ASC ALERT

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IRS Provides Guidance on Changes under the SECURE and Miners Acts

The Internal Revenue Service (IRS) has issued guidance and clarifications on numerous changes brought about by the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act). IRS Notice 2020-68 (Notice) addresses issues relating to the participation of long-term, part-time (LTPT) employees in 401(k) plans, qualified birth or adoption distributions, the small employer automatic enrollment credit, difficulty of care payments as compensation, as well as other items. The Notice also provides guidance regarding the reduction in the minimum age for in-service distributions for pension plans as provided for under the Bipartisan American Miners Act of 2019 (Miners Act). Finally, it offers welcome relief for the timing of plan document amendments, particularly with respect to changes pursuant to the Miners Act. While the Notice does not offer comprehensive guidance, it provides some clarity for plan document providers, TPAs, plan sponsors and others involved with qualified retirement plans. The IRS indicates that it will continue to analyze the SECURE and Miners Acts and anticipates issuing further guidance.

Participation of Long-Term, Part-Time Employees in §401(k) Plans

Perhaps one of the more impactful SECURE Act changes is the provision that limits the period of service an employer maintaining a 401(k) plan may require an employee to complete as a condition of participation in the plan. This rule is often referred to as the long-term, part-time (LTPT) employee rule.

Under new Code §401(k)(2)(D), a 401(k) plan may not require employees to complete a period of service that extends beyond the close of the earlier of: (i) the later of attainment of age 21 or completion of a 12-month period during which the employee has completed at least 1,000 hours of service (consistent with the prior age and service eligibility rule); or (ii) the first period of three consecutive 12-month periods during each of which the employee has completed at least 500 hours of service. Under new Code §401(k)(15), the new LTPT employee rule will not apply unless an employee has attained age 21 by the close of the three consecutive 12-month periods.

Once a LTPT employee meets the age and service requirements, such employee must be able to commence participation no later than the earlier of: (i) the first day of the first plan year beginning after the date on which the employee satisfied the age and service requirements or (ii) the date 6 months after the date on which the individual satisfied those requirements.

ASC Insight: A LTPT employee that meets the new eligibility rule must be allowed to make salary deferrals under the employer's 401(k) plan. However, the new LTPT employee rule does not require a LTPT employee to be otherwise eligible to participate in the plan. Thus, the plan can continue to treat a LTPT employee as ineligible for employer nonelective and matching contributions until the employee has completed a year of service based on 1,000 hours of service.

Although the SECURE Act provides relief from certain nondiscrimination and top-heavy rules, the Notice does not address how plans may apply this relief. The IRS will need to provide future guidance so that plans may properly perform nondiscrimination and top-heavy testing.

This new LTPT employee rule applies for plan years beginning after December 31, 2020. However, 12-month periods of service beginning before January 1, 2021 are not considered in the new **eligibility** determination. The Notice clarifies, however, that the exclusion of 12-month periods prior to January 1, 2021 does not extend to crediting service for **vesting** purposes. Although employers are not required to make employer contributions or matching contributions to LTPT employees, if they are made for LTPT employees, all years of service with the employer generally will count for purposes of vesting. A LTPT employee will be credited with a year of service for purposes of vesting for each 12-month period during which the employee has completed 500 hours of service. Unless an exception exists (e.g. disregarding of years of service prior to age 18), a LTPT employee will receive credit for all service, including service prior to January 1, 2021 for purposes of vesting.

ASC Insight: This new LTPT employee rule necessitates the closer tracking of hours of service over a longer period of time for employees. For many employers, this will increase their administrative burden. Keep in mind that calculating service for LTPT employees may consider different periods of time depending on whether it is for purposes of eligibility or vesting. The IRS acknowledges the increased burden in administering this provision and is seeking comments on how to reduce the potential burden, particularly with respect to calculating vesting service for LTPT employees. ASC and other practitioners are drafting comment letters seeking relief from the recordkeeping burdens and answers to numerous LTPT employee issues that are not addressed in the Notice (e.g., how do the new rules apply when a plan uses elapsed time for crediting service?).

Fortunately, except for the tracking of hours, plan sponsors will not need to apply the new LTPT employee rules until the 2024 plan year - the first plan year that a plan must allow a LTPT employee to participate. This gives the IRS some time to issue further guidance and for plan sponsors to implement the LTPT employee requirements.

The new LTPT employee rule does not apply to collectively bargained plans.

Qualified Birth or Adoption Distributions

The SECURE Act provides an exception to the 10% additional tax (i.e., the early distribution penalty when a participant takes a distribution prior to an otherwise distributable event) for qualified birth or adoption distributions (QBADs) up to $5,000, from certain "applicable eligible retirement plans.". In addition, the SECURE Act allows individuals to recontribute the QBADs they receive, subject to certain requirements. Notice 2020-68 answers specific questions relating to individuals receiving QBADs.

With respect to individuals receiving QBADs, the following rules apply:

- A QBAD is any distribution from an "applicable eligible retirement plan" to an individual if made during the one-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.
- "Applicable eligible retirement plan" include 401(a) defined contribution plans, 403(a) annuity plans, 403(b) annuity contracts, governmental 457(b) plans and IRAs. Defined benefit plans may not permit QBADs.
- •An individual receiving a QBAD must include the name, age, and Taxpayer Identification Number (TIN) of the child or eligible adoptee on the individual's tax return for the taxable year of the distribution.
- An eligible adoptee is any individual (other than a child of the taxpayer's spouse) who has not attained age 18 or is physically or mentally incapable of self-support. Determining whether an individual is an eligible adoptee is done in the same manner as the disability determination for purposes of the exception to the 10% additional tax.
- A QBAD is included in an individual's gross income but is not subject to the 10% early distribution tax.
- Each parent may take a QBAD with respect to the same child or eligible adoptee.
- Individuals may take QBADs for multiple births or adoptions of eligible adoptees (e.g., twins, triplets, etc.).
- An individual receiving a QBAD may recontribute an amount equal to all or any portion of the QBAD to an applicable eligible retirement plan in which the individual is a beneficiary and to which a rollover can be made.

With respect to "applicable eligible retirement plans," the following rules apply:

- Employers maintaining applicable eligible retirement plans are not required to permit QBADs from their plans.
- A plan sponsor or plan administrator may rely on the reasonable representations from a participant, unless the plan sponsor or plan administrator has actual knowledge to the contrary.
- An applicable eligible retirement plan that permits QBADs must permit recontributions of such distributions if: (i) the individual received a contribution from that plan; and (ii) he/she is eligible to make a rollover to that plan at the time of the recontribution.
- Plans that allow QBADs do not violate otherwise applicable distribution restrictions.
- QBADs are not treated as eligible rollover distributions for purposes of the direct rollover rules under §401(a)(31), §402(f) notice purposes or §3405 mandatory withholding purposes. Therefore, plans are not required to offer individuals a direct rollover of QBAD amounts. Plan administrators are not required to provide a §402(f) notice to individuals requesting a QBAD, nor are they required to withhold 20% of the distribution, as otherwise required. QBADs, however, are subject to voluntary withholding.
- Even if a plan does not permit QBADs, an individual who receives an otherwise permissible in-service distribution and meets the requirements to take a QBAD may treat the distribution as a QBAD for federal tax purposes on his/her individual federal income tax return. In any case, a QBAD is not subject to the 10% early distribution tax.

ASC Insight: As explained later, plan amendments reflecting an employer's discretionary decision to allow for QBADs are not required immediately. Since we anticipate this provision will commonly be offered in plans and is available for plan years beginning after December 31, 2019, ASC clients should use our SECURE Act Operational Checklist to assist plan sponsors in documenting the operational implementation of QBADs.

Although helpful, Notice 2020-68 leaves many issues relating to QBADs unanswered. The IRS recognizes this and intends to issue guidance addressing additional QBAD issues, including the recontribution rules.

Reduction in Minimum Age for In-Service Distributions in Pension Plans

The Miners Act, which was included in the same legislative package as the SECURE Act, amends the Code to reduce the minimum age for in-service distributions from money purchase pension plans and defined benefit pension plans from age 62 to age 59½ and, from governmental 457(b) plans, from age 70½ to age 59½. These changes are effective for plan years beginning after December 31, 2019.

The Notice confirms these are optional provisions and that employers that maintain money purchase pension plans, defined benefit pension plans and governmental 457(b) plans are not required to implement in-service distributions at such reduced ages. For example, a money purchase pension plan that currently permits in-service distributions at age 62 is not now required to be amended to permit in-service distributions at age 59 ½.

The Notice emphasizes that the change allowing pension plans to reduce the in-service distribution age down to 59 ½ does not mean the plan's normal retirement age (NRA) may be reduced to age 59 ½. Under IRS regulations, a plan's NRA (which is important for ensuring a plan's benefits are definitely determinable) must be an age not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed. The IRS deems a NRA of at least age 62 to be reasonable. In the case of a NRA that is not earlier than age 55 and is earlier than age 62, whether the age is a reasonable NRA is based on all relevant facts and circumstances.

ASC Insight: Several commentators expressed concern that since the reduction of the in-service distribution age to age 59 ½ is discretionary, plan sponsors would need to amend their plans by the last day of the 2020 plan year to implement the earlier age. As explained below, the IRS provides that such an amendment may be delayed until the end of the 2022 plan year (or in some cases to the 2024 plan year), even if the employer operationally applies an earlier age earlier for the 2020 plan year or later.

Small Employer Automatic Enrollment Credit

The SECURE Act adds Code §45T, which provides a tax credit for eligible employers establishing eligible automatic contribution arrangements (EACAs) in their qualified plans. The new credit is $500 for any taxable year of an eligible employer during a credit period and is applicable for taxable years beginning after December 31, 2019.

An employer may establish an EACA in a 401(a) defined contribution plan, 403(a) annuity plan, a simplified employee pension under §408(k) (SEPs), or in a SIMPLE retirement account under §408(p). Governmental plans under §414(d) and plans maintained by tax-exempt employers are specifically excluded. In order to be eligible for the new credit, an eligible employer must have had no more than 100 employees who received $5,000 or more of compensation from the employer for the preceding year. The credit is available for a "credit period" defined as the period of three taxable years beginning with the first taxable year for which an eligible employer includes an EACA in a qualified plan it sponsors.

Notice 2020-68 includes several clarifications relating to the Code §45T.

- An eligible employer may not receive a credit with respect to taxable years in more than one three-year credit period as the credit is only available during a single three-year credit period that begins when the employer first includes an EACA in any qualified plan.
- An eligible employer must include the same EACA in the same plan for the second and third taxable years with the exception of a plan that is spun-off and continues the same EACA in its own plan.
- The credit applies separately to each eligible employer that participates in a multiple employer plan (MEP).

ASC Insight: The small employer automatic enrollment credit should encourage more employers, including participating employers in MEPs, to adopt EACAs. ASC's pre-approved 401(k) plans and 403(b) plans include IRS approved EACA and MEP provisions.

Employers interested in the Code §45T credit should consult with their tax advisors.

Difficulty of Care Payments as Compensation

The SECURE Act amends Code §415(c)(3) to include nontaxable "difficulty of care" payments as compensation for determining the Code §415 limits for an individual. "Difficulty of care" payments are only made to certain qualified foster care providers. This provision applies to both defined contribution and 403(b) plans and is applicable to contributions for plan years beginning after December 31, 2015.

The Notice clarifies compensation under Code §415(c)(3) only includes that of the individual's employer such that "difficulty of care" payments made by anyone, other than the employee's employer, are not included in the definition of compensation under the employer's plan.

ASC Insight: The change to Code §415 compensation to include difficulty of care payments will impact few defined contribution and 403(b) plans, such as plans that include home healthcare workers. If an employer does not make "difficulty of care" payments to its employees, then the employer's plan need not be amended to include them in the definition of compensation under the plan. ASC will include the revision to the Code §415 definition of compensation in its SECURE/CARES Acts interim amendment.

Deadlines for Plan Amendments

The SECURE Act provides a delayed plan amendment date for plan sponsors who implement the new SECURE Act rules, if certain conditions are satisfied:

1. The plan sponsor adopts the amendment no later than the last day of the first plan year beginning on or after January 1, 2022. (For collectively bargained plans and qualified governmental plans, the amendment can be delayed until the last day of the first plan year beginning on or after January 1, 2024.)
2. The amendment applies retroactively to the effective date of the SECURE Act provision or applicable regulation or, for discretionary SECURE Act provisions, the effective date specified in the plan.
3. The plan is operated as if the amendment were in effect during the period beginning on the effective date of the SECURE Act provision or applicable regulation or, for discretionary SECURE Act provisions, the effective date specified in the plan.

Notice 2020-68 provides clarification and, in the case of the Miners Act, relief for the timing of plan amendments.

ASC Insight: Perhaps the most important clarification is that the delayed plan amendment date applies to both **required and discretionary** plan amendments related to the SECURE Act and the Miners Act. Several commentators believed that employers had to adopt discretionary plan amendments (i.e., amendments not required by the law and optional on the part of the employer) by the end of the plan year for which the amendment was effective. Instead, the IRS has taken the position, similar to its position on amendments for the final hardship distribution regulations, that discretionary amendments related to the change in law or regulations receive the same delayed amendment deadlines as required amendments.

For **qualified plans** (i.e., plans qualified under Code §401(a)), the deadline to amend a plan for the SECURE Act, the regulations thereunder or for the change in the permissible in-service distribution age under the Miners Act is the last day of the first plan year beginning on or after January 1, 2022. For collectively bargained plans and qualified governmental plans, the amendment can be delayed until the last day of the first plan year beginning on or after January 1, 2024.

For **403(b) plans** not maintained by public schools, the deadline to amend a plan for provisions of the SECURE Act or the regulations thereunder is the last day of the first plan year beginning on or after January 1, 2022. For 403(b) plans maintained by public schools, the amendment can be delayed until the last day of the first plan year beginning on or after January 1, 2024.

For **457(b) governmental plans**, the deadline to amend a plan for the SECURE Act, the regulations thereunder or the change in the permissible in-service distribution age under the Miners Act is the later of (i) the last day of the first plan year beginning on or after January 1, 2024, or (ii) if applicable, the first day of the first plan year beginning more than 180 days after the date of notification by the IRS that the plan was administered in a manner inconsistent with requirements of Code §457(b).

ASC Insight: This guidance is particularly good news for money purchase pension plans and defined benefit plans for which there was concern that an interim amendment might

need to be adopted in 2020 with respect to the change in the permissible in-service distribution age under the Miners Act. The timing of these amendment deadlines offers employers and retirement plan providers additional time to adopt interim amendments as well as evaluate and implement both required and discretionary changes. Given the timing of the Cycle 3 pre-approved defined contribution plan restatement period with a deadline of July 31, 2022, some may coordinate both the Cycle 3 plan document restatement with the required SECURE Act interim amendment. Since the IRS anticipates the release of further guidance, ASC continues to review and evaluate guidance, as released, and will be preparing a singular interim amendment incorporating the SECURE Act, the Miners Act, and the Coronavirus Aid, Relief, and Economic Security Act (CARES Act).

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