IRS releases SECURE 2.0 guidance

Make Your Plan
February 2024

Key Insights

- A new notice from the IRS (Notice 2024-2) provides guidance on a dozen SECURE 2.0 provisions in a question-and-answer format.
- The guidance may help facilitate implementation of certain provisions of SECURE 2.0, but it is not intended to be comprehensive.
- The IRS has invited comments and suggestions regarding the matters discussed in the notice.

On December 20, 2023, the Internal Revenue Service released Notice 2024-2, which it has described as a "grab bag" that provides guidance on various provisions of the SECURE 2.0 Act of 2022 (SECURE 2.0). The IRS indicated that the notice is not comprehensive but is "intended to provide guidance on discreet issues to assist in commencing implementation of these provisions."

Below is a summary of key SECURE 2.0 provisions addressed in Notice 2024-2.

Automatic enrollment for "new" plans

Background: Unless an exception applies, Section 101 of SECURE 2.0 requires new 401(k) and 403(b) plans to automatically enroll participants at a minimum initial rate of 3% of compensation. That rate must be increased by 1% each year until it reaches at least 10%. These requirements, which apply to plan years beginning after 2024, do not apply to any plan established before December 29, 2022 (the date of the enactment of SECURE 2.0).

Notice 2024-2 includes the following clarifications regarding mandatory automatic enrollment:

- A plan is "established" on the date the plan is adopted, even if the plan takes effect after the adoption date. So, a plan adopted prior to December 29, 2022 (a pre-enactment plan), is exempt from mandatory automatic enrollment, even if the plan first became effective after enactment of SECURE 2.0.
- In the case of the merger of two single employer pre-enactment plans, the merged plan is treated as a pre-enactment plan. The result is the same if a single employer pre-enactment plan is merged with a pre-enactment plan maintained by more than one employer.
- If a pre-enactment plan is merged with a plan established after the enactment of SECURE 2.0, the general rule is that the mandatory automatic enrollment provisions of SECURE 2.0 apply to the merged plan. However, an exception applies in the case of certain business mergers and acquisitions if the plan merger is accomplished within the coverage transition period defined in the

Internal Revenue Code (IRC), which generally is by the end of the plan year following the corporate merger or acquisition. Another exception applies if a "new" plan is merged with a pre-enactment plan maintained by more than one employer (e.g., a multiple employer plan). In such cases, the pre-enactment plan remains grandfathered, but the portion of the merged plan attributable to the "new" plan would be subject to the mandatory automatic enrollment requirements of SECURE 2.0.

- If a plan is spun off from a pre-enactment plan, the spun-off plan is also treated as a pre-enactment plan. However, if the plan from which the new plan was spun off was a plan maintained by more than one employer that was established before December 29, 2022, the spun-off plan is treated as a pre-enactment plan only if the participants in the spun-off plan were previously treated as participating in a pre-enactment plan.

De minimis financial incentives

Background: Effective upon enactment, Section 113 of SECURE 2.0 provided that a *de minimis* financial incentive (one not paid for with plan assets) provided to employees who elect to participate in the plan will not violate the contingent benefit rule, which prohibits conditioning any benefit—other than employer matching contributions—on a decision to participate in the plan. This provision also provides relief from the prohibited transaction rules in the IRC and the Employment Retirement Income Security Act (ERISA).

Notice 2024-2 includes the following clarifications regarding *de minimis* incentives:

- A financial incentive is *de minimis* only if it does not exceed $250 in value.
- A plan can only offer *de minimis* financial incentives to employees who do not have deferral elections already in effect.
- A plan can provide *de minimis* financial incentives in installments that are contingent on the employee continuing to defer, even if those installments are paid over more than one plan year.
- A *de minimis* financial incentive is includible in the employee's gross income and wages and is subject to applicable withholding and reporting requirements, unless the incentive satisfies an exception under the IRC (e.g., nontaxable fringe benefits).

Distributions to the terminally ill

Background: Effective upon enactment, Section 326 of SECURE 2.0 added a new exception to the 10% additional tax that applies to early distributions for any distribution made to a terminally ill individual. To be considered a terminally ill individual, the employee must be certified by a physician as having a terminal illness and furnish sufficient evidence to the plan administrator.

Notice 2024-2 makes the following clarifications regarding distributions to terminally ill individuals:

- Terminally ill distributions are permitted from 401(a) plans, including 401(k) plans, 403(b) plans, and IRAs. However, terminally ill distributions are not available from governmental 457(b) plans.
- The guidance provides details of what must be included in a certification of terminal illness by a physician that is provided to the plan administrator. Also, the guidance clarifies that a "plan administrator" includes an IRA trustee, custodian, or issuer.
- The employee must otherwise be eligible for a permissible in-service distribution to receive a terminally ill distribution.
- If a plan does not permit terminally ill individual distributions, the employee is permitted to treat an otherwise permissible in-service distribution as a terminally ill distribution on their federal income tax return and can receive an exemption to the 10% early distribution penalty by completing IRS Form 5329. The employee must retain the physician's certification in case it is later requested by the IRS. Also, the employee may recontribute the distribution to an IRA.
- Note: The discussion draft of a SECURE 2.0 technical corrections bill currently circulating in Congress would create a new in-service distribution option for terminally ill individuals and would permit a participant to self-certify as to their terminal illness.

Plan amendment deadlines

Background: Section 501 of SECURE 2.0 generally provides for a plan amendment deadline of the last day of the first plan year beginning on or after January 1, 2025 (i.e., December 31, 2025, for a calendar year plan), for any changes made to the plan by SECURE 2.0 or subsequent regulation. Governmental plans and applicable collectively bargained plans have until the last day of the first plan year beginning on or after January 1, 2027 (i.e., December 31, 2027, for a calendar year plan).

This provision also delays the plan amendment deadlines for changes made to the plan by various laws that preceded SECURE 2.0 (e.g., the SECURE Act of 2019, the CARES Act, and the Taxpayer Certainty and Disaster Tax Relief Act of 2020) to align with the plan amendment deadline for SECURE 2.0.

Notice 2024-2 makes the following changes to plan amendment deadlines:

- The guidance provides a new plan amendment deadline of December 31, 2026, for qualified plans and 403(b) plans.

For governmental 401(a) and 403(b) plans, the plan amendment deadline is extended to December 31, 2029.

- The plan amendment deadline for applicable collectively bargained plans is extended to December 31, 2028.
- For governmental 457(b) plans, the plan amendment deadline is extended to the later of December 31, 2029, or, if applicable, the first day of the first plan year beginning more than 180 days after the date of notification by the Treasury secretary that the plan was administered in a manner that is inconsistent with the requirements of Section 457(b) of the Code.

Roth employer contributions

Background: Section 604 of SECURE 2.0 allows a 401(a) plan (including a 401(k) plan), 403(b) plan, or governmental 457(b) plan to permit employees to designate employer matching or nonelective contributions, ones that are nonforfeitable at the time they are received, as designated Roth contributions. This provision is effective for contributions made after December 29, 2022.

Notice 2024-2 makes the following clarifications regarding designated Roth employer contributions:

- Rules similar to the rules for designated Roth elective contributions apply to designated Roth employer contributions, except that Roth employer contributions need not satisfy the rules applicable to elective contributions, such as the special distribution restrictions and inclusion in the ADP test. For example, designation of employer contributions as Roth contributions must be made no later than the time that the contribution is allocated to an employee's account and must be irrevocable. Also, designated Roth employer contributions are subject to income inclusion treatment and separate accounting rules. In addition, an employee must have an effective opportunity to make (or change) their designation of a Roth employer contribution election at least once during each plan year.
- A designated Roth employer contribution is includible in gross income for the taxable year in which the contribution is allocated to the individual's account.
- An employer contribution may be designated as a Roth contribution only if the employee is fully vested in the contribution at the time it is allocated to the employee's account.
- If employer contributions are subject to a vesting schedule, an employee's right under the plan to designate 100% vested employer contributions as Roth contributions will not be treated as failing to satisfy Section 401(a)(4) of the IRC, even if that right is not currently available to a group of employees (i.e., because they are not 100% vested).
- Designated Roth employer contributions are not wages for purposes of federal income tax withholding. However, an employee who designates an employer contribution as a Roth contribution may need to increase their withholding or make estimated tax payments to avoid an underpayment penalty.
- Roth employer contributions made to a 401(a) or 403(b) plan are not wages for purposes of FICA (Federal Insurance Contributions Act) and FUTA (Federal Unemployment Tax Act) taxes.
- Roth nonelective contributions to a governmental 457(b) plan are wages for purposes of FICA but only if FICA taxes normally apply to such employees (such as state and local government employees who are not members of a state or local retirement system). Roth nonelective contributions made to a governmental 457(b) plan are not subject to FUTA taxes.
- The reporting obligations that apply to Roth employer contributions are the same as if, upon allocation to that account, the contribution had been directly rolled over to a designated Roth account in the plan as an in-plan Roth rollover. Thus, designated Roth employer contributions are reported in boxes 1 and 2a of Form 1099-R, and code "G" is used in box 7.
- Plans may limit the contribution sources (i.e., deferrals, matching contributions, and/or nonelective contributions) that are eligible to be designated as Roth contributions. However, the right to make designated Roth contributions is a right or feature subject to the requirements of IRC Section 401(a)(4).

Other guidance

Notice 2024-2 also includes guidance on the following SECURE 2.0 provisions not addressed in this summary:

- enhancement of credit for small employer plan start-up costs (Section 102),
- military spouse retirement plan eligibility credit for small employers (Section 112),
- the contribution limit for Savings Incentive Match Plan for Employees (SIMPLE) IRAs (Section 117),
- employers' ability to replace SIMPLE retirement accounts with safe harbor 401(k) plans during the year (Section 332),
- cash balance projected interest crediting rate (Section 348),
- safe harbor for corrections of employee elective deferral failures (Section 350), and
- SIMPLE and Simplified Employee Pension (SEP) Roth IRAs (Section 601).

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