponsors. References to the “Code” are to the Internal Revenue Code of 1986 and to “Section” are to sections of the Code.

Rules Relating to Safe Harbor 401(k) Plans:

The SECURE Act implements several changes that attempt to simplify the rules for plans with Section 401(k) safe harbor nonelective contributions. The Act eliminates the safe harbor notice requirement for plans designed to satisfy nondiscrimination via nonelective contributions. Additionally, an existing plan may be amended to become a nonelective safe harbor plan for a plan year, if adopted: (i) sooner than 30 days before the close of the plan year (where the nonelective contribution is 3%), or (ii) before the last day of the following plan year and the nonelective contribution is at least 4% of the employee’s compensation. The Act retains the notice requirement for safe harbor plans with matching contributions.

The Act increases the Qualified Automatic Contribution Arrangements (QACAs) cap on elective contributions after the first year to 15% (leaving the 10% limit in place for the first year). Note, no changes were made to the QACA auto-escalation of minimum contributions table.

These provisions of the Act apply to plan years beginning after December 31, 2019.

Required Beginning Date for Mandatory Distributions - Increased to Age 72

The SECURE Act raises the required minimum distribution (RMD) commencement age from 70 ½ to age 72. The amendment applies to individuals who reach the age of 70 ½ after December 31, 2019. Thus, retirees who turned age 70 ½ during 2019 are still required to take the RMD by April 1, 2020 and December 31, 2020, respectively. For those who will turn age 70 ½ in 2020 and after, this amendment is a welcome opportunity for continued growth of their retirement savings.

Modification of Required Distribution Rules for Designated Beneficiaries

The SECURE Act narrows the class of "designated beneficiaries" who are eligible to stretch distributions from an inherited 401(k) account or IRA over their life expectancy – this assumes the participant died prior to distribution of his or her entire interest in the plan. The Act designates individuals who may continue to exercise this option as "eligible designated beneficiaries," a term which includes the deceased participant's surviving spouse or minor child, a disabled or chronically ill individual, or another individual who is less than 10 years younger than the participant. In the case of other designated beneficiaries, funds in an inherited plan must be distributed to the individual within 10 years of the participant's death; including a beneficiary upon the death of the eligible designated beneficiary. The 5-year distribution rule continues to apply in the case of beneficiaries who are not designated beneficiaries.

Portability of Lifetime Income Options

The SECURE Act eases the portability of amounts invested in a lifetime income investment option under a defined contribution plan, Section 403(b) plan or a governmental Section 457 plan when such option is discontinued. For plan years beginning after December 31, 2019, amounts invested in an option with a lifetime income feature may be distributed in a trustee-to-trustee transfer or by distributing an annuity contract up to 90 days before the investment ceases to be an investment option under the plan, without regard to any in-service withdrawal restrictions, if any, under the plan. A lifetime income feature is one that (i) guarantees a minimum level of income at least annually for at least the remainder of the life of the participant or the joint lives of the participant and his or her designated beneficiary, or (ii) provides an annuity payable on behalf of the participant under which payments are made in substantially equal periodic payments at least annually over the life of the participant or the joint lives of the participant and his or her designated beneficiary.

Disclosure Regarding Lifetime Income

The SECURE Act requires inclusion of a "lifetime income disclosure" in at least one defined contribution plan participant statement furnished during any one 12-month period. In general, the disclosure must include – for illustrative purposes – the lifetime income stream equivalent of a participant's (or beneficiary's) total accrued benefit. The Act dictates that, no later than one-year from its enactment, the Secretary of Labor must issue a model disclosure, interim final regulations, and assumptions used to convert a participant's total accrued benefit into lifetime income stream equivalents. The lifetime income disclosure will become applicable to retirement plan benefit statements furnished more than 12-months after the DOL has issued the model notice, assumptions, and interim final regulations.

Fiduciary Safe Harbor for Selection of Lifetime Income Provider

The SECURE Act implements a new safe harbor under ERISA's fiduciary duty of care, skill, prudence and diligence that is narrowly focused on the task of selecting an insurer for a guaranteed retirement income contract. To satisfy the safe harbor, a fiduciary must engage in an "objective, thorough, and analytical search" for a lifetime income provider, taking into consideration its financial capability to satisfy contractual obligations and relative cost of the contract in light of benefits and features provided; ultimately concluding at the time of selection that the insurer is financially capable and the contract cost is reasonable. The Act further delineates the assessment of an insurer's financial capability and clarifies that there is no requirement that the fiduciary select the lowest cost contract. This provision became effective upon enactment of the Act.

Penalty-Free Withdrawals from Retirement Plans in case of Birth or Adoption

The SECURE Act adds "qualified birth or adoption distribution" under Code Section 72(t)(2) to the list of early distributions from an eligible retirement plan excepted from imposition of a 10-percent early withdrawal penalty tax. The aggregate amount distributed may not exceed $5,000 and must be made during the one-year period beginning on the date on which the child is born or the date on which legal adoption (excludes adoption of a spouse's child) is finalized. Further, the Act permits a participant to repay distribution amounts in the form of one or more contributions – treated like rollovers – made to an "applicable eligible retirement plan" (term does not include defined benefit plans) of which he or she is a beneficiary. This provision of the Act applies to plan years beginning after December 31, 2019.

Credit Card Loans Prohibited

The SECURE Act prohibits a plan from making any loan made through the use of a credit card or any similar arrangement. This provision became effective for loans made after the date of enactment of the Act. This prohibition was included to reduce small loans from retirement plans.

Treating Excluded Difficulty of Care Payments as Compensation for Determining Retirement Contribution Limitations.

The SECURE Act creates a special rule for "difficulty of care" payments to foster care parents by allowing an individual who excludes such amounts from gross income under Code Section 131, to elect to include such amounts as compensation for retirement plan purposes. Contributions attributable to difficulty of care payments shall be treated as after-tax and not counted toward the limit under Code Section 415(c). These provisions are effective for defined contribution plans for plan years beginning in 2016 and after, and for contributions to IRAs beginning after the date of the Act's enactment.

Plan Adoption

The SECURE Act permits retroactive adoption of a new stock bonus, pension, profit-sharing, or annuity plan up to the time prescribed for the employer to file its tax return for the taxable year (including extensions thereof); the employer may elect to treat the plan as having been adopted as of the last day of the taxable year. Previously, plans had to actually be adopted by the last day of the calendar year in which they were to be effective. This provision is applicable to plans adopted for taxable years beginning after 2019 and onward.

Combined Annual Reporting for Group of Plans

The SECURE Act directs the DOL and the Treasury to allow consolidated reporting on Form 5500 by members of a group of plans, comprised by individual account or defined contribution plans, that have the same trustee, one or more of the same named fiduciaries, the same administrator, the same plan years beginning on the same date, and that provide the same investments and options to participants. This modification must be implemented by January 1, 2022, and applies to returns and reports for plan years beginning after December 31, 2021.

401(k) Eligibility for Long-Term, Part-Time Employees

The SECURE Act modifies the requisite eligibility terms for 401(k) plans (excluding collectively bargained plans) to include employees who have worked at least 500 hours of service in each of three consecutive years and attained the age of 21. The new criteria are in addition to the traditional year of service requirement based on 1,000 hours. This change is intended to provide a dual eligibility requirement to address the disproportionately negative impact the current 1,000 hours of service requirement has had on women's retirement savings, as women are more likely than men to work part-time. Notably, although employees eligible to participate under this new rule must be allowed to make deferrals, employers are not required to make matching or nonelective contributions to them, nor are they subject to nondiscrimination testing and minimum coverage requirements. This amendment applies to plan years beginning after December 31, 2020; however, the Act permits employers to disregard any 12-month periods that begin in 2020.

Defined Benefit Plan Nondiscrimination Requirement Modified

The SECURE Act provides relief to partially frozen defined benefit plans under nondiscrimination and minimum coverage rules effective for plan years beginning after December 31, 2019. The provision allows grandfathered participants to continue accruing benefits even as the size of the group becomes smaller.

Penalties

The SECURE Act increased various penalties tenfold (10x):

- The penalty for failure to file a Form 5500 increased from $25 to $250 per day, and the annual penalty cap increased from $15,000 to $150,000.
- The penalty for failure to file a Form 8955-SSA increased from $1 to $10 per day per participant, and the annual penalty cap increased from $5,000 to $50,000.
- The penalty for failure to provide withholding notices increased from $10 to $100 per failure, and the annual penalty cap increased from $5,000 to $50,000.

These penalties have a far greater sting as a result of the SECURE Act. Particularly with respect to the Form 5500 filing requirement, plan sponsors should ensure that they are hitting their filing and notice deadlines. The increased penalties apply to returns, statements, and notifications required to be filed, and notices required to be provided, after December 31, 2019.

Multiple Employer Plans with Pooled Providers

The SECURE Act amends the Code to provide for a new type of open multiple employer plan (MEP) – the so-called "pooled employer plan" (PEP) –comprised of two or more employers that do not share a common interest other than having adopted the plan. A PEP is treated as a single plan for purposes of ERISA and may be either defined contribution plans or a plan consisting of individual retirement accounts. The Act requires PEPs to designate a "pooled plan provider" as a named fiduciary of the plan, who is responsible to perform all administrative duties that are reasonably necessary to keep the plan compliant (e.g. conduct nondiscrimination testing, provide participants with the proper disclosures, etc.). The pooled plan provider must register with the Secretary of the Treasury and be subject to administrative audits, examinations, and investigations. The pooled plan provider must acknowledge in writing its status as named fiduciary and plan administrator, and ensure that all other named fiduciaries or persons who handle plan assets are properly bonded. Nevertheless, except with respect to the administrative duties of the pooled plan provider, each adopting employer of the PEP will be treated as the plan sponsor for its portion of the plan's covered employees.

Additionally, MEPs will no longer be subject to the “one bad apple” rule, whereby the failure of one adopting employer to meet the qualification requirements may cause the entire MEP to fail. The Act conditions this relief on two requirements: (i) plan assets attributable to the employer that caused the failure must be transferred to another plan of the employer, and (ii) that employer is responsible for liabilities attributable to its employees covered by the plan.

Lastly, certain MEPs will be permitted to file a simplified Form 5500 if the plan covers fewer than 1,000 participants and no single adopting employer has 100 or more participants covered by the plan.

The new law removes critical hurdles to MEPs and renders them a more viable option for employers going forward. In particular, PEPs should allow smaller employers to band together to leverage their combined purchasing power and to shift the burdens of plan administration to a centralized entity (i.e. the pooled plan provider). These provisions of the Act are applicable to plan years beginning after December 31, 2020.

Timing of Plan Amendments to Conform to SECURE Act

The deadline for plan amendments made pursuant to the SECURE Act, plus any subsequent regulations issued by the Treasury or the Department of Labor, is the end of the first plan year beginning on or after January 1, 2022. With respect to governmental or collectively bargained plans, the deadline is the end of the first plan year beginning or after January 1, 2024.

While plan sponsors have time to amend their plans, many of the provisions are effective as of January 1, 2020 (as noted in this Alert) and will require changes to plan administration and/or plan recordkeeping.

Summary of Remaining Provisions

The SECURE Act includes a number of other provisions that are noted below. The Act:

- Creates a new three-year tax credit for small employers for startup costs for new pension plans that include automatic enrollment.
- Requires the Treasury to issue guidance on the treatment of custodial accounts on the termination of Section 403(b) Plans (allowing participants to continue to maintain them in some circumstances outside of the plan).
- Increases the tax credit for small employer pension plan startup costs from $500 up to $5,000.
- Reduces Pension Benefit Guaranty Corporation (PBGC) premium rates for Cooperative and Small Employer Charity (CSEC) plans for plan years beginning after 2018.
- Expands Section 529 education savings accounts to cover costs associated with registered apprenticeships, student loan repayments, and certain costs associated with elementary and secondary education (up to $10,000 per individual).
- Eliminates the taxation of the unearned income of children at rates applicable to trusts and estates. Such income would be taxed at the parents' marginal tax rates.

Conclusion

The SECURE Act offers the opportunity for many changes to the operation of an employer's retirement plans, some of which will trigger plan amendments. Even if a plan amendment is not immediately necessary, a notice or an update to the plan's summary plan description or administrative procedures may be needed. If you have questions or would like more information regarding the SECURE Act please contact any member of the Krieg DeVault Employee Benefits and Executive Compensation Practice Group for assistance. We will also provide an update on the SECURE Act at our "KD Benefits Outlook" Conference for our clients on April 28th at the Sheraton Hotel Keystone Crossing. Clients will hear more on that very soon!