RIKER DANZIG SCHERER HYLAND PERRETTI LLP

New Year's Resolutions: New Legislation Brings Changes and Challenges to 2020 Employee Benefits, Tax and Estate Planning

Publication:

Riker Danzig Employee Benefits, Tax, Trust and Estates Client Alert January 2, 2020

The "Setting Every Community Up for Retirement Enhancement Act" (the "Secure Act," or "Act") goes into effect beginning in 2020. Employers, employees, IRA owners and plan participants should understand the impact the Secure Act has on planning for the future. The key changes - and challenges - the Secure Act brings to the planning table are described below:

IMPACT ON EMPLOYERS:

Expansion of Multiple Employer Plans: Under current law, groups of (typically small) employers could adopt an umbrella benefit plan, or "multiple employer plan" ("MEP"), so long as the employers were somehow related, for example through geographic location or line of business. Effective for plan years beginning after December 31, 2020, the Secure Act expands the ability of employers to adopt a benefit plan even if the employers are not related, thereby allowing employers to share administrative costs and provide for more efficient, cost-effective plan investment policies. In addition, for certain "covered MEPs," the Act eliminates the "one bad apple rule" that imposed on all participating employers in the MEP liability for the violation of plan requirements by one or more participating employer(s), provided certain conditions are met. Coverage for Long-Term Part-Time Employees: Effective for plan years beginning after December 31, 2020, the Secure Act provides that part-time employees who meet a plan's minimum age requirement (up to age 21), if any, and complete at least 500 hours of service a year over three consecutive years (rather than at least 1000 hours of service in one plan year, as under current law) must be allowed to participate in a 401(k) plan. Collectively bargained plans are excepted. Other nondiscriminatory exclusions (e.g., based on job title or geographic location) would still be allowed. In turn, employers are provided relief from top-heavy nondiscriminatory vesting and benefits testing with respect to their long-term part-time employees.

Disclosures of Lifetime Income Under Defined Contribution Plans: The Act requires an employer to provide a disclosure at least once every 12 months to defined contribution plan participants that illustrates the monthly amount the lump sum balance credited to the participant's account would generate over the participant's lifetime as if the benefit were paid as an annuity, even if the plan does not provide an annuity as a benefit payment option. The employer is provided relief from fiduciary liability if certain safe harbor actuarial assumptions are used and if the disclosure includes model language to be developed by the U.S. Department of Labor. Lifetime income disclosure statements will not be required until after the Department of Labor issues guidance on the disclosures, the safe harbor actuarial assumptions, and the model language.

Employer Relief from Annuity Investments: Effective as of the date of enactment, the Secure Act simplifies the process for offering annuities in Internal Revenue Code Section 401(k) plans and 403(b) plans by providing fiduciary liability relief to the employer for selection of the annuity provider, provided certain safe harbor requirements are met.

Increase in Auto-Enrollment Cap: In an effort to encourage retirement savings, the Act increases the cap on automatic contribution of deferrals under 401(k) plans with safe harbor auto-enrollment from 10% to 15% of a participant's compensation after the first year of deemed deferral election.

Increase in Start-Up Credit for Small Employers: For small employers, the Secure Act increases the tax credit for three years to recover start-up costs for establishing retirement plans for their employees, and provides an extra automatic enrollment credit of up to $500 a year for three years.

Safe Harbor 401(k) Rules: The Act simplifies the safe harbor rules for 401(k) plans by eliminating the annual notice requirement for safe harbor non-elective contributions (i.e., contributions of at least 3% of employee compensation instead of matching contributions) and allowing for non-elective contribution plan amendments after the beginning of a plan year provided certain conditions are met (including having employer non-elective contributions of at least 4% of employee compensation).

Employer Relief Under Closed Defined Benefit Plans: Effective generally as of the date of enactment, the Act provides relief for nondiscrimination testing of closed (frozen) defined benefit plans by permitting benefit increases to older, longer service employees.

Consolidated Form 5500 Filings: Under the Act, an employer will be permitted to consolidate annual reporting (IRS Form 5500 Series) filings for similar defined contribution plans (e.g., with the same trustee, named fiduciary, plan administrator, plan year and investment options). Such consolidated filings are to be implemented no later than January 1, 2022, applicable to returns and reports for plan years beginning after December 31, 2021.

Increase in Penalties for Violation of Filing Requirements: The Act increases the penalties for failure to file annual Forms 5500 and certain other required filings, effective with respect to filings due (including extensions for returns) after December 31, 2019.

IMPACT ON INDIVIDUALS:

IRA Contribution Limits: In recognition that individuals increasingly continue to work well into their traditional "retirement years," effective for contributions made after December 31, 2019, the Secure Act eliminates the prohibition on contributions to a traditional (contributory) IRA by individuals who have reached age 70½.

Elimination of "Stretch IRAs": Effective generally with respect to distributions relating to individuals whose death occurs after December 31, 2019, the Act requires that non-spouse beneficiaries take distribution of an inherited IRA (or 401(k) or 403(b) account) over a maximum 10-year period, rather than the beneficiary's lifetime as under prior law. Alternative planning techniques to cushion the blow on resulting tax burdens include Roth conversions, the backloading of distributions to lower tax years, and naming a charitable remainder trust as the beneficiary so that distributions from the trust to the intended individual beneficiary(ies) can be made over a longer than 10-year time frame, with the remainder going to charity.

Increase in Age for Required Minimum Distributions: Under the Act, for individuals who reach age 70½ after December 31, 2019, required minimum distributions from tax-qualified plans and IRAs must begin upon attaining age 72, rather than age 70½. This delay provides more time for retirement planning and consideration of Roth conversions and IRA distribution scheduling.

Portability of Investments: Under the Secure Act, if lifetime income investments, such as annuities, are eliminated from a defined contribution plan's investment options, plan participants may preserve their lifetime income investments by taking a qualified distribution (e.g., a direct plan-to-plan or plan-to-IRA transfer) or qualified plan distribution annuity contract of the investment without regard to in-service withdrawal restrictions or premature withdrawal penalties.

Distributions for Births and Adoptions: Under the Act, distributions after December 31, 2019, of up to $5000 in the event of a birth or adoption will not be subject to the 10% additional income tax penalty for premature distributions under a 401(k) plan, so long as the distribution occurs within one year of the birth or the adoption becoming finalized.

EFFECTIVE DATES:

Except as specifically set forth above, the features of the Act described in this Client Alert are in general effective with respect to plan years beginning after December 31, 2019. In the absence of official guidance, an employer that complies in good faith with a reasonable interpretation of applicable provisions of the Act will not be deemed to have violated such provisions.

If you have any questions or would like more information regarding this Client Alert, please contact James Karas, Jason Navarino, Robert Daleo, Stephen Pagano, Michael LaMagna or Lauren Spitser.

Attorneys:

James N. Karas, Jr. · Jason D. Navarino · Robert C. Daleo · Stephen J. Pagano · Michael LaMagna · Lauren N. Spitser

Practices:

Corporate Law · Employee Benefits and Executive Compensation · Tax Law · Estate Planning & Administration