Client Alert

January 2020

Sweeping Changes to Retirement Plans and IRAs Implemented by the Secure Act

Overview:

The passing of the Setting Every Community Up for Retirement Enhancement Act of 2019 (the SECURE Act or the Act) at the end of 2019 provides for significant changes to retirement plans and IRAs. In fact, we haven't seen such extensive changes to retirement plans in one piece of legislation since the passing of the Pension Protection Act in 2006. This article highlights key changes made by the SECURE Act to retirement plans and IRAs that have immediate impact for this year. We will be sending additional updates regarding other changes made by the Act and other recent welfare plan legislation.

Action Required:

This Act will require action on the part of plan sponsors with respect to administrative changes, notification to participants and amendments to their plans. The changes described below can be implemented starting this year. With some exceptions identified below, plan sponsors have until December 31, 2022, to adopt a retroactive amendment to reflect the operational changes. Plan sponsors should discuss these changes (and others not mentioned here) with their ERISA attorneys to ensure compliance. If you would like to discuss this, please reach out to any of the Hunton Andrews Kurth attorneys listed below.

1. Change to Post-Death Distribution Rules for Qualified Defined Contribution Plans and IRAs Starting in 2020.

- <u>What has changed</u>: The Act extended the timeframe within which payments under defined contributions plans and IRAs may be made following a participant's death from 5 to 10 years. In addition to surviving spouses, the Act provides for extended payments over the life of additional "eligible" beneficiaries. These include surviving children under age 18, chronically ill or disabled individuals as defined in the Code and any designated individuals who are not more than 10 years younger than the deceased participant.

- <u>Our comment</u>: This change generally limits the period in which qualified defined contribution plans and IRAs must begin and complete distributions to "ineligible" beneficiaries in the event of a participant's death. This means that many beneficiaries will now be required to complete such distributions over a shorter period of time. Plan sponsors of qualified retirement plans (e.g., 401(k) and pension plans) will want to review the minimum required distribution provisions of their plan documents to assess whether an amendment will be appropriate. This change applies to participant deaths starting in 2020.

2. Ability to Make IRA Contributions After Age 70½ Beginning 2020.

- <u>What has changed</u>: Individuals were not allowed to make contributions to IRAs after reaching age 70½. The Act has eliminated that restriction.

- Our comment: This provision (along with the adjustment in the minimum required distribution age from 70½ to 72 discussed below) is one of the several features the Act allows individuals to coordinate tax planning and defer taxation.

3. Delayed Minimum Required Distributions From Age 70½ to 72 Beginning 2020.

- What has changed: Under the previous minimum required distribution requirements, qualified plans and IRAs were required to begin distributions for individuals who have turned age 70½ (and terminated employment for company-sponsored retirement plans). These amounts were not rollover eligible and failure to meet this requirement resulted in a 50 percent excise tax to the individuals. The Act delays the age by which these distributions must begin to age 72 beginning in 2020 for participants who reach age 70½ after December 31, 2019.

- Our comment: One of the most common failures for qualified plans is the failure to timely make minimum required distributions. The delay in having to start minimum required distributions may help compliance with this rule and helps individuals with tax planning in order to delay the required receipt of taxable payments. Because the minimum required distribution rules continue to be a major issue in Department of Labor audits, we strongly advise plan sponsors to carefully review their processes around these rules even in light of the provisions of the Act.

4. Ability to Implement Nonelective Safe Harbor Provision Mid-Year Beginning 2020.

- What has changed: The IRS has historically limited the ability of a 401(k) plan sponsor to implement safe harbor provisions during the plan year. Generally, a plan sponsor has been limited to implementing safe harbor provisions only at the beginning of a plan year, with some exceptions. The Act now allows a 401(k) plan sponsor to amend their plan to make a safe harbor nonelective contribution: (1) no later than 30 days prior to the end of the plan year; or (2) after that date and before the last day for distributing excess contributions for the plan year, so long as the contribution is at least 4 percent of compensation. The Act also eliminates the safe harbor notice requirement for nonelective contributions.

- Our comment: This allows 401(k) plan sponsors greater flexibility in implementing a safe harbor plan. Plan sponsors will now be able to implement a safe harbor nonelective contribution provision toward year-end (or even after year end) when they typically decide whether to make such contributions. Plan sponsors would need to timely adopt an amendment to implement this feature.

5. Increase in the Maximum Automatic Deferral Percentage for Qualified Automatic Contribution Arrangements (QACA) Beginning 2020.

- What has changed: The Act increases the maximum allowable automatic contribution percentage under a QACA from 10 percent to 15 percent.

- Our comment: Retirement professionals generally recommend an annual savings of 15 percent for individuals. Plan sponsors that want to encourage increased employee contributions and savings may want to implement a QACA (or, if they already have a QACA, increase the automatic escalation provision contribution percentage) to encourage increased employee contributions and savings for employees for participants to help employees get closer to that goal. This change would require a plan amendment within the year it is implemented.

6. Penalty-Free Withdrawals from Defined Contribution Plans and IRAs in the Case of Birth of a Child or Adoption Beginning 2020.

- What has changed: Generally, if a participant elects a distribution from a retirement plan prior to age 55 and termination of employment, the distribution is subject to a 10 percent early distribution penalty tax. Starting in 2020, if a participant elects a "qualified birth or adoption distribution" of $5,000 or less within 12 months of a birth or adoption, the distribution is not subject to the 10 percent penalty. A qualified birth or adoption distribution may later be recontributed to the plan if the participant desires to do so.

- Our comment: The costs for a new child, especially adoption costs, can be significant and providing for a penalty-free distribution of $5,000 or less can help assist parents in dealing with these costs. This change will require an amendment.

7. Increased penalties for Retirement Plan Returns and Notices Due after December 31, 2019.

- What has changed: The potential penalties for noncompliance with certain retirement plan return and notice requirements under the Tax Code have increased significantly. For example, the penalty for failure to timely file the annual Form 5500 has increased from $25 per day (capped at $15,000 per year) to $250 per day (capped at $150,000).

- Our comment: These increased penalties make it even more imperative for plan sponsors to be diligent in meeting the deadlines for required notices and filings. We have developed summaries of the various requirements, which may be of assistance to you, and, in the event of a late or missed filing, we can assist you in filing an application with the DOL under the delinquent filer program that can substantially mitigate the potential risk of penalties.

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