Treasury and IRS Issue SECURE Act Guidance

Limited guidance includes some information on the birth/adoption provision.

September 2020

KEY POINTS

- The Treasury and IRS provide limited guidance on specific SECURE Act provisions, which is not intended to be comprehensive.
- Key SECURE Act provisions and open questions still need to be addressed, including changes in RMD rules for beneficiaries and repayment rules for qualified birth or adoption distributions.
- Additional guidance is anticipated, including regulations that address the repayment of qualified birth or adoption distributions.

On September 2, 2020, the Department of the Treasury ("Treasury") and the Internal Revenue Service ("IRS") issued Notice 2020-68 ("Notice"), which provides guidance (in the form of questions and answers) on certain provisions of the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act) and retirement provisions included in the Bipartisan American Miners Act of 2019 (Miners Act).

Specifically, the Notice addresses the following provisions of the SECURE and Miners Acts:

- Participation of long-term, part-time employees in 401(k) plans;
- Qualified birth or adoption distributions ("QBADs");
- The reduction in minimum age for in-service distributions;
- Difficulty of care payments;
- The small employer automatic enrollment credit;
- The repeal of the maximum age for traditional IRA contributions; and
- Deadlines for plan amendments.

Participation of long-term, part-time employees in 401(k) plans

Section 112(a) of the SECURE Act provides that a 401(k) plan may not require an employee to complete a period of service that extends beyond the close of the earlier of:

- The later of attainment of age 21 or completion of a 12-month period during which the employee has at least 1,000 hours of service; or
- The completion of three consecutive 12-month periods during each of which the employee has completed at least 500 hours of service.

The latter is known as the eligibility requirement for "long-term, part-time employees," which will not apply unless the employee has attained age 21 by the close of the three consecutive 12-month periods.

A long-term, part-time employee must be credited with a year of service for purposes of determining vesting for each 12-month period during which the employee completes at least 500 hours of service. However, employers are not required to make nonelective or matching contributions on behalf of long-term, part-time employees (who may be excluded from nondiscrimination, coverage, and top-heavy testing).

These changes generally apply to plan years beginning after December 31, 2020 (except for collectively bargained plans). However, in determining eligibility for long-term, part-time employees, 12-month periods beginning before January 1, 2021, are not taken into account.

The guidance clarifies that each 12-month period for which the employee has at least 500 hours of service must be credited for purposes of determining vesting for eligible long-term, part-time employees, including vesting years of service prior to January 1, 2021. It requests comments on how to reduce potential administrative burdens related to counting years of service beginning before January 1, 2021. This would only be an issue for plans that decide to provide matching or non-elective contributions to long-term, part-time employees (which, as described above, is not required).

Qualified birth or adoption distributions ("QBADs")

Section 113 of the SECURE Act permits an individual to receive a qualified birth or adoption distribution ("QBAD") from an eligible retirement plan or IRA of up to $5,000 without application of the 10% additional tax on early distributions.

A QBAD must be made during the 1-year period beginning on the date on which the child of the individual is born or the legal adoption by the individual of an eligible adoptee is finalized. QBADs are exempt from mandatory 20% withholding, the 402(f) notice requirements, and the direct rollover requirements. An individual may recontribute a QBAD to an eligible retirement plan in which the individual is a beneficiary and to which a rollover can be made. These changes apply to distributions made after December 31, 2019.

The guidance makes the following clarifications:

- Each parent may receive a qualified birth or adoption distribution of up to $5,000 with respect to the same child or eligible adoptee. Also, an individual is permitted to receive qualified birth or adoption distributions with respect to the birth of more than one child or the adoption of more than one eligible adoptee if the distributions are made during the 1-year period following the date on which the children are born or the legal adoption for the eligible adoptees is finalized.
- An eligible retirement plan must accept the recontribution of a qualified birth or adoption distribution from an individual if (a) the plan permits qualified birth or adoption distributions; (b) the individual received a qualified birth or adoption distribution from that plan; and (c) the individual is eligible to make a rollover contribution to that plan at the time the individual wishes to recontribute the qualified birth or adoption distribution to the plan.
- It is optional for an eligible retirement plan to permit in-service qualified birth or adoption distributions.
- A plan sponsor or plan administrator is permitted to rely on reasonable representations from the individual when determining whether an individual is eligible for a qualified birth or adoption distribution (unless the plan sponsor or plan administrator has actual knowledge to the contrary).
- Qualified birth or adoption distributions are treated as meeting the distribution restrictions for 401(k) plans, 403(b) custodial accounts and annuities, and governmental 457(b) plans. Accordingly, an employer may expand its plan distribution options to allow distributions from elective, qualified nonelective, qualified matching, or safe harbor contribution sources in a 401(k) plan.

The guidance indicates that the Treasury and the IRS intend to issue regulations that will address the recontribution rules (including rules related to the timing of recontributions). In addition to the recontribution rules, there remain a number of open questions such as whether a QBAD must be taken prior to a hardship, the impact on safe-harbor notices when a plan adds this provision (and whether this a permissible mid-year change for a safe harbor plan), and whether the distribution right (once added to the plan) becomes a protected benefit which can never be eliminated.

While some plan sponsors may wish to move forward with including QBADs in their plans, they should be cognizant of these issues.

Reduction in minimum age for certain in-service distributions

Section 104(a) of the Miners Act lowers the minimum age from age 62 to age 59½ for in-service distributions from pension plans (including money purchase plans) and governmental 457(b) plans. These changes apply to plan years beginning after December 31, 2019.

The guidance makes the following clarifications:

- In-service distributions in pension and governmental 457(b) plans are optional. Accordingly, a plan is not required to allow for in-service distributions at age 59½. Further, a plan that has a higher age requirement for in-service distributions (e.g., age 62) is not required to lower its age limit.

- In-service distribution age requirements are independent of the requirements for establishing a plan's normal retirement age. If a plan wishes to lower its normal retirement age below age 62 (e.g., age 59½), it must be reasonably representative of the typical retirement age for the industry in which the covered workforce is employed.

Difficulty of care payments

A difficulty of care payment is a type of qualified foster care payment to an individual that is excludable from gross income. Section 116(a) of the SECURE Act allows a taxpayer to elect to increase the nondeductible IRA contribution limit by the amount of excludable difficulty of care payments where the taxpayer's gross income is less than the deductible limit. These changes apply to contributions made after December 20, 2019.

Section 116(b) of the SECURE Act increases the annual additions limit for retirement plans by including difficulty of care payments in compensation used to calculate the limit. Accordingly, a participant in a retirement plan may make or receive contributions that are based on difficulty of care payments, even if the participant has no other compensation. These changes apply to plan years beginning after December 31, 2015.

The guidance makes the following clarifications:

- Difficulty of care payments received by an employee from a source other than his or her employer are not includible in compensation used to calculation contributions to the employer's plan.
- If an employer does not make difficulty of care payments to its retirement plan eligible employees, then the plan does not need to be amended to include difficulty of care payments in the plan's definition of annual additions compensation.

Small employer automatic enrollment credit

Section 105 of the SECURE Act provides a business tax credit of $500 for an "eligible employer" that establishes an eligible automatic contribution arrangement ("EACA") under a qualified employer plan (e.g., 401(a) plans, 403(a) plans, SEPs, and SIMPLE retirement accounts). The new credit applies to taxable years beginning after December 31, 2019.

An "eligible employer" is generally defined as having no more than 100 employees who received at least $5,000 of compensation from the employer for the preceding year. The credit is available for three taxable years ("three-year credit period") beginning with the first taxable year for which an eligible employer includes an EACA in a qualified employer plan that it sponsors. The guidance addresses the application of the credits to employers that sponsor more than one plan, multiple employer plans, and spin-off plans.

The guidance makes the following clarifications:

- An eligible employer must include the same EACA in the same plan to receive the credit. If an employer spins off a portion of a plan that includes an EACA and continues to include the EACA in both the original plan and the spun-off plan it will continue to be eligible for the credit.
- In the event an EACA is adopted in tax years beginning prior to 2020, the credit will only be available for tax years beginning after 2019 that fall within the three-year credit period (beginning with the year the EACA was first adopted).
- In the case of a multiple employer plan ("MEP"), the credit applies to each eligible employer beginning with the first taxable year its eligible employees are covered by an EACA under the MEP.

Repeal of the maximum age for traditional IRA contributions

Section 107(a) of the SECURE Act repeals the prohibition on making contributions to a traditional Individual Retirement Arrangement (IRA) for individuals attaining age 70½.

Section 107(b) of the SECURE Act provides that the excludable amount of qualified charitable distributions for a taxable year (up to $100,000 can be excluded from gross income) is reduced by the aggregate amount of IRA contributions deducted for the taxable year and any earlier post-age 70½ contributions that were not previously excluded from gross income. These changes apply to contributions and distributions made for taxable years beginning after December 31, 2019.

The guidance makes the following clarifications:

- Financial institutions are not required to accept post-age 70½ contributions. Also, a financial institution that chooses to accept post-age 70½ contributions must amend its IRA contracts to provide for those contributions. The IRS expects to issue revised model IRAs and prototype language addressing changes made by the SECURE Act.
- Financial institutions that choose to accept post-age 70½ contributions must distribute copies of the IRA contract amendment and the related amended disclosure statement to each benefited individual. Copies of these documents must be delivered or mailed to the last known address of the benefited individual not later than the 30th day after the later of the date on which the amendment is adopted or the date it becomes effective.
- An individual may not offset or "net" the amount of required minimum distributions from the individual's IRA by the amount of post-age 70½ contributions for the same taxable year.

Deadlines for plan amendments

Plan amendments for provisions of the SECURE Act must be adopted no later than the last day of the first plan year beginning on or after January 1, 2022. Collectively bargained plans and governmental plans have an additional two years. SECURE Act amendments made within this timeframe are eligible for anti-cutback relief relating to IRS protected benefit rules.

The guidance makes the following clarifications:

- The plan amendment deadline for Section 104(a) of the Miners Act, which lowers the minimum age from age 62 to age 59½ for in-service distributions from pension plans (including money purchase plans) and governmental 457(b) plans, is the same as the deadline applicable to plan amendments for SECURE Act provisions.
- Plan amendments for provisions of the SECURE and Miners Acts that are made after the special amendment deadlines described above may still be considered timely if made within the usual amendment deadlines (such as those outlined in Rev. Proc. 2016-37). However, any amendments adopted after the special amendment deadlines will not be eligible for anti-cutback relief.
- The deadline to amend a trust governing an IRA for SECURE Act provisions is December 31, 2022 (or such later date as the Treasury Secretary prescribes).

Request for comments and need for additional guidance

The guidance is intended to assist with specific implementation issues and is not meant to be comprehensive. It does not address many key SECURE Act provisions, such as the changes in the required minimum distribution rules (“RMDs”) applicable to beneficiaries, nor does it address a number of significant open questions (including the requirements for repayment of QBADs). The Treasury Department and IRS anticipate issuing additional guidance in the future and has invited comments and suggestions, which are due on or before November 2, 2020, on the topics discussed in the Notice.

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T. Rowe Price Retirement Plan Services, Inc.

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