March 31, 2020

BREAKING DOWN THE SECURE ACT - 401(K) AND OTHER DEFINED CONTRIBUTION PLANS

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Benefits experts are still poring through the SECURE Act's various mandated provisions, optional provisions, and effective dates, some of which may be retroactive. This series of articles will break down the implications that the Act has for existing tax-qualified retirement plans. This article will focus on the Act's impact on 401(k) and other defined contribution plans. Related articles address *required minimum distributions*, which impact defined contribution plans and defined benefit plans, and future articles will discuss changes for tax-qualified defined benefit plans only; as well as other changes to the retirement plan landscape.

Remedial Amendment Period

Plan sponsors generally have until the last day of the 2022 plan year to adopt amendments that reflect the Act's required revisions. For calendar year plans the last day is December 31, 2022. Governmental plans have until the 2024 plan year to amend. Remember that operational compliance is still required during the period from the effective date for the Act's required changes and the date the plan is amended.

401(k) Plans: Part-time Long-term Workers - MANDATORY

Prior law: An employer-sponsored 401(k) was permitted to exclude employees who did not complete a year of service, defined as the completion of 1,000 hours of service during a 12-month measurement period.

Under the SECURE Act: Part-time long-term workers must be eligible to make salary deferrals (pre-tax, Roth and catch-up, as applicable) under a 401(k) plan if they (a) obtain age 21; and (b) work at least 500 hours in three consecutive 12-month measurement periods. For purposes of vesting, a year of vesting service is a 12-month measurement period during which a participant works at least 500 hours.

Purpose: This change expands retirement savings opportunities for an employer's long-term part-time workers.

Effective date: The new inclusion and vesting rules are effective for plan years beginning after December 31, 2020.

What to do and when: 401(k) plans sponsors should begin to track part-time workers on the first day of the plan year after December 31, 2020. For calendar year plans, that means January 1, 2021. If part-time workers under a calendar year plan provide at least 500 hours of service in plan years starting January 1, 2021, January 1, 2022 and January 1, 2023, then such part-time workers must be permitted to make deferrals under the 401(k) plan beginning January 1, 2024.

Now is the time for employers and their service providers to plan for tracking part-time employees beginning in 2021 for possible inclusion and for purposes of vesting under the 401(k) plan in 2024.

Special notes: Plans are not required to include these part-time long-term workers in matching or other employer contributions. Additionally, these workers are excluded from non-discrimination (ADP, ACP, 401(a), 410(b)), safe harbor plan and top-heavy testing. Remember that if otherwise eligible part-time employees provide 1,000 or more hours of service and meet any age requirement, they must be included in the retirement plan for all contribution purposes.

Safe Harbor 401(k) Plans: QACA Maximum Deferral Rate Increase - OPTIONAL

Prior law: A Qualified Automatic Contribution Arrangement ("QACA") is an employer-sponsored retirement plan that provides for automatic enrollment. Among the strict requirements applicable to a QACA is a maximum automatic deferral rate of 10% of compensation.

Under the SECURE Act: A QACA plan can now provide a new maximum deferral rate of 15% of compensation, except for the participant's first year, which remains 10%. The minimum thresholds of 3% to 6%, depending on the year of participation, remain in place.

Purpose: This change encourages more retirement savings by permitting higher 401(k) deferral rates for safe harbor plans which provide automatic increases.

Effective date: The new maximum deferral rate can be effective for plan years after December 31, 2019. That is January 1, 2020 for calendar year plans.

What to do and when: Plan sponsors should review the pros and cons of raising the maximum deferral rate, including its impact on matching and other employer contributions. Changing the deferral rate will also impact other plan documentation including a summary of material modifications, safe harbor notices and other employee communications. Remember, plan sponsors must adopt an amendment to change the maximum deferral rate. If you are considering a mid-year change, service providers will need to be consulted to ensure it can be operational as intended.

Safe Harbor 401(k) Plans: Elimination of Notice Requirement and related changes – OPTIONAL

Prior law: In order for a tax-qualified 401(k) plan to rely on the 3% nonelective contribution safe harbor, participants had to be provided (definitive or contingent) notice of the plan's safe harbor status by the 30th day before the end of the plan year. In addition, the safe harbor provision had to be in the plan document.

Under the SECURE Act: A 401(k) plan can be amended as late as 30 days prior to the end of the plan year to provide for a 3% nonelective contribution safe harbor for that plan year, without any notice to participants. A plan can also be amended as late as the last day for distributing excess contributions for a plan year, which is generally the last day of the following plan year, if a plan sponsor provides for a 4% nonelective contribution.

Purpose: This change takes away one more hurdle for employers to adopt safe harbor plans that provide a minimum employer contribution that encourages retirement savings.

Effective date: The changes to safe harbor notice requirements are effective for plan years after December 31, 2019.

What to do and when: Plan sponsors must amend their tax-qualified retirement plans in order to effect these changes. Note that the permitted retroactive amendment may be of special interest to plans which experience ADP/ACP test failures.

Special notes: The Act did not eliminate the notice requirement for matching safe harbor contributions.

In-service withdrawals for birth and adoption expenses - OPTIONAL

Prior law: There were no special provisions for plan distributions related to birth or adoption expenses.

Under the SECURE Act: A defined contribution plan may permit withdrawals of up to $5,000 within one year following the birth or legal adoption of a child. The withdrawal will not be subject to either the 10% penalty for withdrawals by participants under age 59-1/2 or the 20% mandatory withholding for federal income tax. The plan may provide for repayment of the withdrawal.

Purpose: This change provides an opportunity for families to ease some of the immediate financial burdens associated with becoming parents.

Effective date: The new in-service withdrawal opportunity is available for withdrawals after December 31, 2019.

What to do and when: Plan sponsors may amend their plans now to permit these in-service withdrawals. Employers should work with their service providers to implement these new withdrawals. In light of the current lack of guidance from the Internal Revenue Service (IRS), plan sponsors should consider acting conservatively by requiring documentation and certain representations as to the birth or adoption, and setting forth clear repayment provisions. Other operational considerations include updating distribution forms, summary plan descriptions (SPDs), participant communications and reporting requirements.

Lifetime income disclosures - MANDATORY

Prior law: ERISA requires periodic employee benefit statements from defined contribution plans that detail vesting status and account investments.

Under the SECURE Act: A "lifetime income disclosure" has been added as an annual disclosure. The new disclosure must describe a monthly annuity amount that could be obtained with the balance of the participant's account. The monthly amount will be based on assumptions specified by the Department of Labor (DOL) in interim rules to be issued by December 20, 2020, which will include a model disclosure statement. Disclosures that meet legal requirements will protect plan sponsors and other plan fiduciaries from liability based on the information provided in the statements.

Purpose: This change gives participants more information to help them assess their current retirement savings status so they can make appropriate changes for retirement readiness.

Effective date: The disclosure will be required 12 months after the latest of the DOL's issuance of the assumptions to be used, the model disclosure and the interim final rules. The earliest date this requirement will be effective is sometime in 2021.

What to do and when: Plan sponsors should stay in contact with their service providers to timely implement this new requirement. Plan sponsors should anticipate that this requirement will increase plan expenses.

Lifetime income contract portability - OPTIONAL

Prior law: In-service distributions from defined contribution plans are subject to certain restrictions that vary by plan type.

Under the SECURE Act: 401(k) plans, 403(b) plans and governmental 457(b) tax-qualified plans can be amended to provide for the in-service distribution of in-plan annuity contracts if the plan stops offering that investment option. Portability options include direct rollover of the contract to an eligible retirement plan that will continue the investment, or distribution to the participant or beneficiary. Distribution must take place in the 90-day period prior to the investment option becoming unavailable under the plan.

Purpose: This change encourages investment in lifetime income options by expanding portability, and enhances the possibility of retirement readiness.

Effective date: The new distribution option for lifetime investments is available for plan years beginning after December 31, 2019.

What to do and when: Plan sponsors must amend their plans in order to effect this change.

403(b) plan termination and treatment of custodial accounts

Prior law: Under IRS guidance, individual annuity contracts could be distributed to participants, but the guidance did not address individual custodial accounts.

Under the SECURE Act: Individual custodial accounts may be distributed in-kind from a terminating 403(b) plan, without causing immediate taxation to the participant or beneficiary. The IRS has until June 20, 2020 to issue guidance which will include that the distributed custodial account will be maintained by the custodian on a tax-deferred basis until amounts are actually paid.

Purpose: This change conforms the treatment of annuity contracts and custodial accounts in terminating 403(b) plans, and makes it easier for employers to terminate plans with custodial accounts.

Effective date: The treatment of custodial accounts from a terminating 403(b) plan is retroactively effective for taxable years beginning after December 31, 2008. By adopting this retroactive effective date, the in-kind distributions of custodial accounts to participants or beneficiaries to complete a termination during the retroactive period will not be treated as having been taxable distributions.

What to do and when: For plan sponsors that are considering terminating a 403(b) plan with individual custodial accounts, this new flexibility may provide a deciding factor. In addition, plan sponsors should watch from new guidance from the Secretary of the Treasury regarding this change. The guidance must be issued within six months of December 20, 2019.

Questions? Please contact the Findley consultant you regularly work with or Sheila Ninneman at *Sheila.Ninneman@findley.com*, or *216.875.1927*

Article - *The SECURE Act and Required Minimum Distributions*