ADVANCED PLANNING

April 2022

Insights & Ideas

On to the Senate: House passes "SECURE 2.0"

On Tuesday March 29, the House of Representatives passed the *"Securing a Strong Retirement Act of 2022",* also known as "SECURE 2.0". Secure 2.0 builds on the SECURE Act, which was passed in December 2019, to improve retirement savings opportunities for workers. The House passed the bill with a vote of 414 to 5, so there is a good chance that the Senate will show equally bipartisan support for the bill.

Here are some highlights of SECURE 2.0:

Expanding automatic enrollment in retirement plans

SECURE 2.0 would require 401(k) and 403(b) plans to enroll automatically plan participants once they are eligible to participate (although employees could opt out). Enrollees would initially contribute at least 3% of salary, but not more than 10%. Each year after enrollment, contributions would increase by 1% until a goal of 10% is reached. Exceptions exist for businesses with 10 or fewer employees, businesses less than 3 years old, and church and government plans.

Credit for small employer pension plan startup costs

For employers with up to 50 employees, the startup credit is increased from 50% to 100%. Generally SECURE 2.0 provides an additional credit of up to $1,000 per employee based on the amount contributed by the employer on behalf of the employee. The full credit is available to employers of 50 or fewer employees and phased out for employers of 51 to 100 employees.

Increase in age for beginning date for required distributions

Under current law, taxpayers must begin distributions from retirement accounts at age 72. SECURE 2.0 would increase the required beginning date through a phased-in approach. Starting on January 1, 2023, the required beginning date would be age 73 (for individuals who attain age 72 after December 31, 2022, and age 73 before January 1, 2030); then increased to 74 starting on January 1, 2030 (for individuals who attain age 73 after December 31, 2029, and age 74 before January 1, 2033); and to 75 starting on January 1, 2033 (for individuals who attain age 74 after December 31, 2032).

Indexing and increasing catch-up contributions

The Act would index the IRA catch-up contribution limit to inflation in years after December 31, 2023. The current $6,500 limit on catch-up contributions to a retirement plan ($3,000 for SIMPLE plans) would be increased to $10,000 ($5,000 for SIMPLE plans) for individuals age 62, 63, and 64 in tax years after December 31, 2023. The higher catch-up limits would not be available at age 65 or above. The contribution limits would be indexed for inflation.

Roth contributions allowed for SIMPLE and SEP IRAs.

SECURE 2.0 will allow SIMPLE IRAs to accept Roth contributions. The Act will also allow employers to offer employees the ability to treat employee and employer SEP contributions as Roth in whole or in part. Effective for tax years beginning after December 31, 2022.
Under current law, catch-up contributions to a qualified retirement plan may be made as either pre-tax or Roth contributions. Effective December 31, 2022, all catch-up contributions would be designated Roth contributions. This proposal would not apply to Simple IRA or SEP.
Under current law, employer matching contributions to a qualified retirement plan must be made on a pre-tax basis. Effective after the date of enactment, employers may offer participants the option to receive matching contributions as designated Roth contributions. An employer matching contribution that is a designated Roth contribution would not be excludable from gross income.

Multiple employer 403(b) plans

The Act allows charities, educational institutions, and non-profits to participate in multiple employer plans (MEPs), including relief from the "one bad apple" rule, meaning that the violations of one employer do not affect the treatment of compliant employers. For tax years effective after December 31, 2022.

Treatment of student loan payments as elective deferrals for matching purposes

Employees who have difficulty saving for retirement due to student loan debt may receive lower matching contributions from employers. SECURE 2.0 will allow those employees to receive higher matching contributions under a 401(k), 403(b) or SIMPLE IRA to the extent they make "qualified student loan payments". A qualified student loan payment under SECURE 2.0 generally includes payments of indebtedness incurred by the employee solely to pay qualified higher education expenses of the employee with some limitations.

Qualifying longevity annuity contracts (QLACs)

SECURE 2.0 repeals the 25% premium limit imposed under the original QLAC regulations. It does not repeal the dollar limitation (currently $145,000). The ACT also makes technical adjustments to improve the availability of joint-and-survivor annuity benefits, and to allow for a free-look period of up to 90 days after the purchase of a QLAC.

Reduction of excise tax for failure to make required distributions

SECURE 2.0 reduces the excise tax for failure to take required distributions from 50 percent to 25 percent. Additionally, if the failure to take a distribution is corrected in a "timely" manner, the tax is reduced from 25% to 10%. The timely "correction window" would end on the earlier of the date the IRS initiates an audit or demands payment of the tax, and last day of the second taxable year after the year in which the tax is imposed.

One-time election for Qualified Charitable Distribution to be paid to a split-interest entity

The Qualified Charitable Distribution (QCD) rules are expanded to allow for a one-time $50,000 distribution to a charity through a split-interest entity, including charitable gift annuities, charitable remainder unitrusts and charitable remainder annuity trusts.

SECURE 2.0 will also index the $100,000.00 annual limit on QCDs.

Penalty-free withdrawals from retirement plans in case of domestic abuse

SECURE 2.0 will allow plans to permit participants that self-certify that they experienced domestic abuse to withdraw the lesser of $10,000 or 50% of the participant's account. This distribution would not be subject to the 10% early distribution tax. Additionally, the tax on these distributions can be paid over 3 years and the amounts recontributed to the retirement plan would not be taxable and treated as rollovers.

Improving coverage for part-time workers

SECURE 2.0 reduces the three-year (with 500 hours of service per year) rule of the SECURE Act to a 2-year rule, effective for plan years beginning after December 31, 2022.

Removing barriers to the use of life annuities in qualified plans and IRAs

SECURE 2.0 removes barriers to the use of annuities in qualified plans and IRAs by exempting certain annuity features, such as an annual inflation adjustment, from actuarial tests that would otherwise prohibit their use.

Expand age 50 "qualified public safety employee" exemption to 10% penalty

Currently distributions to "qualified public safety employees" may make distributions from governmental retirement plans as early as age 50 without paying the 10% early distribution tax. SECURE 2.0 would expand this exemption to private-sector firefighters.

Change to start date of statute of limitations for the excise tax on excess contributions

Currently the statute of limitations on prohibited transaction, excess contributions and RMD failures starts on the date a return is filed for the violation. SECURE 2.0 provides that the start date begins when the taxpayer files an individual tax return for the year of the violation (or the date that such return would have been due in the case of a person not required to file a return).

Conclusion

SECURE 2.0 takes substantial steps towards increasing the impact of Roth balances in retirement planning. By expanding Roth availability to SIMPLE IRAs and SEP IRAs and providing for the Roth treatment of employer matching contributions and catch-up contributions, retirees may see substantially larger tax-free cash flows in retirement.

Custodians and plan administrators will have a substantial workload in front of them in order to adapt to all of the provisions of SECURE 2.0: changes to account holders' Required Beginning Dates, new exceptions to the 10% additional tax , procedures for enrolling new employees, and more will all increase administrative burdens.

The bill is now in the hands of the Senate. We will have to wait to see what changes may be proposed, or if the bill will pass through substantially unchanged.

For questions about SECURE 2.0 or strategies to consider when helping clients plan for retirement and leaving a legacy, please contact Prudential's Advanced Planning team at 800-800-2738, Option 4 for life insurance support.

Prudential