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The Secure Act of 2019: What Retirement Plan Sponsors Need to Know

The Setting Every Community Up for Retirement Enhancement Act of 2019 (Act) was signed into law on December 20, 2019. The Act represents the first comprehensive legislation impacting retirement plans in over a decade and includes provisions affecting retirement plan sponsors and individuals. This information memo addresses some of the more important provisions of the Act that impact retirement plan sponsors. Bond recently issued an information memo regarding the Act's impact on estate planning, which can be accessed here.

Required Minimum Distribution Date Age Raised. Prior to the Act, the required minimum distribution date was generally the later of April 1 of the year following the year the participant or IRA owner reached 70½ or the date of retirement (an exception to this rule applied for 5% owners). This required minimum distribution date has not been modified in over fifty years to account for increases in life expectancy. Effective for distributions required to be made after December 31, 2019, and for individuals who attain age 70½ after that date, the Act raises the required minimum distribution age to 72. Individuals who attained age 70½ in 2019 (i.e., prior to the effective date of the Act) are still required to commence required minimum distributions by April 1, 2020.

Coverage for Long-Term Part-Time Employees in 401(k) Plans. Under current law, plan sponsors may include a requirement that an employee must work at least 1,000 hours in a measurement period to be eligible to make elective deferrals to a 401(k) plan. In an effort to provide retirement savings access to long-term part-time employees, the Act provides that a 401(k) plan must allow an employee to make elective deferrals to the plan, if the employee has worked at least 500 hours in each of three consecutive plan years. Importantly, the Act does not require that such long-term part-time employees be eligible for purposes of employer nonelective or matching contributions under a plan (i.e., such employees can still be excluded by virtue of failing to complete 1,000 hours in a plan year). This change is generally effective for plan years beginning after December 31, 2020; however, the first year during which the 500 hour requirement will be measured does not commence until January 1, 2021. This change does not apply to collectively bargained plans.

Provisions to Ease the Creation of Pooled Retirement Plans of Unrelated Employers. Prior to the Act, it was possible for unrelated employers to create multiple employer plans (MEPs) for the benefit of their respective employees, if the employers had a commonality of interest. The Act eliminates the commonality of interest requirement and allows unrelated employers to establish "pooled plans" or "open MEPs" for the benefit of their employees, if certain requirements are satisfied. In addition, the Act eliminated the so-called "one bad apple" rule that previously resulted in disqualification of the entire MEP, if a single employer in the plan failed to satisfy a qualification requirement. These changes are effective for plan years beginning after December 31, 2020.

"Safe-Harbor" 401(k) Plan Provisions. Under the Act, employers who maintain an automatic enrollment "safe harbor" 401(k) plan (i.e., a qualified automatic contribution arrangement) may generally increase the maximum automatic contribution percentage limit to 15% of eligible compensation (prior to the Act, the maximum automatic contribution percentage was 10%). However, for the first deemed election year, the cap remains at 10%. This change is effective for plan years beginning after December 31, 2019.

Additionally, effective for plan years beginning after December 31, 2019, the requirements governing safe harbor 401(k) plans that utilize a nonelective contribution of at least 3% of compensation have been simplified by eliminating the annual safe harbor notice requirement. Further, the Act allows a 401(k) plan to be amended to add a safe harbor nonelective contribution design up to 30 days prior to the end of the plan year. An amendment is allowed to add a safe harbor feature after that time, if the amendment provides a nonelective contribution of at least 4% of compensation for all eligible employees and the plan is amended no later than the last day for distributing excess contributions for the plan year (typically this date is the close of the following plan year).

Withdrawals for a Qualified Birth or Adoption Permitted Without Penalty. The Act added an in-service withdrawal option with respect to applicable eligible retirement plans (e.g., 401(k) plans and 403(b) plans) in the case of a "qualified birth or adoption." Plan distributions of up to $5,000 used to pay for expenses related to a qualified birth or adoption are penalty-free if taken within a year of the birth or adoption. Prior to the Act, such distributions would normally be subject to a 10% excise tax if taken before the participant attained 59½. Because the $5,000 limit is applied on an individual basis, it is possible for both parents to elect a distribution on account of a qualified birth or adoption. Further, a participant who receives a qualified birth or adoption distribution may recontribute the amount to the plan and have that amount treated as an eligible rollover distribution that is transferred back to the plan. Qualified birth and adoption distributions are permitted for distributions made after December 31, 2019.

New Tax Credits For "Small Employers". The Act contains two provisions to encourage "small employers" (generally, employers with no more than 100 employees) to offer employer-provided retirement plans. First, the Act increases the small employer pension plan startup credit that is available to certain small employers to the greater of: (1) $500, or (2) the lesser of (a) $250 for each eligible employee who is non-highly compensated, or (b) $5,000. In addition, the Act creates a new tax credit of up to $500 per year for employers that establish qualifying plans (e.g., 401(k) plans and SIMPLE IRA plans) that include automatic enrollment arrangements. This credit is in addition to the existing start-up credit. The tax credits are effective for tax years beginning after December 31, 2019 and apply for up to three years.

Closed Defined Benefit Plan Nondiscrimination Rules Modified. The Act modifies the nondiscrimination rules that apply to defined benefit plans that are no longer open to new participants to permit existing participants to continue to accrue benefits. In many cases, such plans are not discriminatory at the time of the freeze but may fail to satisfy the applicable nondiscrimination requirements as the result of workforce attrition. This change is designed to protect the benefits of older and longer-service employees who continue to be eligible under these closed plans. This provision became effective upon enactment of the Act (December 20, 2019).

Provisions Relating to Annuities. The Act includes several provisions relating to lifetime income investments (i.e., annuities), including the following:

- **Portability of Lifetime Income Options.** Effective for plan years beginning after December 31, 2019, the Act provides that if a lifetime income investment is no longer authorized to be held as an investment option under the plan, the plan may make a direct trustee-to-trustee transfer to another eligible retirement plan of the lifetime income investment or distribute the lifetime income investment in the form of a "qualified plan distribution annuity." The distribution must be made within the 90-day period ending on the date when the lifetime income investment is no longer authorized to be held as an investment option under the plan.
- **Easing of Requirements Necessary for Defined Contribution Plans to Offer Lifetime Income Streams.** Effective December 20, 2019, the Act creates a new safe harbor to satisfy ERISA's prudence requirement with respect to the selection of insurers for a guaranteed retirement income contract. If the safe harbor requirements are satisfied, a fiduciary is protected from liability for any losses that may result to participants and beneficiaries due to an insurer's inability to satisfy its financial obligations. The safe harbor is designed to help mitigate plan fiduciary concerns regarding adding annuities to a defined contribution plan investment menu.

Defined Contribution Plan Benefits Statements Required to Contain Lifetime Income Stream Disclosures. The Act requires defined contribution plan benefit statements to disclose, at least once annually, the amount of the lifetime income stream that the participant's plan account balance could provide. The Act directs the U.S. Department of Labor to develop a model disclosure for this purpose. The disclosure requirement is delayed until the first benefit statement that is provided more than 12 months after the issuance by the DOL of regulations and the model disclosure.

Plan Loans. Effective on the enactment date (December 20, 2019), plans are prohibited from making plan loans via credit cards or similar arrangements. The Committee Report for the Act indicates that the intention behind this change is to preserve retirement savings that may be depleted by the frequent use of a credit card loan for routine and small purchases.

Adoption Date for Qualified Plans. Prior to the Act, in order for a qualified plan to be deemed maintained for the tax year, the plan was required to be adopted by the last day of the tax year. For plan years beginning after December 31, 2019, a qualified plan may be deemed maintained for the tax year if the plan is adopted prior to the due date for the tax return for such tax year. This change affords employers additional time and flexibility to adopt a new plan.

In Kind Distributions Upon Termination of 403(b) Plan. The Act directs the Secretary of Treasury to issue regulations providing that if an employer terminates a 403(b) plan that includes a custodial account, the plan administrator or custodian may distribute an individual custodial account to a participant or beneficiary to effectuate the termination. The individual custodial account will be maintained on a tax-deferred basis if the account adheres to the Code Section 403(b) requirements. This change will be welcome for plan sponsors who have historically faced compliance risks in connection with terminating 403(b) plans that are funded by individual custodial accounts. Once issued, the guidance will apply retroactively for taxable years beginning after December 31, 2008.

Penalties. Effective for required filings beginning after December 31, 2019, the Act modifies the penalties imposed on plan administrators for failure to file certain retirement plan returns. The new penalty for a failure to file a Form 5500 is $250 a day, not to exceed $150,000. The new penalty for failing to file an annual registration statement identifying participants who have separated from service with a vested benefit (IRS Form 8955-SSA) is $10 per participant, not to exceed $50,000.

Next Steps

Plan sponsors should begin to assess the impact of the Act now, as a number of the Act's provisions are effective in 2020. While the Act provides that, for most plans, amendments are not due until the last day of the first plan year beginning on or after January 1, 2022, plan sponsors will need to address operational compliance issues with respect to the Act's requirements before that date. The timing of employee communications and updates to summary plan descriptions also will need to be considered.

If you have any questions about this memorandum, or if you need assistance with the implementation of the Act, please contact any member of our Employee Benefits and Executive Compensation Practice Group listed below.

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