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SECURE Act Makes Sweeping Changes to Retirement Plans

December 20, 2019

This evening, the President is expected to sign into law an end-of-year appropriations bill that includes the Setting Every Community Up for Retirement Enhancement Act (the "SECURE Act" or "Act"), a significant retirement plan reform package.

Many of the SECURE Act's provisions are set to become effective January 1, 2020 for calendar-year plans. The major changes implemented by the SECURE Act are described below:

Changes to Participant Eligibility and Distribution Requirements

The SECURE Act makes the following changes to participant eligibility requirements and permits the following new types of distributions:

- The Act expands the minimum eligibility requirements for 401(k) plans. Generally effective January 1, 2021, 401(k) plans must permit part-time workers who work for 500 hours or more per year for three consecutive years to be eligible to make contributions to the plan, provided that they satisfy any age requirement under the plan. Employers can elect to exclude these employees for purposes of coverage, nondiscrimination (including ADP testing), and top-heavy testing.

- The Act changes the required beginning date rules for required minimum distributions for individuals who attain age 70½ on or after January 1, 2020. Previously, terminated employees were required to begin taking minimum required distributions on April 1 of the calendar year after the employee turned age 70½. Under the SECURE Act, the required beginning date is changed to April 1 of the calendar year after the employee turns age **72**. (Employees are still not required to begin taking minimum required distributions until they retire unless they are 5% owners.)

- The Act makes an additional exception to the 10% early withdrawal penalty available for qualified childbirth or adoption expenses up to $5,000.

- The Act also allows individuals over age 70½ to make traditional IRA contributions.

Changes to Plan Administration

The SECURE Act also makes a number of significant changes to the way retirement plans are administered. In part, effective January 1, 2020:

- The Act makes the following changes with respect to safe harbor plans <u>that use nonelective safe harbor contributions</u>:
  - Eliminates the annual safe harbor notice requirement.
  - Permits plans to become a safe harbor plan any time prior to 30 days before the plan year-end;

  - Permits amendments establishing a new safe harbor plan within 30 days before the close of the plan year in limited circumstances where the nonelective contribution is at least 4% of compensation.

- The Act requires defined contribution plans to include "lifetime income disclosures" in participant statements annually (or provide a separate statement doing so) that show the value of the participant's accrued benefit as a lifetime income stream. This provision will not become effective until the DOL issues regulations and a model disclosure.

- Under prior law, qualified automatic contribution arrangements ("QACAs") could not have a default automatic enrollment rate higher than 10%. The Act increases the maximum default automatic enrollment rate to 15%.

- The Act permits active participants in 403(b) plans and governmental 457(b) plans, as well as certain qualified defined contribution plans, to make a direct trustee-to-trustee transfer of lifetime income investments to another qualified plan or IRA if the plan no longer authorizes investments in a lifetime income investment.

Safe Harbor for Selecting Lifetime Income Annuity Providers

The Act also creates a safe harbor, effective immediately, for plan fiduciaries selecting annuity providers for guaranteed retirement income contracts. This safe harbor makes it easier for plans to offer lifetime income benefit options. Generally, in order to take advantage of the safe harbor, plan fiduciaries must:

- Engage in a thorough, objective, and analytical search to identify insurers, considering the ability of the insurers to satisfy the contract and the cost associated with the contract.

- Obtain representations from the insurer that it is licensed to offer guaranteed retirement income contracts, that it is in good standing with regulators based on specified criteria, that it undergoes regular financial examinations (at least every five years), and that the insurer will notify the plan fiduciary of any changes affecting its representations.

Changes Affecting 529 College Savings Plans

The SECURE Act will impact Code Section 529 plans in two significant ways:

- The Act expands the definition of "qualified higher education expense" to include expenses a beneficiary incurs for fees, books, supplies or equipment required to participate in an apprenticeship program, provided the program is registered with the Department of Labor.

- The Act allows 529 plan assets to be used to pay qualified education loans. Previously, 529 assets could not be used to pay such loans. The assets of a 529 account may be used to pay the loans of the beneficiary or the beneficiary's siblings (including step-siblings). Distributions up to $10,000 per individual will be considered a "qualified higher education expense" if used to pay education loans. This is a lifetime, not annual, limit. These changes will apply to distributions taken after December 31, 2018.

Other SECURE Act Changes

In addition to the changes described above, the Act creates and expands certain tax credits designed to incentivize small business adoption of retirement plans, creates a safe harbor for selection of annuity providers

for guaranteed retirement income contracts, makes changes to existing law designed to facilitate the creation of pooled retirement plans, and increases penalties for employers who fail to timely file Forms 5500.

Year-End Appropriations Act Also Repeals Certain Affordable Care Act Taxes

The year-end appropriations act also includes the repeal of three taxes enacted in connection with the Affordable Care Act:

- The excise tax on high-cost employer-sponsored health coverage, commonly referred to as the "Cadillac tax" (effective January 1, 2020);
- The annual fee imposed on health insurance providers (effective January 1, 2021); and
- The medical device excise tax (effective with respect to sales of medical devices after December 31, 2019).

Next Steps

In light of the potentially significant operational changes required by the SECURE Act, plan sponsors will need to work in close coordination with their recordkeepers and document vendors to decide what operational changes to make and keep good records of those changes for when plan amendments are required.

If you have any questions regarding the Act or if you would like assistance assessing the impact of the Act on your plans, including any desired changes to your plans' design, please contact a member of our Employee Benefits Practice Group listed below. For more information concerning our employee benefits practice, please visit us at www.KutakRock.com.

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