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SECURE Act

Congress Secures Legislation Aimed at Improving Retirement Savings

On December 20, 2019, President Trump signed into law H.R. 1865, Further Consolidated Appropriations Act, 2020. Among its various provisions, H.R. 1865 includes the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act) as Division O. The SECURE Act represents one of the most significant reforms in the retirement savings space since the Pension Protection Act of 2006 and is likely to improve outcomes for American employers, workers and retirees.

This alert first provides an overview of the key changes to US retirement savings policy that the SECURE Act will bring about, and then discusses expected next steps in terms of regulatory implementation and possible additional legislative reforms.

I. SECURE Act's Retirement Policy Changes

a. Open Multiple Employer Plans

The SECURE Act loosens up requirements for unrelated employers to utilize Open Multiple Employer Plans (Open MEPs) by treating pooled employer plans – for purposes of the Employee Retirement Income Security Act of 1974 (ERISA) – as single plans. Pursuant to the SECURE Act, a "pooled employer plan" is a defined contribution plan that is established or maintained in order to provide benefits to the employees of two or more employers and that meets various requirements set forth in the legislation. The Open MEPs provision applies to multiple-employer qualified defined contribution plans that either: (1) are sponsored by employers that both have a common interest other than having adopted the plan and control the plan; or (2) have a "pooled plan provider." A "pooled plan provider" is a third party who serves as the plan's primary fiduciary and is responsible for plan administration, largely minimizing the risks and burdens previously imposed on individual employers.

Moreover, the SECURE Act specifically amends the Internal Revenue Code – the so-called "one bad apple rule" – so that pooled employer plans will not lose tax-favored treatment and become disqualified merely because a participating employer has plan qualification issues.

b. Lifetime Income Issues

Given the increased risks associated with longer life expectancies and the uncertainties surrounding how to efficiently and effectively draw down retirement assets, the SECURE Act includes several provisions addressing lifetime income issues, including a long awaited fiduciary safe harbor for lifetime income investment options:

- **Fiduciary safe harbor for selection of lifetime income provider** – The legislation provides an optional safe harbor that allows fiduciaries to satisfy the prudence requirement with respect to the selection of insurers for a guaranteed retirement income contract.
- The safe harbor also protects fiduciaries from liability for any losses that may result to the participant or beneficiary due to an insurer's inability in the future to satisfy its financial obligations under the terms of the contract.
- **Portability of lifetime income options** – The legislation permits qualified defined contribution plans (section 403(b) plans or section 457(b) governmental plans) to make a direct trustee-to-trustee transfer of lifetime income investments or distributions of a lifetime income investment in the form of a qualified plan distribution annuity to another employer-sponsored retirement plan or Individual Retirement Account (IRA). However, in order to do so, such investments must no longer be authorized to be held as an investment option under the plan.
- **Disclosure regarding lifetime income** – Pursuant to the SECURE Act, benefit statements provided to defined contribution plan participants must now include a lifetime income disclosure, which illustrates the monthly payments the participant would receive if the total account balance were used to provide lifetime income streams. Such disclosures must be made at least once during any 12-month period and in accordance with the model that the Secretary of Labor is required to develop. Importantly, plan fiduciaries and sponsors will not face liability under ERISA solely for providing lifetime income stream equivalents that are derived in accordance with proper assumptions and guidance, and that include the explanations contained in the forthcoming model disclosure.

c. 401(k) Plans

Another key set of changes relate to 401(k) plans, including the following:

- **Increased auto enrollment safe harbor cap** – Effective for plan years beginning after December 31, 2019, the legislation increases the automatic escalation cap from 10% to 15% of employee pay for Qualified Automatic Contribution Arrangements.
- **Simplification of safe harbor rules** – The SECURE Act eliminates the safe harbor notice requirement, but still allows employees to make or change an election at least once per year. Additionally, the legislation permits amendments to nonelective status at any time before the 30th day before the close of the plan year. Amendments made after that time are allowed if: (1) the amendment provides a nonelective contribution of at least 4% of compensation for all eligible employees for that plan year; and (2) the plan is amended no later than the last day for distributing excess contributions for the plan year.

- **Long-term part-time worker participation in 401(k) plans** – Another provision in the SECURE Act requires employers maintaining a 401(k) plan to have a dual eligibility requirement under which an employee must complete either a one-year of service requirement (i.e., 1,000-hour rule) or three consecutive years of service where the employee completes at least 500 hours of service. For employees who are eligible solely because of the new 500-hour rule, their employers may elect to exclude such employees from testing under the nondiscrimination and coverage rules.

d. Pension Plans

Prior to the SECURE Act, pension plans were permitted to allow distributions to employees who are age 62 and who did not have a separation from employment at the time of the distribution. Effective for plan years beginning after December 31, 2019, age 62 is changed to 59½.

e. Non-Discrimination Testing Rules

The legislation modifies the nondiscrimination rules with respect to closed plans (i.e., plans that do not allow for new participants after a particular date, but which, nevertheless, permit existing to continue to accrue benefits) so as to prevent plans that are not discriminatory at the date on which they no longer allow new participants from becoming discriminatory over time. These modifications are necessary to protect the benefits for older, longer service employees as they near retirement.

f. Other Changes

In addition to the aforementioned changes, the SECURE Act also provides for an increase in the credit limitation for small employer pension plan start-up costs and creates a new tax credit for employers of up to US$500 per year to help cover start-up costs for new 401(k) plans and SIMPLE IRAs with automatic enrollment features.

Other SECURE Act provisions: (1) permit consolidated Form 5500 filings for similar plans with the same investments and fiduciaries; (2) increase the age for required minimum distributions from age 70½ to age 72 (effective for tax years beginning after December 31, 2019) and repeals the prohibition on deductible contributions to a traditional IRA by an individual who has attained age 70½; and (3) expand Section 529 education savings accounts to cover up to US$10,000 of qualified student loan repayments, as well as costs associated with registered apprenticeships, homeschooling, and private elementary, secondary, or religious schools.

Additionally, to offset the cost of the expanded retirement savings benefits included in the legislation, the SECURE Act modifies the required minimum distribution rules with respect to defined contribution plan and IRA balances upon the death of the account owner. Specifically, the SECURE Act requires that distributions be distributed by the end of the 10th calendar year following the year of the employee or IRA owner's death, unless the distribution is made to: (1) the surviving spouse of the employee (or IRA owner); (2) disabled or chronically ill individuals; (3) individuals who are not more than 10 years younger than the employee (or IRA owner); or (4) the child of the employee (or IRA owner) who has not reached the age of majority. The legislation also increases penalties for failure to file: (1) retirement plan returns; (2) Form 5500; (3) registration statements; (4) notification of change; and (5) required withholding notices.

II. Regulatory Implementation and Additional Legislative Reforms

Given that most retirement savings plans will need to be amended as a result of the SECURE Act – which generally provides for an amendment period until the 2022 plan year (or the 2024 plan year for governmental plans) – we expect that the Internal Revenue Service (IRS) and Department of Labor (DOL) will soon propose regulations to implement the legislation's various policy changes.

Additionally, both the House Ways and Means Committee and the Senate Finance Committee are likely to seek to build upon the SECURE Act's momentum and make additional reforms to retirement savings policies. Specifically, given his past positions, House Ways and Means Committee Chairman Richard Neal (D-MA) may well continue looking at auto enrollment issues. On the other side of the Capitol, the Senate Finance Committee is likely to build on legislation by Senators Rob Portman (R-OH) and Ben Cardin (D-MD), which includes nearly 60 provisions designed to, among other things: (1) increase savings in 401(k) plans and IRAs; (2) reduce barriers to lifetime income retirement options; and (3) help improve coverage in the small employer market and among part-time workers.

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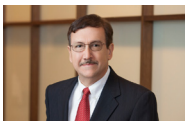

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