A SUMMARY OF THE SECURE 2.0 ACT OF 2022

PROVISIONS IMPACTING INDIVIDUALS

On December 29, 2022, the SECURE 2.0 Act was signed into law. The legislation expands on many retirement planning areas addressed by the original SECURE Act of 2019.

While some of the details still need to be clarified by various government agencies, the new law makes some significant changes in several retirement and tax planning areas. Here is a summary of 17 of the provisions that are most impactful to individuals, what is changing, and when they go into effect.

DISTRIBUTION RULE CHANGES

Further Increase to Required Minimum Distribution (RMD) Age

When the original SECURE Act passed in 2019, the age to start RMDs from certain retirement accounts was raised from the longstanding age of 70½ to age 72. **The SECURE 2.0 Act further raises the RMD age.** For individuals who turn 72 after December 31, 2022, and 73 before January 1, 2033, the RMD age is 73. For individuals who turn 75 after December 31, 2032, the RMD age is 75. Those who turned 72 in 2022 will still need to satisfy their first RMD by April 1, 2023.

Note: The actual provision contains a perceived error in the dates for someone born in 1959. It is expected that a technical correction will be issued in the future to correct it.

Elimination of RMDs for Employer Plan Roth Accounts

Under current law, employer plan Roth accounts, such as Roth 401(k) and Roth 403(b), are subject to the same RMD rules as all other accounts in an employer plan. **Starting in 2024, Roth accounts in employer plans will no longer require RMDs during the owner's life**, aligning them with the rules of Roth IRAs.

Note: RMDs for employer plan Roth accounts will still be due for 2022 and 2023.

Reduction in the Missed RMD Penalty

Under prior law, missed RMDs were subject to a **50%** penalty of the amount not taken. **Starting in 2023, the penalty is reduced to 25%.** If the mistake is deemed to be corrected in a timely manner, the penalty can be further reduced to **10%.**

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Additional Surviving Spouse Distribution Option

Under current law, a surviving spouse has several options to choose from when determining how to inherit a qualified account from a deceased spouse. The SECURE 2.0 Act adds one more option to the list. **Starting in 2024, a surviving spouse will be allowed to elect the option to be treated as their deceased spouse.** This means they can use their deceased spouse's date of birth to calculate RMDs. This could be beneficial for a surviving spouse who is older than his or her deceased spouse. Another benefit to this election is that it does not eliminate the stretch option for an eligible designated beneficiary of the surviving spouse.

Substantially Equal Periodic Payment Exception Changes (also known as 72(t) distributions)

Under current law, any account that is being used for a 72(t) distribution is not eligible for a partial rollover or partial transfer. A rollover or transfer of anything less than the entire account balance results in a material modification of the 72(t) distribution, resulting in retroactive penalties. **Under the SECURE 2.0 Act, starting in 2024, partial rollovers or transfers of such accounts will not result in a penalty provided that the aggregate distributions taken from the original and the new account satisfy the 72(t) requirement.** Example: An individual has an IRA at company ABC currently receiving a 72(t) distribution. Starting in 2024, he or she could transfer part of it to an IRA at company XYZ, and if the combined distributions from the accounts at ABC and XYZ meet the 72(t) requirement, it would not be considered a material modification. Since the aggregate distribution amount does not change, neither account is subject to retroactive penalties.

CONTRIBUTION RULE CHANGES

Traditional and Roth IRA Catch-Up Contributions To Be Indexed to Inflation

Under current law, the Traditional and Roth catch-up contribution limit for those age 50 and over is a flat $1,000 not adjusted for inflation. **Starting in 2024, the catch-up contribution will be adjusted annually for inflation in $100 increments.**

Employer Roth Contributions

Under prior law, all employer contributions to an employer-sponsored plan were treated as pretax contributions. **After the passing of the SECURE 2.0 Act,** employees can elect to have these contributions directed to a Roth option. While this is effective immediately, the IRS will likely need to issue additional guidance before employers and administrators can accommodate the change in rules.

Mandatory Roth Catch-Up Contributions for High Earners

Not only will the SECURE 2.0 Act allow more flexibility for Roth contributions in employer plans, it will also require certain high-income individuals wishing to make catch-up contributions, to do so on an after-tax basis. **Starting in 2024, individuals aged 50 and older whose wages exceed $145,000** (indexed annually for inflation) in the previous year from the employer sponsoring the plan, **will be required to make catch-up contributions on a Roth basis.** In other words, the catch-up contribution, if made, will be included in their taxable income, and cannot be made on a pretax basis.

Note: This rule change only pertains to 401(k), 403(b), and governmental 457(b) plans, not Traditional or SIMPLE IRAs. What is also not specifically addressed is the scenario in which someone changes jobs and does not have income from their current employer in the previous year, or if he or she has income from multiple employers that, in aggregate, exceeds the limit.

Increased Employer Plan Catch-Up Contributions for Those Aged 60, 61, 62, and 63

Starting in 2025, individuals aged 60, 61, 62, and 63 participating in an employer plan with a salary deferral component will be eligible for an additional catch-up contribution. For 401(k) and 403(b) plans, the catch-up contribution limit will be increased to the greater of $10,000 (indexed annually for inflation) or 150% of the regular catch-up contribution limit for the year. **For individuals making salary deferral contributions in a SIMPLE IRA, the catch-up limit will be increased by the greater of $5,000 (indexed annually for inflation) or 150% of the regular SIMPLE IRA catch-up contribution for the year.**

Note: As described above, some individuals will be required to make catch-up contributions on a Roth basis. There may be a perceived drafting error in this provision that would disallow catch-up contributions. A technical correction is expected at some point.

Roth Contributions for SEP and SIMPLE IRAs

Beginning in 2023, the SECURE 2.0 Act allows Roth contributions to both SEP and SIMPLE IRAs. In the past, all contributions to these accounts were made on a pretax basis. Moving forward, any amount allocated to a Roth option will be included in the taxpayer's income for the year. Even though the SECURE 2.0 Act authorizes these types of accounts starting January 1, 2023, it may take some time before custodians and employers can accommodate these elections.

Matching Contributions on Qualified Student Loan Payments

Starting in 2024, the SECURE 2.0 Act will allow employers to treat qualified student loan payments made by the employee as elective deferrals in determining a matching contribution in an employer-sponsored plan. This provision will allow employees to take advantage of a company's match even if they are not contributing to the plan because they are making student loan payments, or if they are not contributing enough to receive the full match.

OTHER PROVISIONS

New Exceptions to the 10% Early Withdrawal Penalty

The SECURE 2.0 Act added a number of new exceptions to the 10% early withdrawal penalty. Some of the new exceptions include:

- **Qualified Disaster Recovery Distributions**

  If an individual's primary place of residence is within a federally declared disaster area, he or she is allowed to distribute a maximum of $22,000 from qualified retirement accounts free of the 10% penalty. The distribution must be taken within 180 days of the disaster and can be included in income either in the year of the distribution or ratably over three years beginning in the year of the distribution. Amounts taken under this exception can be paid back within three years to avoid taxation. This exception can be applied retroactively to disasters occurring after **January 26, 2021.**

- **Terminal Illness**

  Starting in 2024, if an individual is certified by a physician as having an **illness or condition which can reasonably be expected to result in death within 84 months or less,** he or she may be eligible for the terminal illness exception.

- **Domestic Abuse**

  Starting in 2024, victims of domestic abuse will be able to withdraw up to: the lesser of 50% of their vested balance, or $10,000 (indexed for inflation) from a defined contribution plan, **free of the 10% penalty.** To avoid potential taxation, the amount can be repaid within three years of the withdrawal.

- **Emergency Withdrawal**

  Starting in 2024, individuals who experience an unforeseeable or immediate financial need relating to necessary personal or family emergency expenses may be able to withdraw money from a qualified account without penalty. The amount of the withdrawal is capped at **$1,000** and only one emergency withdrawal will be permitted each calendar year. In addition, if someone has already taken an emergency withdrawal, to be eligible to take a subsequent withdrawal, one of the following will need to occur:

  - The individual has fully repaid the prior emergency withdrawal;
  - Three years have passed since the last emergency withdrawal; or
  - The individual's regular contributions since the withdrawal have exceeded the amount of the withdrawal.

529 to Roth IRA Transfers

The SECURE 2.0 Act is ushering in a new type of tax-free transfer/rollover. **Starting in 2024, individuals will be allowed to transfer/rollover funds directly from a 529 savings account to a Roth IRA.** This was initially proposed in the *College Savings Recovery Act of 2017* and has now finally been made law as part of the SECURE 2.0 Act. While it is potentially a good option for leftover education funds, it comes with many limitations.

- The 529 account must be open for at least 15 years.
- Any contributions made in the last five years, and any earnings associated with those contributions, are ineligible for transfer.
- The funds must be transferred to a Roth IRA in the name of the 529 account's beneficiary (not the owner).
- The amount that can be transferred each year is the beneficiary's IRA contribution limit for that year, meaning the beneficiary must have earned income.
- Any regular IRA contributions made each year decrease the amount available for transfer. Example: If the beneficiary has a Roth IRA contribution limit of **$6,500** for the year, but they make a **$2,000** Roth IRA regular contribution, only **$4,500** could be transferred from the 529 to the Roth for that year.
- The maximum transfer allowed per individual's lifetime is **$35,000.**

The idea behind this new allowed transfer seems straightforward. If a beneficiary has leftover funds in a 529 account that were not used for college, they can be transferred to a Roth IRA to be used for retirement instead. It encourages education savings in 529 accounts, with some level of protection against having to pay penalties if the beneficiary doesn't end up using it all for education, or they choose to not attend college at all.

Note: There are many unanswered questions about this new provision that will require future guidance to determine exactly how to interpret the nuances of this new rule.

Emergency Savings Account in Employer Plans

Starting in 2024, employer-sponsored retirement plans, such as 401(k) and 403(b), will be allowed to offer participating employees an emergency-linked savings account to be used for unanticipated expenses. Employees who are not a more than 5% owner in the business, not in the top 20% of compensation for the employer, and not a highly compensated employee (**$135,000** for 2023) will be allowed to contribute a maximum of **$2,500** to these accounts. These emergency savings accounts will be linked to the existing employer-sponsored plan and will count as deferred salary for purposes of matching employer contributions. Contributions will be treated as being made after tax, and distributions will be tax- and penalty-free.

Note: There are still aspects of this new provision that need to be clarified.

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