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SECURE 2.0 – PROVISIONS THAT MAY IMPACT YOU BEFORE 2024

The SECURE 2.0 regulations passed in the last week of 2022 introduced a lot of changes to retirement plans. Some are optional and some will be phased in over the next few years. There are a few that are important to update you about now because **you may need to act on them before the start of 2024**. The Winter 2023 Newsletter on our website, www.crepen.com, has a longer list of the changes, but these are the key ones that will affect plans in the next few months.

LONG TERM PART TIME EMPLOYEES (LTPTE)

Let's start with the most complicated one ***and the one that probably requires the most action on your part***. If you have a 401(k) plan with an hours of service eligibility provision for plan entry, then starting January 1, 2024 you will also have to allow "long term, part time employees" into the plan for deferral purposes only. (If your plan doesn't offer deferral contributions, this won't affect you.) These employees will also need to be automatically enrolled, if you have that provision in your plan.

An LTPTE is someone who, starting in 2021, has worked at least 500 hours in three consecutive years. You ignore any time period before 2021 for this determination, and the first "year" is the employee's first 12 months (we recommend that successive periods shift to the plan year for ease in review). Here are some examples:

Example 1: Ted was hired in 2019 and has worked 700 hours every year since. We ignore the years before 2021. He has three consecutive years with at least 500 hours since 2021: 2021, 2022, and 2023. Therefore, he is allowed to defer on 1/1/24, and you must give him the opportunity to do so as if he were any other employee.

Example 2: Sam is just like Ted, but he only worked 300 hours in 2022. Again, we ignore 2019 and 2020. 2021 is year one, but then 2022 is a break, because he worked less than 500 hours. So you would start counting Sam's three consecutive years over again in calendar 2023. because he once again worked more than 500 hours.

Example 3: Rita was hired 5/17/21. Her first counting period is 5/17/21 - 5/16/22, her second is the 2022 calendar year (assuming you shift to the calendar year method for all employees), and her third would be calendar year 2023, making her eligible 1/1/24. While this is sooner than exactly three years, it will be much easier to have all your LTPTEs eligible on the same day (the first day of the plan year) than at various dates throughout the year.

LTPTEs are brought into the plan for deferral purposes only - this is a special eligibility category. If they do not meet the plan's eligibility criteria for any other plan allocation (including safe harbor), then they don't get that contribution. (There is a provision that lets you give them an employer allocation, but that adds a separate vesting schedule to your plan which would greatly increase the plan's complexity and the rules aren't written yet for how to handle it; so we generally do not recommend it). They also don't get top heavy minimum allocations. If your plan has an age requirement, that still must be met by the LTPTE to be eligible under this special rule. Note that if an LTPTE ever satisfies the plan's normal entry requirements, then they enter the plan fully as a normal participant. The other side of this is that if your plan's eligibility already allows employees to enter the plan with only 500 or fewer hours worked (for example, immediate eligibility), then this whole LTPTE thing is a non-issue for your plan.

Then, effective January 1, 2025, the three year consecutive requirement drops down to two years. So if you're counting periods under either method and you reach two in 2025 or on 1/1/25, then the LTPTE is eligible. And ERISA 403(b) plans will now also become subject to these rules, though many offer immediate eligibility on deferrals for all employees.

You should review your non-eligible employees' work history now for the past several years in order to determine who will become an LTPTE on 1/1/24, eligible for deferrals only. Work with your plan's financial advisor to get them set up to defer, if they wish, and also work with your payroll provider - you may have to set up a separate payroll category if payroll is automatically, for example, giving a match to all who defer.

For those of you worried about this moving your participant count into "large plan" territory and being required to get an annual independent audit for the Form 5500, the IRS is meeting you halfway. Starting with the 2023 plan year, only participants with account balances count for this determination. So if you have 20 LTPTEs but only two of them defer, then only two count for your 5500 plan size determination, not all 20.

The idea behind all this is that Congress is reacting to the fact that fewer people are working just one full-time job and instead are making a living by holding down several part time jobs. This change might give them access to the retirement plans that many are currently not able to achieve. It remains to be seen if workers working 500 - 999 hours per year will be able to take advantage of this opportunity

There are many unanswered questions as to how this will work with plan administration, and we are still waiting for IRS guidance. The plan amendment for this will be done in 2025. If instead you want to change your plan's eligibility overall so that LTPTEs will be regular participants sooner and this will be less of an administrative burden, that amendment would be done now - contact your Creative Pension Consultants administration team to discuss this option further.

EMPLOYER CONTRIBUTIONS DEPOSITED AS ROTH

This was allowed by the regulations as of the end of 2022, and while it's a popular idea, there are so many questions about how it will work that it's practically impossible to use it yet. Most financial institutions have decided to not allow it until additional guidance is given by the IRS. The IRS is supposed to give more information about how it will work for taxation, options, etc., and then the financial institutions will have to program it before this will become viable. At the moment, we have no timeframe as to when this might be.

CATCH-UP DEFERRALS AS ROTH FOR HIGH EARNERS

Effective January 1, 2024, any participant who earned more than $145,000 in the prior year must make their catch-up deferrals as Roth in the following year. For example, if you had W-2 income (or net self-employed income if you're a sole proprietor or partner in a partnership) of $150,000 in 2023, then in 2024 the additional catch up deferrals over the base deferral limit (whatever the base and catch-up amounts will be for 2024; we don't know yet) would have to be deposited as Roth deferrals, even if your base deferrals were pre-tax. **You should consult with your payroll provider to ensure that they will be coding this properly and to discuss any changes you may need to make.** In the coming months, we will be reviewing all our plans and amending those that do not already have Roth to add it - stay tuned for more information. If you are taxed as a sole proprietor or a partnership, this is another reason for the owners/partners to not make employee deferral deposits until after the year ends (like we've probably suggested before); depending on your income, you may be subject to this one year and not the next.

As you can imagine, this is a significant change in the reporting of payroll for the many providers that report all the deferrals in one 'bucket' up to the combined total of the base plus catch-up. Plus, there are nondiscrimination test issues this unintentionally brings up for non-safe harbor plans. We have no guidance from the IRS on any of this yet. Many significant figures in the industry have called for this provision to be delayed until guidance is released, but until we hear differently, we have to be ready for it as best as we can.

SELF-CERTIFICATION FOR HARDSHIP DISTRIBUTIONS

A hardship distribution is typically a withdrawal from the plan that a participant can take while still employed only if they have a financial need that meets one of the IRS' pre-defined 'safe harbor' reasons (note that this isn't the same kind of "safe harbor" contribution you might have in your plan - that phrase gets used a lot in the pension world). Currently, the participant would have to prove to you that their situation qualifies under one of the allowable reasons, then also prove how much was required to satisfy the outstanding payment, and then only that amount could be withdrawn. The plan sponsor would have to gather documentation from the participant, review it, determine if it was legitimate, accurate, and relevant.

The new regulations have made it easier for the plan sponsor to allow the participant to self-certify: The participant affirms that they have a need that qualifies under one of the defined reasons (selecting which one), determines how much they need, and certifies that they have and will retain the paperwork to prove it all should it be necessary. Then the plan sponsor would have no responsibility for the transaction, unless you know for certain that the participant is misrepresenting the facts. This reduces the time and energy you or your staff spends on these processes and puts the participant in more control of their account. Might they abuse it? That is a legitimate concern, and there is no way to say they can't or won't. You can either offer the self-certification option to all participants or to none. If your plan is subject to an annual audit for being a large plan, you should discuss this with your audit manager before choosing the self-certify option.

Implementing this is simple: Contact your Creative Pension Consultants administration or distribution team when you get your next hardship request, ask for the self-certification package instead of the regular hardship package, and we'll note that you have elected to proceed with self-certification.

Happy Summer! As always, if you have any questions, feel free to contact your Creative Pension Consultants administration team.