Q4 2023

REGULATORY Update

IRS Grants Relief for Roth Catch-Ups

Plan sponsors and their service providers now have a two-year reprieve before they must implement the new Roth catch-up contribution mandate. The SECURE 2.0 Act of 2022 changed the catch-up contribution rules so that participants aged 50 and older who earned $145,000 or more in FICA wages in the prior year may only make after-tax Roth catch-up contributions, effective January 1, 2024.

While this rule change seems simple, it's proving difficult for plan sponsors, payroll providers, and recordkeepers to implement because the IRS has not yet provided details on how to administer or apply this mandate. With outstanding questions and no guidance, few plans and service providers have been able to make the necessary process and systems changes to implement the Roth mandate by 2024.

In response to numerous requests for relief, the IRS is providing a two-year "administrative transition period" so that plans will not have to implement Roth catch-up contributions until January 1, 2026. For 2024 and 2025, plans will be deemed to meet the compliance requirements of this SECURE 2.0 provision if they continue to allow all participants aged 50 and older to make pretax catch-up contributions, even those earning more than $145,000, and even if the plan does not offer Roth accounts.

In its announcement of this relief, Notice 2023-62, the IRS also confirmed that catch-up contributions will not be eliminated beginning in 2024, as had been feared based on a SECURE 2.0 drafting error.

Questions and Comments

In advance of releasing much-needed guidance on this new mandate, the IRS also provided some insight into its current position on the following outstanding issues:

- Workers who do not receive wages subject to FICA (e.g., sole proprietors) would not be subject to this mandate
- A plan could treat a participant's election to make pretax catch-up contributions as an election to make Roth catch-up contributions if the participant is deemed subject to the Roth mandate
- A participant who works for more than one employer participating in the same multiple-employer plan would not have to aggregate their wages from multiple employers to determine if they are subject to the Roth catch-up mandate

The IRS requests industry comments on these and other related issues by October 24, 2023. Comments are specifically requested on the issue of whether plans that do not want to offer Roth accounts can comply with the law change by restricting catch-up contribution eligibility to those who earn less than $145,000.

Continued Relief for Missed Beneficiary Payments

The rules for beneficiaries inheriting qualified retirement savings changed drastically beginning in 2020. The IRS proposed regulations to interpret and provide guidance on these big rule changes in 2022 but surprised the retirement plan industry with its interpretation of one provision. With these regulations still in a proposal state and much of the industry questioning the IRS's interpretation, plan sponsors and beneficiaries are still unsure whether certain payments are required each year. The IRS had previously provided relief for plans and beneficiaries for missed payments in 2021 and 2022 and now has issued Notice 2023-54 to provide the same relief for 2023. This relief gives plan sponsors and beneficiaries who fall into this specific scenario assurance that they will not be penalized for not making an annual payment in 2021, 2022, or 2023.

Where the Confusion Lies

The SECURE Act of 2019 changed the retirement plan beneficiary payment options to require most nonspouse beneficiaries to deplete inherited accounts within 10 years of the plan participant's death. This new 10-year rule was assumed to operate the same as the old 5-year rule, such that beneficiaries could take payments at will or even leave the account intact as long as it is depleted by the end of the 10th year. But the IRS's proposed regulations require beneficiaries subject to the new 10-year rule to take a life expectancy payment from the inherited account each year in addition to depleting the account within 10 years if they inherited from a participant who died after their required beginning date for taking RMDs. Essentially, once a plan participant is required to start annual payments, the beneficiary inheriting the account must continue taking annual payments over a term no longer than 10 years.

Because of the confusion over the interpretation of the 10-year rule, the IRS is providing relief from the excise tax that would apply for a missed beneficiary payment. The IRS is also providing relief to defined contribution plans that failed to make these payments as required under the proposed regulations, stating the plan will not be treated as having a qualification failure merely because a payment was not made.

This relief applies to beneficiaries who are required to follow the 10-year rule and who inherited a plan account from:

- A participant who died in 2020, 2021, or 2022 after their required beginning date, or
- Another beneficiary who was taking life expectancy payments and died in 2020, 2021, or 2022

The IRS notice also states that the final regulations—when issued—will not be effective before 2024.

RMD Relief for Participants Born in 1951

With Notice 2023-54, the IRS also provides relief for plan participants who were born in 1951 and are expected to begin taking RMDs at age 72 in 2023. Although SECURE 2.0 raised the RMD starting age to 73, effective in 2023, the law was passed so close to the start of 2023 that many plans could not reprogram their systems in time to stop RMDs being paid to these individuals in 2023 or to report them as distributions eligible for rollover rather than RMDs. The IRS provides relief for plans that made these payments by indicating the plans will not be deemed to have failed to comply with the rules for making rollover eligible distributions, including tax withholding and reporting. The relief also allows participants who mistakenly received an RMD between January 1 and July 31, 2023, to roll it back into the plan by September 30, 2023.

Self-Correcting Plan Errors Now Easier

The IRS has long provided the Employee Plans Compliance Resolution System (EPCRS) to help plan sponsors correct operational, demographic, and document errors in plan administration. Plan sponsors could follow one of three programs under EPCRS, depending on the type and severity of the error, to correct the mistake and bring the plan back into compliance. Only certain types of errors could be self-corrected under EPCRS, but this prong of the corrections program allowed plan sponsors to correct the problem following a method laid out in EPCRS without having to contact the IRS or pay a sanction for committing the error.

SECURE 2.0 changed the rules for self-correction under EPCRS, making it easier for plan sponsors to self-correct more types of errors (e.g., loan errors). The IRS, not yet ready to roll out an overhaul to its corrections program, has published interim guidance in Notice 2023-43, which plan sponsors can rely on in the meantime to take advantage of the SECURE 2.0 changes.

Under SECURE 2.0 and Notice 2023-43, plan sponsors may self-correct most "Eligible Inadvertent Failures" (EIFs) regardless of the type of failure or when it occurred, including errors that occurred prior to the enactment of SECURE 2.0. An EIF is generally a failure that occurs despite the existence of internal controls the plan has implemented to maintain compliance and avoid potential errors. An EIF cannot be egregious, relate to the diversion or misuse of plan assets, or directly or indirectly relate to an abusive tax avoidance transaction. A correction must be made within a "reasonable period," the definition of which depends on the facts and circumstances of the error. Corrections made within 18 months of when the error was discovered will be deemed to have been made within a reasonable time.

Plan sponsors may self-correct an EIF using an applicable correction method from the existing EPCRS guidance or another reasonable method that is not expressly prohibited under EPCRS if they satisfy certain conditions:

- Have established practices and procedures reasonably designed to promote and facilitate compliance with applicable tax code requirements
- Identify the error and demonstrate a commitment to self-correction before the IRS identifies the problem
- Restore the plan or participants to the position in which they would have been had the failure not occurred, using a correction method that is reasonable and appropriate for the failure

Plan sponsors should review their internal controls to ensure that each area of plan administration has processes and procedures in place to help prevent errors. If an error is discovered, plan sponsors may want to engage a plan correction professional to make certain the error can be self-corrected under this guidance and to evaluate the correction options. Additionally, plan sponsors must document the following in writing to self-correct under this interim guidance:

- The failure, the date it was identified, the years in which it occurred, and the number of employees affected
- An explanation of how the failure occurred and proof that the plan had practices and procedures in place to facilitate compliance
- The correction method used and proof that the correction was made
- Changes to practices and procedures that will be implemented to avoid recurrence of the failure

Available in 2024: Matching Contributions Based on Student Loan Payments

One of the most anticipated provisions of SECURE 2.0 is the new option for employers to help their employees who may be struggling to pay down student loans and save for retirement because they can't afford to do both. Although other options exist for employers to help their employees pay for the cost of higher education, such as tuition reimbursement plans and student loan assistance, this new provision is different and potentially less expensive for the employer.

Effective January 1, 2024, employers who make matching contributions to a 401(k) plan, 403(b) plan, governmental 457(b) plan, or SIMPLE IRA may calculate those contributions based on an employee's student loan payments for the year instead of (or in addition to) any salary deferrals the employee made to the plan. To be clear, this is not an additional payment or benefit for that employee. It is simply a matching contribution the employer would have otherwise been obligated to make if the employee made salary deferrals into the plan and was eligible to receive a matching contribution.

Further IRS guidance is needed to flesh out the details, but plan sponsors considering adopting this feature should know the following:

- Matching contributions may be made into the plan based on qualified student loan payments (QSLPs). A QSLP is a payment made by an employee in repayment of a qualified education loan incurred by the employee to pay for qualified higher education expenses.
- Only QLSPs up to the deferral limit (or the employee's salary if less), reduced by the amount of any deferrals made, may be considered for the QLSP match each year.
- Plan sponsors may rely on an annual employee certification as to the amount of QSLPs and may establish an annual deadline (no earlier than three months after the end of the plan year) by which a claim for a QSLP match must be made.
- Employers must provide the QSLP match on at least an annual basis and can make the QSLP match at a different frequency than it makes other matching contributions (e.g., per payroll).
- If QSLP matches are made, they must be available to all employees eligible to receive a matching contribution on salary deferrals.
- The matching and vesting rates for QLSP matches must be the same as those that apply for matching contributions on salary deferrals.
- Employees receiving a QLSP match may be tested separately for nondiscrimination.

We Can Help

We are ready to provide you with the ideas, guidance, and foresight to position your firm for success. If you would like to review your plan's features or operations, or industry developments that may affect your plan, we're here to assist you.