CITY OF Los Angeles
DEFERRED COMPENSATION PLAN

# Board Report 23-24



Date: June 20, 2023

To: Board of Deferred Compensation Administration (Board)

From: Staff

Subject: SECURE 2.0 Provisions

**<u>Recommendation:</u>**

That the Board:

a) Adopt the SECURE 2.0 Act provisions related to Required Minimum Distributions that change the beginning age that participants are required to take Required Minimum Distributions, effective in 2023, and excludes Roth account balances in determining the RMD amount, effective in 2024;
b) Adopt the SECURE 2.0 Act provision that requires age 50 catch-up contributions to be after-tax/Roth only for those participants whose FICA wages exceed $145,000 (indexed) in the prior calendar year, effective in 2024;
c) Adopt the SECURE 2.0 Act provision to increase age-based catch-up contribution limits to the greater of $10,000 or 150 percent of the regular age 50 catch-up amount for participants who reach ages 60, 61, 62, and 63, effective in 2025;
d) Adopt the SECURE 2.0 Act provision eliminating the first of the month rule, effective upon enactment;
e) Provide direction for provisions related to distributions allowable with self-certification of unforeseen or immediate financial needs;
f) Authorize the Board Chairperson to execute a plan sponsor letter of direction to Voya to make these adopted provisions available to DCP participants; and
g) Direct staff to incorporate the adopted provisions into the DCP Plan Document, to be presented to the Board for review and final approval.

**<u>Discussion:</u>**

## A. Background

In March of 2022, the House of Representatives passed the Securing a Strong Retirement Act (SECURE 2.0 Act). On December 23, 2022, the U.S. Senate passed the Consolidated

Appropriations Act, 2023, which contains the SECURE 2.0 Act. The consolidated bill was signed into law by President Biden on December 29, 2022.

The SECURE 2.0 Act[1] is composed of numerous retirement reform provisions that begin to take effect in 2023 and continue over the next several years. In order to begin the review of applicable provisions to be adopted, staff requested from Segal, the plan administration consultant, to provide initial guidance. A list of action items was provided and is attached to this report (**Attachment A**).

It is not uncommon for legislation of this nature to require technical corrections. On May 23, 2023, a letter ("clarifying letter") was additionally issued by the Chairs and Ranking Members of the House Means & Ways Committee and the Senate Finance Committee to the Treasury and IRS to clarify the intent of certain provisions of SECURE 2.0 and indicate corrective language would be forthcoming (**Attachment B**). Four provisions are acknowledged, but the two that pertain to the plan are detailed in the applicable sections further in this report.

Congress has stated a deadline of the end of plan year 2027 for governmental plans to amend their Plan Documents to include necessary SECURE 2.0 provisions. The National Association of Government Defined Contribution Administrators (NAGDCA) has penned letters to request additional guidance and also more time on behalf of governmental plans that might require additional time to implement these provisions (**Attachment C**), particularly those that require plans to set up designated Roth accounts (**Attachment D**).

At this time, staff recommends implementing some of the provisions as soon as administratively possible for the immediate benefit of the plan and its participants. Additional provisions are included below for the Board's information and consideration.

## B. Recommended Provisions to be Immediately Adopted

- **Changes to Required Minimum Distribution Provisions (Mandatory)**
  - **Section 107** increases the age to begin Required Minimum Distributions (RMDs) to age 73 beginning in 2023 (those who are not age 72 by the end of the 2022 calendar year). Those who already began taking RMDs will not be impacted by this change, and will continue to take RMDs. The following chart details the changes to the RMD age and the date of their first distribution. All individuals taking their first RMD have until April 1 of the subsequent calendar year to receive the distribution.

| Period | Required Beginning Age | First Required Distribution |
|---|---|---|
| Born before July 1, 1949 | 70 ½ | Past |
| Born July 1, 1949 through December 31, 1949 | 72 | Past |
| Born in 1950 | 72 | 4/1/2023 |
| Born in 1951 | 73 | 4/1/2025 |

[1] SECURE 2.0 Act of 2022: https://www.congress.gov/117/bills/hr2617/BILLS-117hr2617enr.pdf (starting page 817)

| Period | Required Beginning Age | First Required Distribution |
|---|---|---|
| Born in 1952 | 73 | 4/1/2026 |
| Born in 1953 | 73 | 4/1/2027 |
| Born in 1954 | 73 | 4/1/2028 |
| Born in 1955 | 73 | 4/1/2029 |
| Born in 1956 | 73 | 4/1/2030 |
| Born in 1957 | 73 | 4/1/2031 |
| Born in 1958 | 73 | 4/1/2032 |
| Born in 1959* | 73 | 4/1/2033 |
| Born in 1959* | 75 | 4/1/2035 |
| Born in 1960 | 75 | 4/1/2036 |

** Due to a technicality with the statutory language, it was unclear what the required beginning date (RBD) would be for those born in 1959, however, it is anticipated that clarification will be issued by Congress and Treasury before it becomes effective. The clarifying letter indicates the intent was to further increase the starting RMD age to 75 for those who turn 73 after December 31, 2032.*

- **Section 325** indicates the after-tax (Roth) account balance will no longer be subject to RMDs during the participant's lifetime, and is effective for tax years after December 31, 2023. Previously, both the pre-tax and Roth account balances were taken into account when calculating the RMD amount.
- **Section 302** reduces the missed RMD Penalty from 50% to 25% of the amount of the missed payment. If failure to take the RMD is corrected in a timely manner, the penalty may be reduced to 10% of the distribution.
- **Action**: Amend the Plan Document to include the newly required beginning age for 2023 and to specify the exclusion of Roth account balances in determining RMD amounts in 2024. No action is needed to amend the Plan Document regarding the RMD penalty change, but communications will need to be reviewed.

- **Roth Requirement for Age 50 Catch-Up Contributions, for Employees Earning Over $145,000 (Mandatory)**
  - **Section 603**, as noted earlier in this report, states that participants whose FICA wages exceed $145,000 (indexed) in the prior calendar year are allowed to make Age 50 Catch-Up contributions only on a Roth basis. Catch-up contributions allow participants who are age 50 and older to make additional contributions to their account, up to the designated IRS limit. Section 603 is effective for taxable years after December 31, 2023.
    - The clarifying letter indicates Congress intended that participants' whose wages exceed $145,000 (indexed) for the prior calendar year are permitted to make catch-up contributions only on a Roth basis, while participants earning less would continue to be permitted to make catch-up contributions on either a pre-tax or a Roth basis.
      - The original language could be interpreted that Congress intended to disallow catch-up contributions altogether beginning in 2024.

    - Staff has been advised that this provision does not apply to those who are enrolled in Special Catch-Up, which permits participants who are within three calendar years of normal retirement age to defer up to twice the normal contribution limit for three consecutive years, as long as the participant had under-contributed in prior eligible years.
  - **Action**: Amend the Plan Document to reflect the new rule, effect required changes to work processes and related payroll system programming, and update participant communications.

- **Increased Catch-Up Contribution Limits for those Aged 60-63 (Mandatory for Plans Offering Catch-Up Contributions)**
  - **Section 109** increases age-based catch-up contribution limits to the greater of $10,000 or 150 percent of the Age 50+ Catch-Up amount for participants who reach ages 60, 61, 62, and 63. The provision is effective in the tax year after December 31, 2024.
    - This provision is subject to the Roth only contribution requirement under Section 603 discussed above for higher earners.
    - After age 63, participants revert to the Age 50+ Catch-Up contribution limit (with contributions to be made on a Roth basis only for higher earners).
    - This provision for Age 60-63 Catch-Up contributions cannot be used in the same tax year as Special Catch-up.
  - **Action:** Amend the Plan Document to reflect the new rule, effect required changes to work processes and related payroll system programming, and update participant communications.

- **Elimination of the First Day of the Month Requirement for Contribution Elections**
  - **Section 306** allows participants' contribution elections to be effective any time prior to the compensation being available to the participant. Participants will no longer have to wait until after the first day of the month for new contribution elections to take effect. As an example, previously a participant had to elect a contribution change in May to have it take effect in June; the new provision removes this administrative requirement and will allow participants to make changes to their deferral amounts as soon as administratively feasible.
  - **Action:** Amend the Plan Document to reflect the new rule, effect required changes to work processes and related payroll system programming, and update participant communications.

## C. Optional Provisions for Consideration and Discussion

The SECURE 2.0 Act contains optional provisions that allow for additional distribution and savings options that will require consideration by the Board. The Board may either provide direction or refer these topics to the Plan Governance & Administrative Issues Committee for further discussion. One type of provision that requires the Board's direction is related to potential self-certification of unforeseen or immediate financial needs.

- **Self-Certification of Unforeseen Emergency Withdrawals**
  - **Section 312** allows participants to self-certify that a hardship withdrawal or unforeseen emergency distribution is based on an immediate and heavy financial need, and the amount requested is no more than necessary.
    - Plans may further choose to impose limitations, such as how many times this may be done or up to what amount.

        - Currently, participants must show financial need of a specific amount and provide documentation of the financial need, and prove it meets the criteria for an unforeseeable emergency hardship.
        - Staff recommends that this provision not be adopted at this time. As indicated by Segal, though it may lighten the administrative burden of review, it may encourage distributions when there is not a substantial financial need. This provision is better to be revisited in the future, when other plans and third-party administrators may have more experience and data regarding how this may be administered.

- **Emergency Personal Expense Withdrawals Permitted**
    - **Section 115** allows participants to take one distribution per calendar year with no early withdrawal penalties for "unforeseeable or immediate financial needs relating to necessary or personal family emergency expenses."
        - The distributions are limited to $1,000, may be repaid within three years, and is restricted to one withdrawal per three-year repayment period if not repaid. If the account has less than $2,000, only the amount over $1,000 may be taken.
        - The plan can rely on a participant's written self-certification of an unforeseeable or immediate financial need.
        - This would be considered an in-service distribution and would be effective for distributions made after December 31, 2023.
        - Staff believes that this could be beneficial to participants and considered an alternative to the provision above for general self-certification of unforeseen emergency withdrawals. It is recommended that staff be directed to research the work process with the third-party administrator and return back to the Board for additional review and action.

## D. Other Provisions Under Review

There are a number of other provisions that would be generally beneficial to Plan participants or are some sort of administrative clarification. Whether a mandatory or optional provision, closer review would be needed to determine if any change to the Plan Document is even necessary. Staff will return to the Board at a future date with additional recommendations. Some examples of these types of provisions are included below, with more provisions included within Attachment A.

- **(Mandatory) Surviving Spouse RMD Election, to be Treated as Employee**
    - **Section 327** allows surviving spouses to elect to defer RMDs until the year in which the plan participant would have attained RMD age. RMDs will also be calculated under the life expectancy table available for the plan participant. The provision is effective for tax years after December 31, 2023.

- **Repeal of Direct Payment Requirement for Tax Free Payments from a Governmental Plan to Pay Public Safety Officers Medical Insurance Premiums**
    - **Section 328** permits a participant who is an eligible retired public safety officer to take a tax free distribution from a plan to be used to pay medical and long-term care premiums, beginning in 2023. Currently, payment must be made to the provider directly from the DCP to qualify for the tax free distribution. Though Segal indicates participants may take advantage of this tax exclusion directly, staff believes it would be ideal to amend the Plan Document if clarification is needed.

- **Recognition of Tribal Government Domestic Relations Orders**
    - **Section 339** allows plans to recognize domestic relations orders issued by Indian tribal governments as "qualified domestic relations orders" (QDRO), for any orders received after December 31, 2022. A review will be necessary to see if a Plan Document clarification is necessary, otherwise, it may be a written clarification to be provided in internal QDRO procedures.

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Attachment A

Segal

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# Memorandum

**To:** Esther Chang
Daniel Powell

**From:** Melanie Walker

**Date:** April 28, 2023

**Re:** The City of Los Angeles Deferred Compensation Plan - SECURE 2.0 action items

Below is a list of provisions of the SECURE 2.0 Act of 2022 (SECURE 2.0) and their effective dates, along with a brief description of each provision's potential impact on your plan. In addition, we included a list of action items for your Plan to take or consider in complying with, or taking advantage of, specific provisions of SECURE 2.0 that are effective in 2023 or earlier.

SECURE 2.0 was enacted on December 29, 2022. Effective dates, however, vary by provision. Plans must comply operationally based on the applicable effective date even though no written amendments are required before the end of the plan year beginning on or after January 1, 2027 for governmental plans.

Please note that Segal is neither a law firm nor a tax firm. The information in this memo should not be construed as legal or tax advice to the Plan sponsor or Plan fiduciaries. We recommend that the Plan consult with legal counsel prior to taking, or refraining from taking, any action on the matters addressed below.

************************ **Effective in 2023 or earlier** ****************************

## 1. Increased Required Beginning Date (RBD) Age (Section 107)

Section 107 of the Act increases the RBD age to age 73 ***starting in 2023*** for anyone who was not age 72 by the end of the 2022 calendar year (i.e., those born on and after January 1, 1951). The new RBD for a participant is April 1 of the year following the year of attaining age 73 or the year following separation from service, if later. Participants who turned age 72 in 2022 (i.e., born in 1950) would have attained RBD on April 1, 2023, unless they have not yet separated from service.

A person born in 1951 will have an RBD of April 1, 2025 (assuming they have separated from service). Therefore, the only first RMDs that would occur in 2024 will be for beneficiaries or older participants who separated from service in 2023. Under IRS regulations, the first distribution year is the first year for which a minimum payment of benefits must be made. However, that first distribution does not have to be paid until April 1 of the following year (the RBD). The second distribution would be required by December 31 of the RBD year.

| Period | Required Beginning Date Age | First Required Distribution |
|---|---|---|
| Born before July 1, 1949 | 70 ½ | Past |
| Born July 1, 1949 through December 31, 1949 | 72 | Past |
| Born in 1950 | 72 | 4/1/2023 |
| Born in 1951 | 73 | 4/1/2025 |
| Born in 1952 | 73 | 4/1/2026 |
| Born in 1953 | 73 | 4/1/2027 |
| Born in 1954 | 73 | 4/1/2028 |
| Born in 1955 | 73 | 4/1/2029 |
| Born in 1956 | 73 | 4/1/2030 |
| Born in 1957 | 73 | 4/1/2031 |
| Born in 1958 | 73 | 4/1/2032 |
| Born in 1959 | 73 | 4/1/2033 |
| Born in 1959 | 75 | 4/1/2035 |
| Born in 1960 | 75 | 4/1/2036 |

SECURE 2.0 also increases the RBD age in 2033 to age 75. However, there is a technical problem with the statutory language. Those born in 1959 are in both classes: ages 73 and 75. Congress and Treasury are aware of the flaw, and it will be fixed well before it is effective. We recommend only addressing age 73 at this time. There is plenty of time to address age 75, assuming Congress does not further revise the RBD age prior to 2033.

***Action Items:***

- Immediately notify participants who will be age 72 in 2023 that they do not have to commence benefit payments until April 1, 2025
- 2024 will not have any new RMDs required because of age
- Participants who have separated from service and attain age 73 in 2024 will have an RBD of April 1, 2025, and the plan will have to comply with this rule in operation even though the plan need not be amended until later
- Amend the Plan document (subsection 9.04(c)) to include the new RBD age; we recommend that you amend the Plan to be consistent with operational rules, rather than wait until the 2027 deadline
- Do not include the 2033 change to age 75 at this time because a statutory or regulatory fix will affect the necessary plan language
- Update Plan communications to participants to explain the new rules, including websites, newsletters and Plan summaries or handbooks

## 2. Missed Required Minimum Distribution (RMD) Payment Penalty Tax Reduced (Section 302)

The Act reduces the penalty tax on participants who fail to take RMDs, when required by the Code, from 50% to 25% of the missed payment. If the failure is corrected in a timely manner as defined under the Act (generally, within two years of when originally required), the tax is reduced to 10%. Section 302 is ***effective for taxable years beginning after enactment***.

***Action Items*:**

- Plan sponsors should update any Plan communications or other documents if they refer to the penalty for failure to take an RMD timely
- A participant pays the penalty on IRS Form 5329, due at the time of income tax filing for the calendar year in which the distribution must be made (last day permitted)

## 3. First-of-the-Month Rule Eliminated (Section 306)

Prior to enactment of SECURE 2.0, participants in a 457(b) plan generally may only defer compensation if an agreement providing for the deferral has been entered into before the first day of the month in which the compensation is paid or made available. The Act conforms the rule for governmental 457(b) plans to rule for 401(k) and 403(b) plans by allowing participants of governmental 457(b) plans to change their deferral rate at any time before the compensation is available to the individual. Section 306 is ***effective for taxable years beginning after the date of enactment.***

***Action Items:***

- Modify payroll processes to allow for faster implementation of deferral elections, including changes after initial deferral
- Notify participants of this new deadline for deferral election changes
- Amend the Plan document (Section 4.01(b) and (d)) and Plan forms and communications to reflect new rule

## 4. Native American Tribal Court QDROs Accepted (Section 339)

The Act allows governmental plans to treat domestic relations orders issued by Native American Tribal Courts in the same manner as those issued by state courts – meaning that they can be considered QDROs. Section 339 is effective for domestic relations ***orders received by the plan after December 31, 2022***, including any such order which is submitted for reconsideration after such date.

This provision may not require a Plan amendment. It just clarifies that a Native American tribal court domestic relations order is to be treated like a DRO issued by a state court and use the qualification procedures as it would any other DRO. If a plan has been rejecting such domestic relations orders, it should revise its policy.

***Action Items*:**

- If the Plan has been rejecting tribal QDROs, it should change QDRO processing rules
- If the Plan has been rejecting tribal QDROs, you may want to contact relevant parties and tell them they can resubmit (this is not required)
- A Plan amendment is not required
- Consider making a clarification in written QDRO procedures

## 5. Self-Certification of Unforeseeable Emergency Events Allowed (Section 312)

A governmental 457(b) plan may allow distributions due to an unforeseeable emergency. Generally, the participant must show financial need of a specific amount and demonstrate that his or her situation is one of the unforeseeable emergency events listed in relevant regulations or approved by the Plan, as well as provide documentation of the financial need. The Act allows plans to accept a participant's self-certification of an unforeseeable emergency event. The Treasury may provide that a plan cannot accept self-certification if the plan has actual knowledge of the falsehood of the certification. Section 312 is ***effective for plan years beginning after enactment***.

Self-certification will simplify administration but might also encourage unforeseeable emergency distributions when there is no real financial need. The new provisions do not prevent a participant from taking a distribution of his or her entire account balance at any time for any reason. However, plans are not required to allow self-certification; it is optional. If plans do allow self-certification, they are permitted to impose limitations on self-certified unforeseeable emergency distributions at their discretion.

***Action Items*:**

- If your Plan wants to adopt this provision, a Plan document amendment (Section 9.09) will be required, including any specific limitations on self-certification of distributions; we recommend amending the Plan in the year in which the change takes effect
- If your Plan wants to adopt this provision, any changes should be communicated to participants, and withdrawal forms and other Plan communications need to be updated

## 6. Federally-Declared Disaster Distributions Permitted (Section 331)

The IRC includes special distribution and loan rules when the President declares a national emergency. These are similar to the rules adopted statutorily in the CARES Act for the COVID-19 emergency. Note that these are not "hardship" rules but special "disaster" rules.

Rather than providing for special rules on a disaster-by-disaster basis, the Act provides permanent rules for the use of retirement funds in the case of any federally declared disaster. Plans can permit participants to take distributions of up to $22,000 without incurring the 10% premature distribution penalty (this penalty does not apply to 457(b) plans). A participant receiving such a distribution can spread the income over three years for federal income tax purposes. Participants can repay distributions to an eligible retirement account within three years. The limit on disaster-related loans is increased to the lesser of 100% of the present value of the vested account or $100,000. Additionally, participants can recontribute amounts that were distributed within 180 days prior to the disaster purchase a home, which qualified for exemption from the 10% premature distribution penalty. Section 331 is ***effective for disasters occurring on or after January 26, 2021***.

The law standardized the special rules that apply in a Presidential-declared disaster. Plans may want to adopt an amendment (or operate in accordance with a planned later amendment) and automatically trigger these special distribution and loan provisions when a disaster declaration applies. Most disasters are limited to certain geographic areas and automatic application may confuse plan administration as some participants will be eligible for relief and others not eligible.

***Action items*:**

- Plans do not have to offer any of these distribution and loan changes when there is a disaster; however, they may choose to do so to the extent desired up to the maximum amounts (e.g., plan may allow distributions but not loans)
- If your Plan wants some, or all, of the disaster relief rules to go into effect automatically (without the need for further amendment), the Plan document should be amended to include the automatic disaster trigger (Section 9.12)
- We recommend that you communicate any Plan changes related to federally-declared disasters to participants and work with your record keeper to implement administration of these changes

## 7. Roth Matching and Nonelective Contributions Permitted (Section 604)

Sponsors of defined contribution plans, including 401(a) plans and governmental 457(b) plans, may allow participants to elect to have employer matching and nonelective contributions treated as Roth contributions. It is optional on the part of the plan sponsor to provide this, and then optional on the part of the participant whether to elect Roth treatment. Section 604 is ***applicable upon enactment***.

There are technical issues as to how an employer and employee treat the Roth contributions when made since they are supposed to be taxed on the way into the plan. Questions involve whether the amounts will be made subject to income tax withholding and/or FICA withholding. The IRS is likely to issue guidance on these tax issues quickly.

***Action items*:**

- Roth treatment is optional on the employer's part, and only if the employer selects it can participants elect to make these types of Roth contributions
- We do not recommend that employer matching and nonelective contributions be made to a governmental 457(b) plan, but rather to a separate 401(a) plan, because the 457(b) plans have a lower total contribution limit and employer contributions are subject to FICA taxes in a 457(b) plan
- Plans considering this should discuss with their record keepers whether, and when, they can handle this change
- If this change is desired, Plan documents and forms should be amended to allow employer contributions on a Roth basis, and the changes should be communicated to participants

## 7. Qualified Birth or Adoption Distribution Repayments Limited to Three Years (Section 311)

The SECURE Act allowed plans to permit birth and adoption distributions (BOADs). If such a distribution was made, the plan had to allow repayment indefinitely. SECURE 2.0 limits the period in which repayment of birth or adoption distributions to the plan or an IRA can be made to three years. Section 311 is effective for distributions made after the date of enactment; distributions made prior to enactment may be paid back, if the participant wishes, any time before January 1, 2026.

This provision is relevant because your Plan has a special rule for birth or adoption distributions and allows those distributions to be repaid back into the plan. The plan will have to limit the repayment period.

***Action item*:**

- The Plan document must be amended to limit repayment to within three years for BOAD amounts withdrawn after enactment (and to January 1, 2026 for earlier distributions) (Section 9.08)
- We recommend that you communicate this change to participants in general and specifically to any participants who have received this type of distribution

## 8. Repeal of direct payment requirement in HELPS provision (Section 328)

Current law provides an exclusion from gross income ($3,000) for a distribution from a governmental retirement plan to a public safety officer to pay for their health insurance premiums and long-term care insurance (Healthcare Exclusion for Law Enforcement and Public Safety Officers or HELPS). The exclusion required that the plan directly pay the insurance premiums, which was a significant administrative burden for plans. Section 328 repeals the direct payment requirement and is ***effective for distributions made after the date of enactment*** of this Act.

***Action Item*:**

- Your Plan document currently provides for direct payment, which can remain, if desired (Section 9.02).
- Plans likely will not need to take any action for eligible participants to take advantage of this tax exclusion on their own. Such participants can report their eligibility for the exclusion on their federal income tax return. Plans may want to communicate the tax exclusion to their participants, to the extent applicable.

****************************** **Effective in 2024** **********************************

## 1. Increased Cash-Out Limit for Small Account Balances (Section 304)

The Act increases the cash-out limit for small account balances after two years without any contributions, from $5,000 to $7,000. Section 304, which increases the value to $7,000 and ***applies to distributions made after December 31, 2023***. This special cash-out provision and the level of the cash out (up to $7,000) remains permissive. Since your Plan's current cash-out language (Section 9.03) refers to the greater of $5,000 or value specified in IRC section 411(a)(11)), the increase to $7,000 is automatic. However, we recommend that you update the Plan document language and communications to participants to reflect the $7,000 cash-out limit before this change goes into effect. Alternatively, you may amend your Plan to retain the $5,000 limit (or any other dollar amount up to $7,000).

## 2. Plans Allowed to Make Matching Contributions Based on Student Loan Repayments (Section 110)

The Act includes a provision allowing governmental 457(b) plans to treat an employee's student loan payment to a non-plan lender as an elective employee deferral for purposes of triggering matching contributions. The student loan repayments that the plan takes into account for purposes of generating matching contributions cannot exceed the maximum elective deferral limit for the year ($22,500 in 2023) less the actual elective deferrals the employee makes to the plan. Section 110 is ***effective for contributions made for plan years beginning after December 31, 2023*** (for student loan payments made after the effective date). There are questions about how and whether the provision applies where a parent repays a loan for a student.

This provision is optional. If you desire to add this type of matching contribution to your Plan (or a separate 401(a) defined contribution plan), you will need to amend your Plan document, communications, forms and notices for this purpose.

## *3*. Emergency Savings Account Permitted (Sections 127)

This section allows a plan to establish a Pension-Linked Emergency Savings Account (PLESA) for non-highly compensated employees. The PLESA allows employers the option to offer their non-highly compensated employees an emergency savings account featue within a governmental 457(b) plan. The PLESA is being referred to as a "sidecar" account; it is a subaccount within a governmental 457(b) plan and subject to its own special rules. Investments in the PLESA are limited to certain capital preservation type investments; generally liquid, no risk assets. However, the elective contributions count against the maximum permissible elective contributions for the year. An employee may take money out of the PLESA at the participant's discretion. Apparently, no evidence of an "emergency" is required.

To the extent your Plan provides for automatic enrollment and Roth contributions, you may establish a PLESA using automatic enrollment, with an opt out, at no more than 3% of salary. The portion of the account attributable to employee contributions under the PLESA is capped at $2,500 (the employer can set a lower limit) plus earnings within the year. No PLESA contributions are allowed if the account balance at the beginning of the year exceeds $2,500 because of earnings until the balance is below $2,500. These contributions must be treated as elective Roth contributions. If the employer provides a match for elective contributions that match would also have to apply to elective contributions made to the PLESA but the match would go into the regular match account, not into the PLESA. At separation from service, employees may take their PLESA as cash or roll it into a Roth account or an IRA. Section 127 is ***effective for plan years beginning after December 31, 2023***.

This provision is optional. In addition, this Section of the Act was written as an amendment to ERISA only. For governmental plans, it is unclear whether they can still offer a PLESA that is consistent with the terms of the ERISA rules while not subject to the provisions of ERISA. Therefore, before a governmental 457(b) plan may offer a PLESA, it appears IRS clarification (or corrective legislation) may be required.

## 4. Emergency Personal Expense Withdrawals Permitted (Section 115)

The other approach to emergency savings is a new distribution rule allowing a participant to take a small amount (up to $1,000) out of their governmental 457(b) plan. The distribution may be taken only once every three years unless the participant has paid back the previous distribution. The participant has the option of repaying the distribution within three years. The participant cannot take out another $1,000 unless the amount has been repaid or three years have passed.

The distribution, which is referred to as an "emergency personal expense distribution," can be any amount up to $1,000 but the participant only gets one such distribution per calendar year. If the account has less than $2,000, only the amount over $1,000 may be taken. Also, all of the participant's accounts in all plans of an employer are aggregated in determining whether more than $1,000 has been withdrawn.

The plan can rely on a participant's written self-certification of an unforeseeable or immediate financial need. The Secretary may by regulations include an "actual knowledge" prohibition on accepting a certification, meaning that the plan would be prohibited from accepting a self-certification if it had actual knowledge that the participant did not have an unforeseeable or immediate financial need. Section 115 is ***effective for distributions made after December 31, 2023***.

This provision is optional. If you desire to add this type of in-service distribution to your Plan, you will need to amend your Plan document, communications, forms and notices for this purpose.

## 5. Pre-Death RMDs from In-Plan Roth Accounts Eliminated (Section 325)

Roth IRAs are not subject to the RMD rules even while the Roth IRA owner is alive. This provision will apply this same rule to Roth accounts in governmental 457(b) plans. Section 325 is ***effective for tax years beginning after December 31, 2023***. The new rule does not apply to a 2023 RMD taken April 1, 2024, which means any required distribution for a Roth account prior to January 1, 2024 must be paid to the applicable participant or beneficiary.

Operational compliance is required beginning in 2024. Your Plan must not require minimum distributions from Roth accounts after the effective date. In addition, we recommend you amend your Plan document, communications, forms and notices for this purpose by the effective date.

## 6. Age-Related Catch-Ups Required to be Roth Contributions (Section 603)

The Act requires all age-related "catch-up" contributions to governmental 457(b) plans of participants who had FICA wages of at least $145,000 (indexed) for the prior year to be made only in the form of Roth contributions. "Catch-up" contributions are additional elective contributions that older participants can make. "Roth" contributions are after-tax elective .mandatory for plans that offer catch-up contributions.

Participants with FICA wages below the limit can continue to make the contributions on a pre-tax basis. However, the plan must provide participants with FICA wages under $145,000 the ability to make Roth catch-up contributions (to avoid having a feature only available to the highly compensated employees). Section 603 is ***effective for taxable years beginning after December 31, 2023***.

The IRS will need to provide guidance on how to interpret "FICA wages" for purposes of this provision since certain groups such as the self-employed or governmental employees not covered by Social Security do not technically have FICA wages. IRS is aware of the need for guidance.

In order to comply with this change, you must amend the Plan document (Section 5.01(b)), modify payroll processes and tax reporting, as well as communicate the change to participants and update forms and notices, as applicable.

## 7. Plan Withdrawals for Individuals in Cases of Domestic Abuse (Section 314)

The Act created a new distribution event for distributions taken from 457(b) plans or other DC plans (other than money purchase plans) in circumstances involving domestic abuse (as defined in the provision). This provision also states that the 10% premature distribution penalty (if otherwise applicable) does not apply to a distribution that meets the requirements of the new provision. The amount of the distribution is limited to the lesser of $10,000 (as indexed in the future) or 50% of the nonforfeitable amount in the account. Adopting a new distribution event is optional for the plan sponsor; if adopted, a plan amendment would be required.

A participant may repay the distribution to an IRA (or to the plan if it accepts such repayments) within three years. Section 314 is ***effective for distributions made after December 31, 2023***.

****************************** **Effective in 2025** **********************************

### 1. Certain Older Participants to Permitted Make Higher Catch-Up Contributions (Section 109)

Current law permits older workers (age 50 and above) to make catch-up elective contributions up to a limit ($7,500 in 2023). The Act increases the yearly amount for workers who are ages 60 – 63 to the greater of $10,000 or 50% more than the regular catch-up amount in beginning in 2025. These amounts are then indexed for inflation starting after 2025. Section 109 is optional and ***effective for taxable years beginning after December 31, 2024***.

If you desire to add these additional catch-up contributions to your Plan, you will need to amend your Plan document and update participant communications, forms and notices for this purpose.

### 2. Long-Term Care Contracts with Retirement Plan Distributions (Section 334)

This provision provides a new optional in-service distribution event for 457(b) and other DC plans (other than a money purchase plan) for the purpose of paying premiums for long-term care contracts, as well as exempting such distribution from the 10% premature distribution penalty (if applicable). The annual limit of such distribution is the smallest of (1) the amount paid for the coverage, (2) 10% of the employee's nonforfeitable accrued benefit in the plan, or (3) $2,500 (indexed). The contract may be for the participant, spouse or a family member. Section 334 is ***effective for distributions made at least three years after enactment.***

*******************************************************************************************************

It is important to note that we did not include information about the following provisions of the SECURE 2.0 Act in this memorandum due to limited applicability to your Plan:

1. The Act added new exceptions to the 10% early distribution penalty under IRC §72(t), which does not apply to governmental 457(b) plans, including for terminally-ill participants. The Act did not create a separate, in-service distributable event for this purpose.

2. The Act also included several provisions related to plan annuities, such as enhanced limitations on Qualifying Longevity Annuity Contracts (QLACs) and increasing commercial annuities.

3. Finally, SECURE 2.0 included specific rules permitting Plans to no longer recoup certain overpayments, to self-correct inadvertent failures and extending automatic enrollment corrections under the IRS Employee Plans Compliance Resolution System (EPCRS), which has limited applicability to governmental 457(b) plans.

We hope this information is helpful. Once you have had a chance to review this memorandum, please let us know if you would like to schedule a call to discuss any issues related to the SECURE 2.0 Act.

cc: Stephen E. Murphy

Congress of the United States
Washington, DC 20515

May 23, 2023

The Honorable Janet Yellen
Secretary of the Treasury
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

The Honorable Daniel Werfel
Commissioner of Internal Revenue
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D.C. 20224

Dear Secretary Yellen and Commissioner Werfel:

We are writing as the Chairs and Ranking Members of the Committees of jurisdiction to ensure that Congressional intent is carried out with respect to several provisions of recently enacted retirement legislation. The provisions, sections 102, 107, 601, and 603 of the "SECURE 2.0 Act of 2022" ("SECURE 2.0") (Division T of the Consolidated Appropriations Act, 2023), were enacted on December 29, 2022 (Pub. L. No. 117-328).

Section 102 of SECURE 2.0 increases the credit for small employer pension plan startup costs ("startup credit"), in part by allowing eligible employers a credit for a portion of employer contributions made to the plan. The provision could be read to subject the additional credit for employer contributions to the dollar limit that otherwise applies to the startup credit. However, Congress intended the new credit for employer contributions to be in addition to the startup credit otherwise available to the employer.

Section 107 of SECURE 2.0 increases the age at which required minimum distributions from a retirement plan are required to begin. Specifically, it changes the age on which the required beginning date for required minimum distributions is based (the "applicable age").

Congress intended to increase the applicable age from age 72 to age 73, for individuals who turn 72 after December 31, 2022 and who turn 73 before January 1, 2033, and to increase the applicable age from age 73 to age 75 for individuals who turn 73 after December 31, 2032. However, with respect to the increase from age 73 to age 75, the provision could be read to apply such increase to individuals who turn 74 (rather than 73) after December 31, 2032, which is inconsistent with Congressional intent.

Section 601 of SECURE 2.0 permits SIMPLE IRA plans and SEP plans to include a Roth IRA. Section 601 could be read to require contributions to a SIMPLE IRA or SEP plan to be included in determining whether or not an individual has exceeded the contribution limit that applies to contributions to a Roth IRA. However, Congress intended to retain the result under the law as it existed before SECURE 2.0 was enacted regarding SIMPLE IRA and SEP contributions (taking into account that section 601 permits SIMPLE IRA and SEP plans to include a Roth IRA). Thus, Congress intended that no contributions to a SIMPLE IRA or SEP plan (including Roth contributions) be taken into account for purposes of the otherwise applicable Roth IRA contribution limit.

Section 603 of SECURE 2.0 requires catch-up contributions under a retirement plan to be made on a Roth basis, for taxable years beginning after 2023, if the participant's wages from the employer sponsoring the plan exceeded $145,000 for the preceding calendar year. A conforming change to section 603 might be read by some to disallow catch-up contributions (whether pre-tax or Roth) beginning in 2024. Congress did not intend to disallow catch-up contributions nor to modify how the catch-up contribution rules apply to employees who participate in plans of unrelated employers. Rather, Congress's intent was to require catch-up contributions for participants whose wages from the employer sponsoring the plan exceeded $145,000 for the preceding year to be made on a Roth basis and to permit other participants to make catch-up contributions on either a pre-tax or a Roth basis. This Congressional intent was noted in the Committee Report to accompany S. 4808, the Enhancing American Retirement Now Act (S. Rept. 117-142).

We intend to introduce technical corrections legislation to correct erroneous statutory language, which may include items not addressed in this letter, so that the provisions carry out Congressional intent. Please contact Payson Peabody (Chairman Smith), Kara Getz (Ranking Member Neal), Drew Crouch (Chairman Wyden), and Jamie Cummins (Ranking Member Crapo) with any questions you or your staff may have.

Sincerely,

Jason Smith
Chairman
House Committee on Ways and Means

Richard E. Neal
Ranking Member
House Committee on Ways and Means

Ron Wyden
United States Senator
Chairman
Committee on Finance

Mike Crapo
United States Senator
Ranking Member
Committee on Finance

**National Conference of State Legislatures (NCSL)**
**National Association of Counties (NACo)**
**United States Conference of Mayors (USCM)**
**National League of Cities (NLC)**
**International City/County Management Association (ICMA)**
**National Association of State Treasurers (NAST)**
**Government Finance Officers Association (GFOA)**
**National Association of State Auditors, Comptrollers and Treasurers (NASACT)**
**International Association of Fire Fighters (IAFF)**
**National Association of Police Organizations (NAPO)**
**National Council on Teacher Retirement (NCTR)**
**National Conference of Public Employee Retirement Systems (NCPERS)**
**National Association of Government Defined Contribution Administrators (NAGDCA)**
**National Association of State Retirement Administrators (NASRA)**

May 11, 2023

By Electronic Mail

Carol Weiser
Benefits Tax Counsel, Office of Tax Policy
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

**Re: SECURE 2.0 Guidance for Governmental Plans**

Dear Ms. Wiser:

On behalf of the national organizations listed above, representing state and local governments and their elected officials, finance officers, retirement plans and employees, we are writing regarding expected guidance surrounding the "SECURE 2.0" retirement security provisions enacted recently in P.L. 117-328. We appreciate the assistance that Treasury and IRS have historically provided governmental plans with regard to implementing federal retirement-related legislation and regulations. In particular, there has been long-standing recognition of the state and local statutory and regulatory governance structures in place for public retirement plans, which are not preempted by or subject to the Employee Retirement Income Security Act (ERISA) like those in other sectors. We strongly urge Treasury and IRS to again acknowledge and respect these unique legal constructs when issuing guidance surrounding SECURE 2.0 for governmental plans.

First, we request that Treasury and IRS recognize that many governmental plans will need additional time to come into compliance with the catch-up contribution provisions in SECURE 2.0. These provisions would require, beginning in 2024, that such contributions be made on an after-tax (Roth) basis for individuals earning more than $145,000 in the prior plan year, and that those making less than $145,000 be given the option to make contributions on a Roth basis. Many governmental plans do not currently provide for Roth contributions in their structure or have the legal authority under state or local statutes to offer after-tax catch-up contributions. As a result, statutory changes permitting such treatment will be required, and they cannot reasonably be

enacted and implemented before the current effective date.
Treasury and IRS have long acknowledged that, unlike other plans, governmental plan provisions that may require modifications in order to be in compliance with new Federal requirements are often embodied in state and/or local statutes and may therefore require additional time to be adopted.[1] In addition, Treasury-IRS have recognized the unique challenges posed by changes to governmental retirement plans given the constitutional protections provided to benefits under both state and federal law. For example, the IRS provided such appropriate relief using a transitional compliance period in the early 2000s with the implementation of the Treasury Regulations under Code Section 401(a)(9). Specifically, during the process of finalizing the 401(a)(9) Regulations, the IRS recognized the difficulty that state and local governments face in changing plan provisions due to state constitutional or statutory prohibitions on benefit reductions. Therefore, in addition to the transitional provisions provided to all retirement plans, the final regulations provided grandfathering relief and "good faith" compliance for governmental plan provisions in effect on a certain date.[2]

Importantly, given the unique nature of governmental plans, without a similar type of relief – a delayed effective date[3] or grandfathering relief assuming "good faith" compliance for governmental plans will satisfy the Code requirements – some governmental plans will be forced to suspend all catch-up contributions until the necessary authority to offer Roth contributions can be added to their structure. Certainly, the inability to make catch-up contributions to a retirement plan during the crucial years prior to retirement would be counter to Congress' goals of encouraging retirement savings. Furthermore, some plans do not have the legal authority to suspend catch-up contributions and will be faced with either being out of compliance with the new IRC requirements or in violation of their state or local statutes. This also does not seem to be the intended goal of SECURE 2.0.

Second, we also urge Treasury and IRS, when promulgating regulations for governmental plans, to keep in mind their exemption from ERISA and many sections of the Internal Revenue Code, as well as their coverage under state and local statutes. Guidance should not run contrary to these exclusions or fail to acknowledge the governing statutes and definitions in place at the state and local levels of government. For example, with regard to the new catch-up contributions, we ask that Treasury and IRS honor reasonable, good faith compliance with the definition of compensation that is used under the terms of the plan and/or applicable state and local statutes and regulations. Similarly, Treasury and IRS have and should continue to recognize that eligibility

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[1] Significant lead time may be necessary in order to, among other things: i) meet legislative bodies' pertinent filing deadlines; ii) secure passage by the legislative bodies with the authority to amend the plan; iii) acquire final approval by the applicable executive; and iv) finalize implementation by the affected plans. Further, some state legislatures meet only biennially; others require plan amendments, once passed, to receive a fiscal impact report and then obtain approval in a subsequent legislative session; and many local governmental plan provisions are subject to collective bargaining agreements that may also take time to be modified, where necessary.

[2] This relief provided that governmental plan distribution options in effect on April 17, 2002, "will not fail to satisfy section 401(a)(9) merely because the annuity payments do not satisfy the requirements of A-1 through A-15 of [1.401(a)(9)-6]." However, the grandfathered options "must satisfy the statutory requirements of Code Section 401(a)(9), based on a reasonable and good faith interpretation" of that section. Treas. Reg. § 1.401(a)(9)-6, Q&A 16.

[3] For example, recent guidance (Notice 2022-33) that extended plan amendment deadlines included the following effective date for governmental plans: "90 days after the close of the third regular legislative session of the legislative body with the authority to amend the plan that begins after December 31, 2023."

rules for participation in governmental plans are enshrined in state and local statutes and Congress specifically excluded state and local government retirement plans from the participation requirements of IRC Code Section 410.

Finally, with regard to any provisions that may require technical corrections legislation, it would be extremely beneficial if Treasury and IRS issued timely guidance in expectation of a future legislative correction based on legislative intent. This has been done in the past and we are encouraged by public statements that the agency is considering issuing similar guidance under this approach for SECURE 2.0. In this regard, we would stress the need for such guidance to be as timely as possible to permit governmental plans to take all appropriate steps to be in compliance with the new law's requirements.

Thank you for your time and consideration. We would greatly appreciate the opportunity to meet with you to discuss these matters further. Please feel free to contact our organizations' representatives below:

Brian Wanko, NCSL, brian.wanko@ncsl.org, 202-624-8197
Paige Mellerio, NACo, pmellerio@naco.org, 202-942-4272
Larry Jones, USCM, ljones@usmayors.org, 202-293-2352
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Matt Petersen, NAGDCA, mpetersen@nagdca.org, 859-469-5789
Jeannine Markoe Raymond, NASRA, jeannine@nasra.org, 202-624-1417

Cc: Rachel Levy, Associate Chief Counsel
Helen Morrison, Deputy Benefits Tax Counsel
William Evans, Attorney-Advisor

NAGDCA

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February 7, 2023

By Electronic Mail

Ms. Rachel Levy
Associate Chief Counsel
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Internal Revenue Service
1111 Constitution Avenue, NW
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Ms. Carol Weiser
Benefits Tax Counsel
Office of Tax Policy
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

Ms. Helen Morrison
Deputy Benefits Tax Counsel
Office of Tax Policy
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

**Re: Catch-up Contributions Correction**

Dear Madams:

The National Association of Government Defined Contribution Administrators (NAGDCA) is writing regarding the omission of certain legislative language in Section 603 of the *SECURE 2.0 Act of 2022* (SECURE 2.0). We appreciate the help that Treasury has provided in clarifying previous issues and look forward to any assistance you can offer on this issue.

NAGDCA governmental members oversee plans for participants from 65 state and territorial government entities and 157 local government entities, including counties, cities, public safety agencies, school districts, and utilities. NAGDCA's members administer governmental deferred compensation and defined contribution plans, including Section 457(b), 401(k), 401(a), and 403(b) plans. The association provides a forum for working together to improve defined contribution plan operations and outcomes by sharing information on investments, marketing, administration, and the federal laws and regulations governing these plans.

On December 23, 2022, Congress passed SECURE 2.0 as part of a government spending bill (Div. T, H.R. 2617, 117th Cong.). Section 603 of SECURE 2.0 was intended to function as a revenue raising provision by requiring all catch-up contributions made to defined contribution plans be made on a Roth basis, except for those with $145,000 or less in wages for the prior year. However, as you are aware, a drafting error in the final version of the bill eliminated important text that executes this provision. We recognize that the IRS and Treasury are generally constrained by statutory language but believe there is a path that the IRS and Treasury may look to to resolve this inadvertent error.

Specifically, we submit that Treasury could issue guidance to the public now following the approach it used in Notice 2007-99 with respect to the interpretation of Internal Revenue Code section 402(l) as added by the Pension Protection Act of 2006; that is, that the agency is issuing guidance in expectation of a future legislative correction. This approach is reasonable, as the relevant lawmakers and their staff are aware of this technical error, but may have difficulty finding a timely legislative vehicle to immediately advance such a correction. Further, we submit that enough legislative history exists for Treasury to properly issue guidance stating that it will follow Congressional intent for the provision, rather than the erroneous final text (*see* Senate Finance Committee's plain English section-by-section summary; Joint Committee on Taxation's revenue estimate; Sec. 603, H.R. 2954, 117th Cong.; Sec. 1102, S. 4808, 117th Cong.). Additionally, Treasury could rely on the absurdity principle of statutory construction to arrive at the conclusion that Congress did not intend to pass legislation that is clearly ineffective.

Thank you for your time and consideration. We would be happy to meet with you to discuss this matter further if it would be helpful. Please call David Levine at 202-861-5436, Brigen Winters at 202-861-6618, or the undersigned at 859-469-5789 if you have any questions.

Sincerely,

Matt Petersen
Executive Director