FEATURE:
RETIREMENT BENEFITS

By **Bruce D. Steiner** & **Denise Appleby**

Selected Provisions of the Recently Enacted SECURE Act 2.0

The new law includes over 90 changes to the rules that govern individual retirement accounts and employer plans

Three years after the Setting Every Community Up for Retirement Enhancement Act of 2019, Pub. L. 116–94 (SECURE Act 1.0) was signed into law, SECURE Act 2.0 (Act 2.0) was signed into law on Dec. 29, 2022, as part of the Consolidated Appropriations Act, 2023 Pub. L. 117-164.[1] Act 2.0 builds on SECURE Act 1.0, making over 90 changes to individual retirement account and employer plan provisions. Most of these provide opportunities to help clients save for retirement, including allowing employers to add provisions that benefit their employees.

Here's an overview of selected provisions.

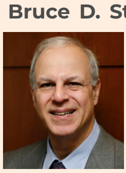
First RMD Year

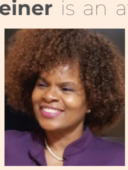
SECURE Act 1.0 increased the first required minimum distribution (RMD) year from the year the employee or IRA owner (participant) reaches age 70½ to the year the participant reaches age 72. Section 107 of Act 2.0 further increases the first distribution year to age 73 for participants attaining age 72 after 2022 and attaining age 73 before 2033, and age 75 for participants attaining 74 in 2033 or later.

Note: There's an overlap for those born in 1959, because they fall into the age 73 and age 75 starting ages. We anticipate that this will be resolved under technical corrections.

Participants in employer plans are still able to defer RMDs past these ages until retirement if permitted under the plan. The option to defer RMDs past these ages still isn't available to any participant who's a 5% owner of the employer.

Bruce D. Steiner is an attorney with Kleinberg, Kaplan, Wolff & Cohen, P.C. in New York City, and **Denise Appleby** is CEO of Appleby Retirement Consulting Inc. in Grayson, Ga.





This new age for beginning RMDs benefits participants who don't need the money for current living expenses, as it allows for longer tax deferral of the amounts.

Planning opportunity: Many taxpayers do Roth conversions between retirement and RMD age if they're retired and in lower tax brackets. This change will give those participants additional years to do Roth conversions during their lower tax brackets years before they must begin RMDs.

This provision applies to participants who will reach age 72 after 2022.

IRA Catch-Up Amount

Individuals age 50 or over at the end of the year may contribute an additional $1,000 to their IRAs. Under Section 108 of Act 2.0, this amount will be indexed for inflation beginning in tax year 2024. This is the first time IRA catch-up contributions are indexed for inflation since introduced under the Economic Growth and Tax Relief Reconciliation Act of 2001.

Contributions to Employer Plans

The catch-up contribution limit for individuals age 50 or over is $3,500 for Savings Incentive Match Plan for Employees (SIMPLE) IRAs and $7,500 for salary deferral plans other than SIMPLEs in 2023. These limits are adjusted for inflation.

Section 109 of Act 2.0 increases catch-up contributions for plan participants ages 60 to 63. These amounts are:

- For Internal Revenue Code Section 401(k), Section 403(b) and governmental Section 457(b)

plans, the adjusted dollar limit is the greater of $10,000, or an amount equal to 150% of the regular catch-up contribution limit in effect for 2024.
- For SIMPLE IRAs and SIMPLE 401(k) plans, the adjusted dollar amount is the greater of $5,000 or an amount equal to 150% of the regular catch-up contribution limit in effect for 2025.

These amounts will be adjusted for cost-of-living increases in the year beginning after Dec. 31, 2025, and the base period will be the calendar quarter beginning July 1, 2024. This will provide an opportunity for eligible participants to give their retirement savings a boost, in preparation for retirement.

This provision takes effect in taxable years beginning after Dec. 31, 2024.

Age for ABLE Accounts

Achieving a Better Life Experience (ABLE) accounts may be established for individuals who receive certain benefits by reason of blindness or disability occurring before age 26. Section 124 of Act 2.0 increases the age requirement from 26 to 46.

This provision is effective for taxable years beginning in 2026.

529 Plans Converted to Roth IRAs

To help prevent IRC Section 529 plan (529 plan) balances that aren't used to cover qualified education expenses from being subject to income tax and the 10% early distribution penalty, Section 126 of Act 2.0 allows up to $35,000 to be converted from a 529 plan to the beneficiary's Roth IRA. This $35,000 is a lifetime limit and is subject to several restrictions, including:

- The 529 plan must have been maintained for the 15-year period ending on the date the amount is distributed from the 529 plan;
- The amount converted for a year can't exceed the aggregate amount contributed to the 529 plan (plus earnings attributable) before the 5-year period ending on the date of the distribution;
- The amount must be moved directly from the 529 plan to the Roth IRA (trustee to trustee); and
- The amount, when added to any eligible regular traditional and Roth IRA contribution made for the 529 plan's beneficiary for the year, can't exceed the IRA contribution limit in effect for the year.

Once these amounts are converted to a Roth IRA, they become subject to the same treatment that applies to amounts converted from traditional IRAs to Roth IRAs.

This provision affects distributions from the 529 plan after Dec. 31, 2023.

Section 201 of Act 2.0 allows plans to offer more choices, including annuity payments that increase by a constant percentage at a rate that's not less than 5%, payments and return of premium death benefits and limited lump-sum payments.

More Choices for Certain Plans

There are restrictions on the design of annuities available to participants in defined contribution plans and to IRA owners who are of RMD age. These restrictions prevent increases in annuity payments except in limited cases.

Section 201 of Act 2.0 allows plans to offer more choices, including annuity payments that increase by a constant percentage at a rate that's not less than 5%, payments and return of premium death benefits and limited lump-sum payments.

This provision applies to calendar years ending after Dec. 29, 2022 (the date of enactment).

Increase in QLAC Amount

Under current regulations, qualified longevity annuity contracts (QLACs) may be purchased for participants under defined contribution plans and

IRAs. A QLAC is an annuity in which the payments begin at up to age 85. By deferring payments, an IRA owner may obtain larger monthly payments. This allows an IRA owner to protect against living a very long time and running out of money without having to commit a large amount of money to the annuity. It also allows IRA owners to spend their other money more freely, knowing that they'll receive payments from the QLAC if they live a long time.

The QLAC premium was limited to the lesser of 25% of the value of the account or $125,000. Act 2.0 eliminates the 25% limit and increases the premium amount to $200,000 (indexed). Act 2.0 also provides for a 90-day free look period, during which the purchase of the contract may be rescinded.

Section 325 of Act 2.0 repeals the RMD requirement for designated Roth accounts.

Statute of Limitations on Penalties

Before Act 2.0, the statute of limitations on the excise taxes for excess contributions and failure to take RMDs didn't begin until the taxpayer filed Form 5329. This created a hardship for IRA owners who weren't aware of this deadline and believed that the statute of limitations for these penalties was three years from when they filed their income tax returns.

Under Section 313 of Act 2.0, the statute of limitations for excess contributions is six years from when the IRA owner files an income tax return and three years from when the IRA owner files an income tax return for failure to take RMDs. However, this change doesn't apply in the case of an excess contribution when an IRA acquires property for less than fair market value.

This provision took effect on Dec. 29, 2022.

Prohibited Transactions

Under IRC Section 408(e)(2), if an IRA engages in a prohibited transaction, it ceases to be treated as an IRA and is treated as having distributed all of its assets. This penalty is far more severe than the one for an employer plan or exempt organization engaging in a prohibited transaction.

Some practitioners believed that if there were a risk that an investment could be a prohibited transaction, and the IRA owner segregated it in a separate IRA, only that IRA would cease to be treated as an IRA if it were determined to be a prohibited transaction. That would avoid tainting the IRA owner's other IRAs.

Section 322 of Act 2.0 clarifies that this is the case. An IRA owner concerned that an investment may be a prohibited transaction may safely segregate that investment in a separate IRA, thus protecting their other IRAs.

This provision applies to taxable years beginning after Dec. 29, 2022.

No RMDs for Roth 401(k) Owners

Roth IRA owners aren't required to take distributions during their lifetime. However, participants are subject to RMDs from designated Roth accounts (Roth 401(k), Roth 403(b) and Roth governmental 457(b) accounts). Section 325 of Act 2.0 repeals the RMD requirement for designated Roth accounts. As a result, beginning in 2024, employees may decide between keeping their assets in a designated Roth account or rolling them over to a Roth IRA without having to consider RMDs during their lifetime. Key factors in making this decision will include the availability of desired investment choices, investment expenses and asset protection.

This provision affects distribution years 2024 and after (except for distributions otherwise required with respect to 2023).

Deceased Employee Election

Section 327 of Act 2.0 provides that a surviving spouse may elect to be treated as the deceased employee for purposes of the RMD rules, effective beginning in 2024. A surviving spouse who makes this election would begin RMDs no earlier than the date the deceased participant would have reached RMD age. Further, if a spouse beneficiary who makes this election dies before they're required to start RMDs, the beneficiary RMD rules would apply as if the spouse beneficiary is the employee. Once made, this election is irrevocable.

Charity as Remainder Beneficiary

Under the SECURE Act 1.0, a trust for a disabled or chronically ill beneficiary is eligible for the life expectancy stretch as long as all of the current beneficiaries are disabled or chronically ill, and the remainder beneficiaries are individuals or trusts for the benefit of individuals. Thereafter, the 10-year rule applies. However, in many cases, an IRA owner leaving IRA benefits to a trust for a disabled child wants a charity to receive some or all of the remainder of the trust on the disabled child's benefit. In some cases, a charity provides assistance for the disabled beneficiary. In other cases, the IRA owner doesn't have any other children or has other children but otherwise provides for them.

Section 337 of Act 2.0 provides that in the case of a trust for a disabled or chronically ill beneficiary, a charity that may receive qualified charitable distributions (a public charity other than a donor-advised fund) that's a remainder beneficiary will be treated as a designated beneficiary. This allows an IRA owner to create a trust for a disabled or chronically ill beneficiary and name a charity as a remainder beneficiary and still qualify for the life expectancy stretch.

This provision took effect on Jan, 1, 2023.

Catch-Up Contributions

Under current tax law, plan participants may choose whether to make catch-up contributions to a designated Roth account (if permitted under the plan) or a pre-tax account or to split them between both accounts. Under Section 603 of Act 2.0, catch-up contributions to 401(k) plans must be designated Roth contributions if the employee's compensation from that employer was more than $145,000 (indexed). This makes catch-up contributions less attractive for employees who otherwise wouldn't contribute to

designated Roth accounts. Many employees prefer to make elective deferrals (contributions) to traditional accounts because they expect to be in a lower tax bracket after they retire. Beginning in 2024, they'll have to decide whether the benefit of making catch-up contributions outweighs the higher tax bracket that may apply to designated Roth contributions.

This provision takes effect for taxable years beginning after Dec. 31, 2023.

Aggregation of RMDs isn't permitted among annuities IRAs and other IRAs.

Waiver of 10% Excise Tax

An excise tax of 10% is imposed on excess nondeductible contributions made to qualified employer plans. The tax is required to be paid by the employer making the contributions. When determining the amount of an employer's excess nondeductible contribution for any taxable year, certain amounts aren't taken into account, including contributions to a SIMPLE IRA or SIMPLE 401(k), which aren't deductible when contributed solely because such contributions aren't made in connection with a trade or business of the employer. Section 118 of Act 2.0 adds contributions to Simplified Employee Pension plan IRAs to this exception, when the contributions aren't deductible when contributed solely because such contributions aren't made in connection with a trade or business of the employer.

This provision took effect on Dec. 29, 2022.

Aggregation of RMDs

Aggregation of RMDs isn't permitted among annuities IRAs and other IRAs. The same restriction applies to defined contribution plans. Section 204 of Act 2.0 allows aggregation with annuities and accounts by treating accounts that an individual holds as the owner of one account for RMD purposes. The same provision is extended to accounts and annuities that an individual holds as a beneficiary of the same decedent.

The Secretary of the Treasury (or the Secretary's delegate) is required to amend applicable sections of the RMD regulations and IRC to eliminate any excise tax that would have applied without this provision. These amendments will be deemed to have been made as of Dec. 29, 2022. Until such time, taxpayers may rely on good faith interpretation of this provision.

Reduction of Excise Tax

An excise tax of 50% applies to RMDs that aren't distributed by the deadline. Taxpayers may request a waiver of the deadline if the deadline was missed due to reasonable error. Under Section 302 of Act 2.0, the excise tax is reduced to 25%, and further reduced to 10% if the shortfall is corrected on a timely basis. Taxpayers may still request a waiver of the excise tax if the deadline was missed due to reasonable error.

This is effective for tax years beginning after 2022.

Action Plan for Advisors

We've covered only some of the changes made by Act 2.0. Many of those that we didn't cover provide incentives for employers to provide employee benefits under employer plans and for employees to participate. There are several provisions under which the 10% additional tax on early distributions are automatically waived on limited amounts, including when distributions are taken due to domestic abuse and by individuals with qualifying terminal illnesses.

We included the applicable sections of Act 2.0 for the sections that we covered in the event you desire to read about these changes further. In preparation for educating clients about these changes, we recommend creating a simple list of all the changes that might be important to your clients, including effective dates. This list can be used to help identify which clients should be contacted now.

Endnote

1. The text of Pub. L. 117-164 is available at *www.congress.gov/bill/117th-congress/house-bill/2617*.