Rael & Letson

Summary of Secure 2.0 Act

For Multiemployer Defined Contribution Plans

On December 29, 2022, the SECURE 2.0 Act was signed into law as part of the Consolidated Appropriations Act, 2023. The new law includes significant changes to retirement rules that primarily focus on expansion of retirement savings opportunities and access in Defined Contribution Plans ("DC Plans"). Following is a high-level summary of the key Secure 2.0 provisions affecting Multiemployer DC plans along with our observations and conclusions.

Provisions Potentially Affecting All ME DC Plans

Secure 2.0 contains several changes that could affect multiemployer Money Purchase and Profit Sharing ("401(k)") DC Plans. These changes fall into three categories:

- Distributions/Access
- Disclosure
- Administration

Distributions/Access

A primary goal of Secure 2.0's retirement changes is to enhance distribution flexibility and asset access for plan participants. The following changes have been made to improve distribution flexibility and participant access to funds:

Deferring the Required Beginning Date

Participants are required to receive a minimum distribution from qualified retirement plans at their Required Beginning Date. This date is generally April 1st of the calendar year following the calendar year in which a legally defined age is attained. Plans can defer this date for those that are not 5% owners of their companies to their age at employment termination. The amount of the distribution for DC plans is the account balance divided by a legally defined age-based factor.

The 2019 Secure Act extended the attained age used to determine a participant's required beginning date from 70-1/2 to 72 for those born on or after July 1, 1949. Secure 2.0 further extends the attained age to 73 starting in 2023 for those born on or after January 1, 1951, and before January 1, 1960. Starting in 2033, the attained age is increased to age 75 for those born on or after January 1, 1960.

Financial penalties for late minimum required distributions are the responsibility of the individual but plans can have disqualification risk for not complying with the minimum required distribution regulations. Secure 2.0 reduces the individual penalties for tax years beginning in 2023 from 50% to 25% of the late distribution and to 10% if corrected within a window period that could be as long as 2 years after the end of applicable tax filing year.

▶ **Rael & Letson Observations:** Many current demographic projections forecast a shortage of workers in the next 10-20 years. Phased retirement is also gaining in popularity. As a result, deferring required distributions to a later age adds desired flexibility for some people. There will be no mandatory age-based distributions in 2023 and none in 2033 and 2034 as a result of the age jumps. In 2023, plans should consider how they would like to implement these changes. With these age extensions, plans may not wish to increase mandatory distribution start ages and/or permit in-service distributions at earlier ages.

Permitting Emergency Savings Access

Secure 2.0 contains two voluntary sponsor actions to make available funds for emergency access. The first law change permits plans starting in 2024 to establish separate emergency participant accounts called "Pension Linked Emergency Savings Accounts" where non-highly compensated participants (generally less than $145,000 in 2022 for 2023) can make after-tax Roth contributions as long as the emergency account does not exceed $2,500 or some lesser plan-defined amount. Employer contributions are not allowed to be made to these emergency accounts. Also, these emergency accounts are to be invested safely with a state or federally insured financial institution and must permit withdrawal from the emergency account at least once per month. Finally, they are portable to other Roth accounts in the Plan and can be paid in cash at employment termination. The second law change allows plans to permit participants to receive one distribution per year from their DC account for unforeseen emergency needs starting in 2024. These emergency distributions from existing accounts cannot exceed $1,000. Distribution rules for these existing account distributions are similar to the Cares Act Coronavirus CRDs in allowing participants to self-certify to Emergency need.

Both types of emergency distributions, along with any plan distributions permitted for domestic abuse (up to $10,000), terminal illness, or Long-term care funding ($2,500 per year), are not subject to the 10% early distribution penalty tax starting in 2024. Income taxation of emergency distributions from existing accounts is permitted to be spread over 3 years and can be avoided by paying back the taxable portion owed in each year.

▶ **Rael & Letson Observations:** "Leakage" of potential retirement assets is a significant challenge to retirement readiness. Loans, Hardship withdrawals and distributions at termination already contribute heavily to the loss of potential retirement assets. Adding Pension Linked Emergency Savings Accounts will likely lead to further leakage of potential retirement assets. Furthermore, administration will likely be complex and costly. As a result, it is unlikely that Multiemployer DC Plans will elect to establish them. Emergency withdrawals that are permitted by plans from existing accounts would not be large enough to address most emergency issues and could be tempting to some members to use for non-emergency purposes. Multiemployer DC Plans considering adding emergency fund access should thoroughly evaluate the pros and cons of adoption for their members.

Increasing the Mandatory Cash-out Threshold

For many years, plans have had the option to cash out all participants' accounts in one lump sum when the balance is less than $5,000. Secure 2.0 increases this Mandatory plan directed lump sum cash out limit to $7,000 starting with plan years beginning in 2024.

▶ **Rael & Letson Observations:** Plans have discretion on whether to impose Mandatory cash outs for participants who terminate with small account balances. The decision to apply the Mandatory cash out provision in a Multiemployer DC Plan is one that should be revisited with the increase in the cash out limit from $5,000 to $7,000. Most plans have immediate vesting so small accounts are often prevalent. Trustees should re-evaluate whether a Mandatory cash out provision results in asset leakage by examining rollover patterns and whether this is a concern for retirement readiness.

Permitting Auto-Portability

Starting December 29, 2023, Secure 2.0 allows DC plans to contract with an “automatic portability provider” to automatically roll over any amounts from provider established IRAs to the contracted DC Plan absent direction otherwise from the affected DC Plan participant. Plan participants would maintain control in two ways. First, by controlling what is rolled into the provider established IRA. Second, by the ability to opt out of the automatic rollover provision.

- **Rael & Letson Observations:** This will help build DC plan assets and could help reduce participant expenses for DC operations. Also, asset consolidation may help DC Plans reduce lost participant searches. Auto-portability, however, will add operational burden and cost to effectively comply.

  Multiemployer plan participants naturally have some auto-portability when they move between employers in the plan. Also, most Industries have National reciprocity that permits contributions in another jurisdiction to be sent to the participant’s home fund. These factors coupled with the fact that it is common for participants to return to the Industry and maintain plan account balances may discourage some multiemployer sponsors from adopting auto-portability for their Multiemployer DC Plans. For others, analysis may project that auto-portability will ultimately reduce participant expense charges following a strong communications campaign and participant action to roll over existing IRAs into the automatic portability provider IRA (thus triggering the automatic rollover into the DC Plan).

Establishing a National Retirement Lost & Found Registry

By the end of 2024, the DOL, with assistance from the IRS, must establish a National lost and found registry to that will contain plan contact information and participant data for lost participants. Plans will be required to initially submit and refresh thereafter any changed plan administration contact information. In 2025, information on terminated vested participants will need to be provided annually so that participants do not lose track of their retirement assets. This information is required to be safely stored by the DOL and is only to be used to accurately connect the participant or beneficiary to the plan.

- **Rael & Letson Observations:** Lost participants have been an issue for some time and multiemployer plans are not immune. This will require some initial and ongoing support from all DC plans in 2024 and beyond.

Disclosure

Secure 2.0 requires that the DOL, IRS and PBGC review and present a coordinated report to Congress by the end of 2025 that addresses the effectiveness of the reporting and disclosure requirements and includes recommended changes. To assist the government agencies, plans may be contacted to provide survey responses. In addition, there are two other changes that may affect disclosure processes for some Multiemployer DC Plans.

Performance Benchmarks for Asset Allocation Funds

For DC Plans that have mixed asset class investment alternatives, such as target date funds, for participant investment direction, Secure 2.0 requires the DOL to provide regulations before the end of 2024 clarifying that administrators may use a benchmark that is a blend of different broad-based security market indices in meeting investment performance disclosure requirements to participants.

Rael & Letson Observation: Plans using a benchmark to satisfy performance disclosure requirements must comply with a set of reasonable disclosure standards to assure that the benchmarks are accurate and current.

Benefit Statements

Secure 2.0 requires that DC Plan sponsors provide at least one benefit statement per year in paper form to plan participants starting in 2026.

Rael & Letson Observation: Paper statements are still the practice in the Multiemployer DC Plan industry so few plans will need to consider this change requiring a switch from electronic to paper once per year.

Administration

Two changes relevant to Multiemployer DC Plans were made under Secure 2.0 that are targeted to ease administrative burden and reduce plan operation cost.

Overpayments

For overpayments after December 29, 2022, retirement plan fiduciaries do not have to seek recovery of all or a part of any "inadvertent benefit overpayment" from a participant or beneficiary that is not "culpable", or from any plan sponsor of or employer to an individual account plan. If trying to collect an inadvertent benefit overpayment from a participant or beneficiary, plan fiduciaries are no longer permitted to charge interest and can now collect no more than 10% in any year. Generally, collection of future inadvertent benefit overpayments is limited to those that occurred within a 3-year period prior to discovery.

Rael & Letson Observations: Inadvertent benefit overpayments in Multiemployer DC Plans are uncommon and when present usually involve Qualified Domestic Relations Orders or rollovers. Attempting to collect for inadvertent benefit overpayments in DC plans may still be warranted. Counsel should advise when Individual Account Overpayments are waived and funded by participant expense charges or from forfeitures.

EPCRS Corrections

The Employee Plans Compliance Resolution System ("EPCRS") is the most efficient and effective way to self-correct inadvertent eligible plan operational failures before they are brought to the plans attention by the DOL. A notable change is to now permit correction of 401(k) Loan operational failures through ERCRS in satisfaction of all previous more onerous and costly correction methods. The IRS is required to update existing guidance under Revenue Procedure 2021-30 before the end of 2024 to update for Secure 2.0 changes.

Rael & Letson Observations: Identifying and expeditiously self-correcting any Operational errors through EPCRS is a best practice to avoid more time-consuming and costly corrective actions. The Secure 2.0 expansions that cover more failures are a welcome change for DC Plans.

Provisions Potentially Affecting Profit Sharing Plans

Secure 2.0 made some significant changes to laws intended to boost retirement savings in profit sharing plans that may have the opposite effect for Multiemployer DC Plans with 401(k) pre-tax deferral features.

Require Auto-Enrollment and Auto-Escalation for New 401(k) Features

Secure 2.0 requires plans with 401(k) features established on or after December 29, 2022 to require auto-enrollment for all participants at a level that is at least 3% of compensation. Furthermore, for participants that do not override the default enrollment level, default levels must increase each year by 1% until the autoenrollment level reaches at least 10% (plans can decide to go to as high as 15%).

▶ **Rael & Letson Observations:** As a result of conversions of Money Purchase Plans and some new plan startup, about 50% of Multiemployer DC Plans are Profit Sharing Plans with about ½ of those allowing 401(k) pre-tax deferrals. 401(k) plans in the multiemployer industry usually have a menu of flat dollar employer deferral options but some plans have a menu with % of pay alternatives. Auto-Enrollment—establishing a default pre-tax employee contribution level that an employee must affirmatively change—is unusual for Multiemployer DC Plans given the nature of participant movement between employers.

Auto-enrollment is largely a non-starter for Multiemployer 401(k) Plans given the very challenging administrative burden and compliance challenges that result from participants moving between employers. The law change is unclear as to whether auto-enrollment will be required for new bargaining units, non-bargaining agreements and/or employers that may join after Secure 2.0 enactment. At best, this provision is likely to stunt DC plan growth in the Multiemployer Industry; at worst, it may result in some plans eliminating 401(k) features or terminating 401(k) plans.

Change Catch-Up Contribution Opportunities

401(k) pre-tax deferrals are subject to an annual dollar limit that is indexed with CPI inflation. For 2023, this limit is $22,500 without “catch-up” contributions and $30,000 with catch-up contributions. Catch-up contributions are 401(k) pre-tax deferrals designated or recharacterized for those who are age 50 by the end of the year (the 2023 catch-up contribution limit is $7,500). Starting in 2025, Secure 2.0 increases the catch-up contribution limit for those who are ages 60-63 to be the greater of $10,000 or 1.5 times the age 50 limit. However, starting in 2024, all catch-up contributions must be Roth (after-tax) contributions for participants who are Highly Compensated Employees (“HCEs”). For 2023, HCEs are generally participants with 2022 Compensation of $145,000 or more.

▶ **Rael & Letson Observations:** Roth contributions can be attractive for younger participants as the investment earnings are not subject to tax. However, the requirement that catch-up contributions be Roth contributions for HCEs complicates the administration for multiemployer plans with catch-up contributions starting in 2024. Because Roth contributions are after-tax contributions, many employers and plan administrators (including recordkeepers) would now have to adapt their processes and systems to track a new type of contribution for HCEs. This burden may lead Boards to discontinue catch-up contributions for HCEs or for all participants, resulting in reduced savings for some multiemployer participants. Given that this change increases tax revenue, we unfortunately expect that modifications to this provision are unlikely.

Permit Self-Certification for Hardship Distribution Qualifications

Hardship distributions of employee contributions in profit sharing plans, including those with 401(k) pre-tax deferral features, are permitted if a plan participant satisfies the statutory qualification standards--the minimum amount required to meet an immediate and heavy financial need from an unforeseeable emergency that cannot be provided from another source--and self certifies that they do not have access to finances that would allow them to address the statutory financial hardship. Prior to Secure 2.0, plans were tasked with approving or denying requests based on purported financial need and participant financial documentation.

For Hardship requests during plan years beginning in 2023, Secure 2.0 extends the Cares Act Coronavirus CRD self-certification process to permit plans with Hardship distributions to pre-approve self-certification by certain participants that the Hardship request meets the statutory qualification standards. Self-certification is not allowed if the plan has knowledge that the participant does not meet the statutory qualification standards.

▶ **Rael & Letson Observations:** Hardship distributions of employee contributions have been cumbersome and expensive to administer. Full self-certification would avoid these challenges for plans that offer Hardship. In contrast, full self-certification could lead to additional abuse with members using the plan as a glorified savings account rather than a retirement savings vehicle. Boards should carefully consider the tradeoffs before approving participant self-certification of Hardship distributions.

Final Thoughts

For the Multiemployer Industry, Secure 2.0's DC changes in the current form will marginally improve disclosure and/or distribution access for some participants and ease the administrative burden for some plans. For multiemployer groups that have or are considering a 401(k) feature, these potential improvements may be offset by the design inflexibility from savings rule changes. As a result, Rael & Letson will be lobbying through our American Academy of Actuaries Committee role to improve or exempt provisions that are onerous to the Multiemployer Industry.