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On December 29, 2022, President Biden signed The Consolidated Appropriations Act ("CAA"), 2023 into law. This legislation contains several important sections that affect employers and employees: SECURE 2.0, the Pregnant Workers Fairness Act ("PWFA") and Providing Urgent Maternal Protection ("PUMP") for Nursing Mothers Act. This paper will address the key components of SECURE 2.0.

Setting Every Community Up for Retirement Enhancement Act ("SECURE 2.0")

Secure 2.0 is a collection of amendments to the laws governing retirement savings which build upon the provisions of the Secure Act of 2019. Some of the provisions include requiring automatic enrollment in some workplace plans, increasing "catch up" contributions that older workers can make and boosting part-time workers' access to retirement plans. There are also provisions related to increasing employees' ability to create emergency savings and access emergency funds. The overarching goal is to encourage individuals to save for retirement.

Below is a summary of the new provisions under SECURE 2.0 that will impact retirement plans.

Automatic Enrollment and Automatic Escalation

Beginning in 2025, most new 401(k) and 403(b) plans must meet the requirements for an eligible automatic contributions arrangement, including automatic enrollment with a default rate of between 3% and 10% with a 90 day unwind feature, and automatic escalation of 1% per year up to at least 10% but not more than 15%. Existing plans will be grandfathered.

Automatic enrollment in a retirement plan is designed to make it easier for employees to participate. Employees who prefer not to participate can opt out. Businesses will be permitted to integrate automatic enrollment with payroll.

> **Exclusions:** This provision does not apply to: (1) 401(k) and 403(b) plans that were adopted prior to January 1, 2025; (2) governmental or church plans; (3) SIMPLE 401(k) plans; (4) new businesses (in existence for less than three years); and small employers (normally employs 10 or fewer employees). For example, employers will not need to have automatic enrollment for any new employees hired after January 1, 2025 as long as the plan was already in effect.

The Act also permits retirement plan service providers to offer plan sponsors automatic portability services for certain low balance retirement accounts. This is intended to make it easier for participants with low balances to rollover their accounts when they switch jobs, rather than cashing out.

Increase to Catch-up Contribution Limits

Starting in 2024, all catch up contributions to non- SIMPLE plans must be Roth contributions for participants with compensation equal to or in excess of $145,000.

Beginning in 2025, the catch-up contribution limit for participants between the ages of 60 and 63 in a SIMPLE plan will increase from $3,000 to the greater of $5,000, or 150% of the regular catch-up amount. Beginning in 2025, catch-up contributions for participants between the ages of 60 and 63 in non- SIMPLE plans will increase to the greater of $10,000 or 150% of the regular catch-up amount. (The catch-up amount for people aged 50 and older in 2023 is currently $7,500.)

One caveat: employees 50 or older earning more than $145,000 in the prior calendar year, all catch-up contributions at age 50 or older will need to be made to a Roth account in after-tax dollars. Individuals earning $145,000 or less, adjusted for inflation going forward, will be exempt from the Roth requirement.

IRAs currently have a $1,000 catch up contribution limit for people age 50 and over. Starting in 2024, that limit will be indexed to inflation, meaning it could increase every year, based on federally determined cost of living increases.

Extension of Multiple Employer Plans (MEP) to 403(b) Plans

The Act will extend the current hardship distribution rules for 401(k) plans to 403(b) plans.

403(b) plans will now be allowed to invest in collective investment trusts.

Beginning in 2023, 403(b) plans may be maintained as a MEP, provided that the MEP is only comprised of either governmental or non-governmental employers. Additionally, 403(b) plans subject to ERISA may maintain a 403(b) pooled employer plan (“PEP ”).

Roth Elections for Matching Contributions

Effective immediately, participants may make a Roth election to employer matching contributions. Previously, matching contributions in employer-sponsored plans were made on a pre-tax basis. Contributions to a Roth retirement plan are made after taxes, after which earnings can grow tax free. Matching and nonelective contributions designated as Roth are not excludable from the employee’s income and must be 100% vested when made. While these provisions take effect immediately, it will likely take time for plan providers to offer this and for payroll systems to be updated.

Student Loan Repayments Treated as Elective Deferral Contributions

Beginning in 2024, even if an employee does not contribute directly to their own 401(k) plan, employers may offer matching contributions to the employee's 401(k) when an employee makes a student loan repayment. This will be an attractive benefit to younger employees who often defer retirement savings while they are repaying student loan debt.

Emergency Withdrawals

Typically, early distributions from tax- preferred retirement accounts, such as 401K plans are taxed an additional 10%. Beginning in 2024, the Act provides an exception for certain distributions for unforeseen emergency expenses, relating to personal or family emergencies. A participant may make a withdrawal of up to $1,000 per year from their retirement account for certain emergencies. The employer may rely on the employee's written certification that they are facing a qualifying immediate emergency personal expense, and that such distribution is not in excess of the amount required to satisfy such financial need. The withdrawal will be taxable and may be repaid within three years, but it will not be subject to the 10% penalty for early withdrawals. Only one withdrawal is permitted during the three-year repayment period if the first withdrawal has not been repaid. Further guidance is expected on this provision.

10% Early Withdrawal Penalty Waived for Terminally Ill

Effective immediately, the 10% penalty on early withdrawals before age 59 1/2 is waived for distributions to terminally ill individuals whose physician certifies that they have a condition that is expected to result in death within 84 months.

Emergency Funds for Victims of Domestic Violence.

Secure 2.0 permits penalty-free withdrawals of small amounts of up to $10,000, or half of the vested account balance, whichever is smaller, for participants who are victims of domestic abuse. Employees may self-certify that they are victims of domestic violence in order to make the withdrawal. This will allow much quicker access to funds to allow victims to relocate into a safer space as fast as possible, thus reducing the chance of danger from assault. The withdrawal is not subject to the 10% premature distribution penalty and may be repaid into the plan as a loan. Further guidance is expected on this provision.

Creation of "Pension Linked Emergency Savings Accounts"

Beginning in 2024, the Act allows employers to create an Emergency Savings Account (ESA) as part of a defined contribution plan. Non-highly compensated employees, may contribute up to 3% of their compensation, not to exceed $2500 indexed for inflation, to an ESA. All contributions must be made on an after-tax basis. Each month, participants may take withdrawals from their ESA and the first four withdrawals for a year would be tax and penalty free. Subsequent withdrawals may be subject to reasonable fees or charges in connection with such withdrawal. Depending on plan rules, contributions may be eligible for an employer match. At separation from service, employees may take their emergency savings accounts as cash or roll it into their Roth defined contribution plan (if they have one) or IRA. In addition to giving participants penalty free access to funds, an emergency savings fund could encourage plan participants to save for short-term and unexpected expenses. Only non-highly compensated employees (i.e. earning less than $145,000) are eligible for ESAs.

Changes to Long-Term, Part-Time Employees

The Act modifies the measuring period for long-term, part-time employees from three years to two years. Beginning in 2025, part-time employees will now be eligible to make plan contributions as of the earlier of one year of service, or the completion of a 24 month period consisting of two consecutive 12 month periods with 500 hours of service and attainment of age 21 by the end of the calendar year. The Act also extends the long-term, part-time employee provision to 403(b) plans that are subject to ERISA.

This provision does not apply to collectively bargained plans or non-resident aliens and the 12 month period beginning before January 1, 2023, is not taken into account for purposes of determining eligibility.

Enhanced Tax Credits for New Smaller Plans

Starting in 2023, businesses with 50 or fewer employees can qualify for a credit equal to 100% of the administrative costs for establishing a workplace retirement plan. The original SECURE Act gave startup businesses with up to 100 employees a tax credit equal to 50% of administrative costs, capped annually at $5000. Eligible businesses with 51 to 100 employees remain subject to the original SECURE Act provision.

Also beginning in 2023, businesses with up to 100 employees might be entitled to a tax credit based on their employee matching or profit-sharing contributions. This credit, which caps at $1000 per employee, phases down gradually over five years and is subject to further reductions for employers with 51 to 100 employees.

Small Financial Incentives for Contributing to a 401(k) or 403(b) Plan

Employers could offer de minimis financial incentives, such as low dollar gift cards, to boost participation in retirement plans. The financial incentives cannot be purchased with plan assets.

Plan Amendments

Plan amendments to satisfy the Act must be adopted no later than the end of the 2025 plan year for non-governmental plans, and the end of the 2027 plan year for governmental plans and collectively bargained plans. The Act also extends the plan amendment deadline for Setting Every Community Up for Retirement Enhancement Act of 2019, the Coronavirus Aid, Relief, and Economic Security Act (CARES), and the Taxpayer Certainty and Disaster Tax Relief Act of 2020 to align with the plan amendment deadlines noted above.

<u>Other Relevant Provisions:</u>

- **Required Minimum Distributions** – the age for required minimum distributions ("RMD") will increase to 73 beginning in calendar year 2023 and 75 beginning in calendar year 2033; beginning in 2024 Roth accounts in employer-sponsored plans are exempt from RMD rules.

- **Creation of a New Retirement Savings Lost-and-Found Data Base** – the Department of Labor must create an online searchable database to assist participants and beneficiaries in locating plan benefits.

- **Increased Dollar Threshold for Mandatory Distributions** - for distributions after Dec. 31, 2023, the involuntary distribution threshold will increase from $5,000 to $7,000.

- **Expansion of Employee Plans Compliance Resolution System ("EPCRS")** – the IRS self-correction program will allow plan sponsors to correct inadvertent failures at any time.

- **Recovery of Retirement Plan Overpayments –** plan fiduciaries may elect not to recoup inadvertent benefit overpayments without risking disqualification of the plan; certain protections apply to participants if repayment is sought.

- **Expansion of 1042 Elections –** beginning in 2028, taxable income on a portion of the proceeds from the sale of an S corporation to an employee stock ownership plan ("ESOP") may be deferred.

The SECURE 2.0 Act contains several broadly applicable changes, apart from the ones in this summary, and many smaller specific changes, that employers may, and in some cases must, incorporate into their plans and plan operations. Generally, the majority of these changes will not require retirement plans to be formally amended until the end of 2025. Employers and plan administrators should consult with their counsel and other advisors to determine which provisions apply to their plans, and how to incorporate them to remain in compliance with this new law.

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