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The IRS Releases Grab Bag Guidance on the SECURE 2.0 Act

The Bottom Line

- The IRS released guidance regarding some of the mandatory and optional changes to qualified retirement plans under the SECURE 2.0 Act of 2022.
- Plan sponsors should speak to ERISA counsel to understand the practical implications of the guidance.

Almost a year after the SECURE 2.0 Act of 2022 was enacted as part of the Consolidated Appropriations Act, 2023, the IRS released guidance (Notice 2024-2) in the form of a grab bag Q&A aptly named "Miscellaneous Changes Under the SECURE 2.0 Act of 2022." The Notice covers a variety of topics including mandatory automatic enrollment, Roth employer contributions, offering *de minimis* financial incentives, terminal illness distributions and plan corrections for missed deferrals.

Additional guidance is expected on the SECURE 2.0 Act of 2022's other provisions, including the requirement that all catch-up contributions made by high wage earners are subject to Roth tax treatment (the IRS delayed this requirement until 2026).

Automatic Enrollment (Mandatory)

Any 401(k) or 403(b) plan established on or after December 29, 2022 (the "Enactment Date") must include an automatic enrollment feature for its cash or deferred arrangement (CODA) (i.e., employee contribution feature) to be qualified.

- **Plan Established Date**: The key date in determining whether a plan is required to include an automatic enrollment feature is the date that the plan was established – not when the employee contribution

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feature became effective. For example, if an employer adopted a plan on October 3, 2022, with an employee contribution feature effective on January 1, 2023, the plan would not be required to include an automatic enrollment feature since the plan was established before the Enactment Date.

- **Plan Mergers**: If two pre-Enactment Date plans, each containing an employee contribution feature, merge together, the resulting plan would not be required to include an automatic enrollment feature. In fact, if in connection with a merger or acquisition, a post-Enactment Date plan is merged into a pre-Enactment Date plan, the resulting plan would also not be required to include an automatic enrollment feature. This is true as long as the plans are maintained by entities in the same controlled group and the plan merger was completed by the last day of the plan year beginning after the corporate event.
- **Spin Offs**: If a plan is formed by spinning off assets from a single employer pre-Enactment Date plan, then the spun-off plan will also be treated as a pre-Enactment Date plan.
- **Multiple Employer Plans**: If an employer adopts a pre-Enactment Date multiple employer plan (e.g., a plan maintained by a professional employer organization (PEO)) on or after the Enactment Date and includes an employee contribution feature in its adoption agreement, then the adopting employer would need to include an automatic enrollment feature with respect to its participation in the multiple employer plan. Similarly, if an employer that adopted a PEO plan on or after the Enactment Date decides to spin-off its assets from the PEO plan, the new spun off plan would be required to include an automatic enrollment feature regardless of when the PEO plan was established if the new spun off plan includes an employee contribution feature.

Roth Employer Contributions (Optional)

A plan sponsor may amend its 401(k) or 403(b) plan to allow an employee to elect to have any employer contribution (matching and profit sharing contributions) designated as a Roth contribution.

- **Election Timing**: Any designation of an employer contribution as a Roth contribution must be made by the employee no later than the time that the contribution is allocated to the employee's account and must be irrevocable. Employees must be able to make (or change) that designation at least once per plan year.
- **Vesting Requirements**: Only employees who are *fully* vested in the applicable employer contribution (e.g., matching or profit sharing contributions) at the time such contribution

is allocated to the employee's account may designate such employer contributions as Roth contributions. For example, if at the time matching and profit sharing contributions are allocated to the employee's account, and the employee is fully vested in matching contributions but only partially vested in profit sharing contributions, the employee may only designate the matching contribution as a Roth contribution. Plans that limit these Roth elections to fully vested employees will not be treated as providing a discriminatory benefit, right or feature.

- **Reporting and Withholding**: Roth employer contributions are not included as income for purposes of federal income tax withholding, FICA, or FUTA. Roth employer contributions are simply reported using Form 1099-R for the year in which the contributions are allocated to the individual's account.
- **Other Roth Features**: A plan that allows Roth employer contributions is not required to have other Roth features (e.g., Roth deferrals and/or in-plan Roth conversions).

De Minimis Financial Incentives (Optional)

Employers are now permitted to offer a *de minimis* financial incentive (not derived from plan assets) up to $250 to employees to encourage employees to make contributions to a 401(k) or 403(b) plan maintained by the employer.

- **Eligible Employees**: A *de minimis* financial incentive may only be offered to employees who have not elected to contribute to the plan.
- **Installments**: The *de minimis* financial incentive may be provided in the form of installments that are contingent on the employee's continuing to make contributions to the plan (even if those installments are paid over more than one plan year). For example, if an employer provides a $100 gift card to an eligible employee with a promise to provide an additional $100 gift card a year later, but only if the employee continues to make contributions at that later date, then the $200 total amount of gift cards is still a permissible *de minimis* financial incentive.
- **Tax Treatment**: A *de minimis* financial incentive is generally includible in the employee's gross income and wages and is subject to applicable withholding and reporting requirements for employment tax purposes (unless an exception applies).

Terminal Illness Distributions (Optional)

An employee who is considered a terminally ill individual may receive a distribution from a 401(k) or 403(b) plan on or after the date on which the employee has been certified by a physician as having a terminal illness without being subject to a 10% early distribution tax.

- **Physician Certification**: A plan may not rely on an employee's self-certification of a terminal illness or physical condition. A physician certification of an employee's terminal illness must include: (1) a statement that the individual's illness or physical condition can be reasonably expected to result in death in 84 months or less after the date of certification; (2) a narrative description of the evidence that was used to support the statement of illness or physical condition; (3) the certifying physician's name and contact information; (4) the date the physician examined the individual or reviewed the evidence provided by the individual, and the date that the certification is signed by the physician and (5) the certifying physician's signature, and an attestation from the certifying physician that the physician confirms that the physician composed the narrative description based on the physician's examination of the individual or the physician's review of the evidence provided by the individual.
- **Distribution Amount**: There is no limit on the amount that an employee is permitted to receive as a terminally ill individual distribution.
- **Repayment of the Distribution**: At any time during the three-year period beginning on the day after the date on which the distribution was received, an employee may recontribute any portion of a terminally ill individual distribution (up to the entire amount of the terminally ill individual distribution) to a qualified retirement plan in which the employee is a beneficiary and to which a rollover can be made.
- **Reclassified In-service Distribution**: If a plan does not permit terminally ill individual distributions and an employee receives an otherwise permissible in-service distribution (e.g., a hardship distribution) that meets the requirements of a terminally ill individual distribution, the employee may treat the distribution as a terminally ill individual distribution on the employee's federal income tax return, thereby avoiding the 10% tax on early distributions.

Safe Harbor for Plan Corrections for Missed Deferrals

The SECURE 2.0 Act created a permanent safe harbor for 401(k) and 403(b) plans that contain an automatic enrollment or automatic escalation feature that either failed to enroll a participant in accordance with the feature or improperly excluded an individual from a plan. This safe harbor mirrors a similar safe harbor under the IRS's Employee Plans Compliance Resolution System (EPCRS) that was set to expire at the end of 2023. Additionally, the IRS clarified that this safe harbor is available even for terminated employees.

For More Information

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