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Retirement Investors Get Another Boost from Washington

SECURE 2.0 will usher in many changes for retirement plans and IRAs over the next several years.

This information is not intended for tax, legal, investment, or retirement advice or recommendations.

Amid the 1,650-page, $1.7 trillion omnibus spending legislation passed by Congress last week and expected to be signed by President Biden were several provisions affecting work-sponsored retirement plans and, to a lesser degree, IRAs. Dubbed the SECURE 2.0 Act of 2022 after the similarly sweeping Setting Every Community Up for Retirement Enhancement Act passed in 2019, the legislation is designed to improve the current and future state of retiree income in the United States.

"This important legislation will enhance the retirement security of tens of millions of American workers — and for many of them, give them the opportunity for the first time to begin saving," said Brian Graff CEO of the American Retirement Association.

What Does the Legislation Do?

The following is a brief summary of some of the most notable initiatives. All provisions take effect in 2024 unless otherwise noted.

- **Later age for required minimum distributions (RMDs).** The 2019 SECURE Act raised the age at which retirement savers must begin taking distributions from their traditional IRAs and most work-based retirement savings plans to 72. SECURE 2.0 raises that age again to 73 beginning in 2023 and 75 in 2033.
- **Reduction in the RMD excise tax.** Current law requires those who fail to take their full RMD by the deadline to pay a tax of 50% of the amount not taken. The new law reduces that tax amount to 25% in 2023; the tax is further reduced to 10% if account holders take the full required amount and report the tax by the end of the second year after it was due and before the IRS demands payment.
- **No RMDs from Roth 401(k) accounts.** Bringing Roth 401(k)s and similar employer plans in line with Roth IRAs, the legislation eliminates the requirement for savers to take minimum distributions from their work-based plan Roth accounts.
- **Higher limits and looser restrictions on qualified charitable distributions from IRAs.** The amount currently eligible for a qualified charitable distribution from an IRA ($100,000) will be indexed for inflation. In addition, beginning in 2023, investors will be able to make a one-time charitable distribution of up to $50,000 from an IRA to a charitable remainder annuity trust, charitable remainder unitrust, or charitable gift annuity.[1]
- **Higher catch-up contributions.** The IRA catch-up contribution limit will be indexed annually for inflation, similar to work-sponsored catch-up contributions. Also, starting in 2025, people age 60 to 63 will be able to contribute an additional minimum of $10,000 for 401(k) and similar plans (and at least $5,000 extra for SIMPLE plans) each year to their work-based retirement plans. Moreover, beginning in 2024, all catch-up contributions for those making more than $145,000 will be after-tax (Roth contributions).
- **Roth matching contributions.** The new law permits employer matches to be made to Roth accounts. Currently, employer matches must go into an employee's pre-tax account. This provision takes effect immediately; however, it may take some time for employers to amend their plans to include this feature.
- **Automatic enrollment and automatic saving increases.** Beginning in 2025, the Act requires most new work-sponsored plans to automatically enroll employees with contribution levels between 3% and 10% of income, and it automatically increases their savings rates by 1% a year until they reach at least

10% (but not more than 15%) of income. Workers will be able to opt out of the programs.

- **Emergency savings accounts.** The legislation includes measures that permit employers to automatically enroll non-highly compensated workers into emergency savings accounts to set aside up to $2,500 (or a lower amount that an employer stipulates) in a Roth-type account. Savings above this limit would go into the employee's Roth retirement account, or, if one does not exist, would not be accepted.
- **Matching contributions for qualified student loan repayments.** Employers may help workers repaying qualified student loans simultaneously save for retirement by investing matching contributions in a retirement account in the employee's name.
- **529 rollovers to Roth IRAs.** People will be able to directly roll over up to a total of $35,000 from 529 plan accounts to Roth IRAs for the same beneficiary, provided the 529 accounts have been held for at least 15 years. Annually, the rollover amounts would be subject to Roth IRA contribution limits.[2]
- **New exceptions to the 10% early-withdrawal penalty.** Distributions from retirement savings accounts are generally subject to ordinary income tax. Moreover, distributions prior to age 59½ also may be subject to an early-withdrawal penalty of 10%, unless an exception applies. The law provides for several new exceptions to the early-withdrawal penalty, including an emergency personal expense, terminal illness, domestic abuse, to pay long-term care insurance premiums, and to recover from a federally declared disaster. Amounts, rules, and effective dates differ for each circumstance.
- **Saver's match.** Low- and moderate-income savers currently benefit from a tax credit of up to $1,000 ($2,000 for married couples filing jointly) for saving in a retirement account. Beginning in 2027, the credit is re-designated as a match that will generally be contributed directly into an individual's retirement account. In addition, the match is allowed even if taxpayers have no income tax obligation.
- **More part-time employees can participate in retirement plans.** The SECURE Act of 2019 required employers to allow workers who clocked at least 500 hours for three consecutive years to participate in a retirement savings plan. Beginning in 2025, the new law reduces the second component of that service requirement to just two years.
- **Rules for lifetime income products in retirement plans.** The Act directs the IRS to ease rules surrounding the offering of lifetime income products within retirement plans. Moreover, the amount that plan participants can use to purchase qualified longevity annuity contracts will increase to $200,000. The current law caps that amount at 25% of the value of the retirement accounts or $145,000, whichever is less. These provisions take effect in 2023. Qualified annuities are typically purchased with pre-tax money, so withdrawals are fully taxable as ordinary income, and withdrawals prior to age 59½ may be subject to a 10% penalty tax.
- **Retirement savings lost and found.** The Act directs the Treasury to establish a searchable database for lost 401(k) plan accounts within two years after the date of the legislation's enactment.
- **Military spouses.** Small businesses that provide immediate enrollment and vesting to military spouses in an eligible retirement savings plan will qualify for new tax credits. This provision takes effect immediately.

These provisions represent just a sampling of the many changes that will be brought about by SECURE 2.0. We look forward to providing more details and in-depth analysis applying to both individuals and business owners in the weeks to come.

Sources: *The Wall Street Journal,* CNBC, Bloomberg, *Kiplinger, Fortune, Plan Sponsor* magazine, National Association of Plan Advisors, and the SECURE 2.0 Act of 2022

[1] Bear in mind that not all charitable organizations are able to use all possible gifts. It is prudent to check first. The type of organization you select can also affect the tax benefits you receive.

[2] As with other investments, there are generally fees and expenses associated with participation in a 529 savings plan. There is also the risk that the investments may lose money or not perform well enough to cover college costs as anticipated. Investment earnings accumulate on a tax-deferred basis, and withdrawals are tax-free as long as they are used for qualified education expenses. For withdrawals not used for qualified education expenses, earnings may be subject to taxation as ordinary income and possibly a 10% tax penalty. The tax implications of a 529 savings plan should be discussed with your legal and/or tax professionals because they can vary significantly from state to state. Also be aware that most states offer their own 529 plans, which may provide advantages and benefits exclusively for their residents and taxpayers. These other state benefits may include financial aid, scholarship funds, and protection from creditors. *Before investing in a 529 savings plan, please consider the investment objectives, risks, charges, and expenses carefully. The official disclosure statements and applicable prospectuses - which contain this and other information about the investment options, underlying investments, and investment company - can be obtained by contacting your financial professional. You should read these materials carefully before investing.*