December 22, 2020

# SECURE Act Important Provisions

***A Message to our Valued Clients and Partners:***

*Once again, we hope you, your families, and your employees and their families are continuing to be safe and well.*

*The SECURE Act was signed into law in December 2019 and contains significant developments for retirement plans. Some of the focus on this law was upstaged by the CARES Act in March 2020. However, there are key provisions that become effective in 2021, which are outlined below.*

*By: David Beck, CPA, QPA, ERPA*

## Executive Summary

The following is a high-level summary of the significant changes made by the SECURE Act and described in more detail below.

- **Part-time Employees -** Plans with eligibility provisions that exclude part-time employees must now expand eligibility for 401(k) contributions to include those employees; *if* they are credited with 500 hours of service in at least 3 years.
    - The earliest date on which these policies will have any effect will be January 1, 2024, further discussions will occur over the next few years.
- **Birth/Adoption -** Participants (and their spouse) who give birth to, or adopt a child are eligible to withdraw $5,000 on a tax-favored basis from their IRAs or retirement plans.
- **Required Minimum Distributions -** The age at which RMDs must commence has been increased from age 70½ to 72.
- **Tax Credits -** Significant new tax credits were created to encourage the establishment of new plans as well as the addition of Automatic Enrollment (effective in 2020).

## PART I: Long-Term Part-Time Employees ("LTPT Employees")

These provisions require that, regardless of a Plan's existing eligibility provisions, employees who are credited with at least 500 hours of service in three *consecutive* 12-month periods must be permitted to make their own payroll deduction contributions.

Plans commonly require that employees be credited with 1,000 hours of service in 12 months of employment in order to be eligible to participate in the Plan. It is for these Plans that the LTPT Employee rules will have the most significant impact.

Because these rules are complex, it is important to describe early on which Plans are exempt from these rules.

- 403(b) Plans are not subject to these rules because the existing "universal availability" standard already requires widespread participation.
- Plans that do not require a minimum number of hours in order to participate in the 401(k) payroll deduction portion of the Plan are not subject to these rules because LTPT Employees would not be excluded from participating in such a Plan.
    - Although a Plan that currently includes the "1,000 hours in 12 months" eligibility provision might be amended to fit within this exception, there are potentially significant complications. The principal considerations are a) the top-heavy rules, and b) the requirement to engage a CPA firm to audit a Plan with more than 100 Participants. Both of these considerations should be discussed with PASI directly as they are complex and heavily based on your Plan's unique circumstances.
        - *Plans already subject to the audit requirement (which are almost never top-heavy) are the most obvious candidates to take advantage of this exception.*

The following points represent the most critical aspects of these rules. Because these rules will have dramatic implications for many Plans, we wanted to provide a thorough analysis of the considerations.

*The first day of the Plan Year that begins during 2021 is referred to in this article as the "Initial Effective Date". Service rendered before the Initial Effective Date is not taken into account for purposes of applying these LTPT Employee rules.*

- The *earliest* an LTPT Employee will become eligible to make contributions to a Plan will be the first day of the Plan Year beginning on or after January 1, 2024.
- <u>Employees hired *before* the Initial Effective Date:</u> Employees who are credited with at least 500 hours of service in three consecutive Plan Years that begin on or after the Initial Effective Date will become eligible to participate in the Plan as LTPT Employees.
- <u>Participants hired *after* the first day of the Initial Plan Year:</u> Employees who are credited with at least 500 hours of service in their first 12 months of employment will receive credit for their first year of service on their 12-month anniversary of employment. Additional years of service will be credited for each *Plan Year* during which the Participant is credited with 500 hours of service. Therefore, a Participant might receive credit for their first 12 months of Employment *and* the Plan Year that includes their first anniversary of employment. This double-counting of service is particularly dramatic for employees hired late in a Plan Year. For example, an employee hired on November 30, 2021 might receive credit for their first year of service on November 30, 2022, and their second on December 31, 2022 -that's 2 full

years of eligibility service in just 13 months (assuming a calendar year plan).

    - It is possible to apply these rules based on each employee's unique employment anniversary, thus avoiding the "double counting" described above, but this method is administratively cumbersome.
    - If, as is the case with virtually all of our clients, the "plan year method" of tracking eligibility is used, then the review of these LTPT Employees would only be required before the beginning of each Plan Year (with the first such review performed before the plan year beginning in 2024).
  - An individual who has satisfied the LTPT Employee service requirements but has not yet attained the minimum required age provided for by the Plan is not eligible to participate until the age requirement is met.
  - LTPT Employees are not eligible for Employer Contributions unless they have satisfied any more restrictive requirements which might apply.
  - LTPT Employees are generally excludable for purposes of nondiscrimination testing and are not taken into account for "top-heavy minimum" contributions.
  - Plans that are designed to avoid these LTPT Employee rules (e.g., by not requiring a minimum number of hours) are *not* permitted to exclude these same employees from top-heavy minimum contributions.
  - LTPT Employees who are covered by collective bargaining agreements are not required to be provided with the participation opportunities described herein.

*It has not yet been clarified whether or not individuals excluded from the Plan based on their employee-type will be subject to these LTPT Employee rules. For example, a Plan might exclude "per diem employees" from participating in a Plan. If a per diem employee meets the LTPT Employee requirements by working 500 hours in 3 consecutive years, must they be provided with an opportunity to contribute? The answer is not yet clear (pending additional guidance).*

*There are also unanswered questions regarding vesting provisions applicable to LTPT Employees, particularly with respect to those employees who subsequently become eligible for Employer contributions under the normal eligibility rules.*

## PART II: Birth/Adoption Related Expenses

A Qualified Birth or Adoption Distribution is a tax-advantaged distribution available to new parents during the 12-month period beginning on the child's date of birth or the effective date of the adoption.

- These distributions are limited to $5,000 per birth or adoption.
- Each parent is entitled to their own $5,000 distribution for the same child.
- Essentially all defined contributions plans are permitted (but not required) to offer this distribution option.
  - *Defined benefit pension plans are not permitted to offer this distribution option.*
- These distributions are **not** subject to the 10% penalty tax on early withdrawals.
- The distribution is not considered eligible for rollover treatment; as such, mandatory federal tax withholding does not apply.
- Such distributions can be repaid to an IRA or a qualified retirement plan in whole or in part in order to reverse the prior taxation of the distribution. Unlike CARES Act distributions (under which repayment is only available for three years), the ability to repay these distributions does not expire at any time.

## PART III: Required Minimum Distributions (RMDs)

The age at which required minimum distributions must commence was increased from age 70½ to age 72.

It should be noted that the CARES Act eliminated Required Minimum Distributions (RMDs) from IRAs and Defined Contribution plans for 2020. RMDs were not waived for defined benefit plans in 2020.

## PART IV: Additional Tax Credit Opportunities

Please click here for a previous write up regarding tax credits available for new plans. There are also tax credit incentives related to adding certain automatic enrollment arrangements. Please contact your plan consultant at PASI for more information regarding these new opportunities.

## PART V: SECURE Act Plan Amendments

As with the CARES Act, SECURE Act Amendments are not required until the end of 2022 at the earliest.

***As always, should you have any questions, or if you would like to talk through these or other issues, please reach out to us.***

Get in Touch with PASI

10 Talcott Notch, 2nd Floor
Farmington, CT 06032
T - 860.284.6880
F - 860.284.6887
info@pasiusa.com
www.pasiusa.com