Publications

Year-End Challenges and Opportunities: Congress Passes SECURE Act, Caddy Tax Repeal, and More

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On Thursday, December 19, the Senate passed two spending bills to fund the government through September 30, 2020, one of which (H.R. 1865, the "Further Consolidated Appropriations Act of 2020" or the "Act") contains the provisions from the *Setting Every Community Up for Retirement Enhancement Act of 2019* (the "SECURE Act," H.R. 1994). The House passed the two spending bills earlier this week and the President is expected to sign them into law by tomorrow. The SECURE Act includes almost thirty provisions aimed at encouraging the adoption of employer-sponsored plans and lifetime income options, altering plan distribution rules, easing administrative requirements, improving certain types of defined benefit plans, and more. Notably, a number of the provisions are effective with the New Year (which is fast approaching!).

The Act also includes a number of other retirement and health and welfare provisions of interest to employers and service providers. Among other things, it repeals three tax provisions from the Affordable Care Act ("ACA") – the "Cadillac tax," health insurer tax, and medical device tax – and includes a series of tax and disaster-related provisions, including provisions affecting employee benefits.

Below is background on the SECURE Act's history and a summary of its key provisions, as well as a summary of other notable retirement and health and welfare provisions in the Act.

I. SECURE Act Provisions (*Division O unless noted otherwise)*

The SECURE Act had its origins in the *Retirement Enhancement and Savings Act* ("RESA," H.R. 1007), which was unanimously passed by the Senate Finance Committee in 2016. RESA's key provisions, which were included in the SECURE Act, included permitting "open" multiple employer plans and creating a fiduciary safe harbor for in-plan lifetime income options. Despite bipartisan support, RESA never received a vote in the full Senate. In 2018, as part of GOP leadership's second round of tax reform bills, many of RESA's key provisions were included in the Family Savings Act ("FSA," H.R. 6757), which passed the House but did not advance in the Senate.

Trying again this spring, Ways and Means Committee Chairman Richard Neal (D-MA) negotiated a new version of RESA – renamed the SECURE Act – by adding a few provisions from the FSA, including an expansion of permitted 529 plan distributions. The House passed the SECURE Act on a vote of 417-3 on May 23, 2019, but the bill languished in the Senate throughout the summer and fall. Senate leadership attempted several times to pass the SECURE Act by unanimous consent, but those efforts were repeatedly blocked by a small group of senators. After months of uncertainty and speculation, the SECURE Act was included in the agreement to fund government through September 30, 2020.

A. Encouraging Employer-Provided Plans

- *Pooled Employer Plans (Section 101).* The SECURE Act permits unrelated employers (i.e., those without so-called "commonality") to pool their resources by participating in a new type of MEP, provided certain conditions are met. The new plans – referred to as Pooled Employer Plans – will be treated as a single plan under the Employee Retirement Income Security Act of 1974 ("ERISA"). The legislation is necessary because of Department of Labor ("DOL") guidance, which generally prevents unrelated employers from participating in a single plan. The SECURE Act also amends the Internal Revenue Code of 1986 (the "Code") to provide a procedure for ensuring that one employer's qualification problem does not lead to the disqualification of an entire Pooled Employer Plan (or of a multiple employer defined contribution plan maintained by employers having a common interest other than adopting the plan). Effective for plan years beginning after December 31, 2020.
- *Increase to Small Employer Plan Start-Up Credit (Sections 104 and 105)*. Under current law, an eligible employer with 100 or fewer employees may receive a nonrefundable income tax credit for qualified start-up costs of adopting a new qualified retirement plan. The SECURE Act increases the amount of the credit (up to $5,000 for three years) and provides for an additional nonrefundable credit (up to $500 per year for three years) for small employers that establish plans that include automatic enrollment or add automatic enrollment as a feature to an existing plan. Effective for taxable years beginning after December 31, 2019.
- *Plan Adoption Date (Section 201).*The SECURE Act allows an employer to adopt a qualified retirement plan after the close of a taxable year so long as it is adopted before the deadline for filing the employer's tax return for the taxable year. Effective for plans adopted for taxable years beginning after December 31, 2019.

B. Lifetime Income Provisions

- *Lifetime Income Disclosure (Section 203).*The SECURE Act requires employers to provide defined contribution plan participants with an estimate of the amount of monthly annuity income the participant's balance could produce in retirement (if benefits were received in a qualified joint and survivor annuity and a single life annuity). The new lifetime income disclosure must be included on participants' annual benefit statements, and employers and plan fiduciaries will not have fiduciary responsibility for providing estimates in accordance with DOL assumptions and guidance. The SECURE Act directs DOL to issue model lifetime income disclosures and prescribe assumptions that may be used in converting participant account balances to lifetime income stream equivalents. Effective for benefit statements furnished more than 12 months after the latest of DOL's publication of an interim final rule or model disclosures and assumptions.
- *Fiduciary Safe Harbor for Selection of Lifetime Income Provider (Section 204).*The SECURE Act creates a new fiduciary safe harbor for employers who opt to include a lifetime income investment option in their defined contribution plan. In 2008, DOL published a safe harbor for annuity selection in defined contribution plans, but many view the rules as too challenging to provide meaningful relief, particularly given the difficulty in evaluating the financial capability of the insurer. The SECURE Act specifies the measures that a plan fiduciary may take with respect to the selection of an insurer to comply with his or her fiduciary duties. Specifically, a fiduciary is deemed to have satisfied its fiduciary requirements with respect to the financial capability of the insurer if the fiduciary receives certain written representations from the insurer as to its status under and satisfaction of state insurance laws. Effective upon enactment.
- *Portability of Lifetime Income Options (Section 109).*The SECURE Act permits participants to make direct trustee-to-trustee transfers (or transfer annuity contracts) to an eligible employer plan/IRA of "lifetime income investments" that are no longer authorized to be held as investment options under a qualified defined contribution, 403(b) plan, or governmental 457(b) plan, without regard to any plan restrictions on in-service distributions. Effective for plan years beginning after December 31, 2019.

C. Changes Affecting Plan Distributions

- *Post-Death Required Minimum Distribution Rules for IRAs and Defined Contribution Plans (Section 401).*The current post-death required minimum distribution ("RMD") rules vary depending on whether an employee or IRA owner dies on or after or before the required beginning date and whether the employee or IRA owner has a designated beneficiary. The SECURE Act changes the post-death RMD rules for non-defined benefit plans to generally require that all distributions after death (for distributions to a designated beneficiary) be made by the end of the tenth calendar year following the year of death. The 10-year distribution requirement generally does not apply if the designated beneficiary is an eligible beneficiary, which is defined as any beneficiary who, as of the date of death is, a surviving spouse, disabled, chronically ill (including certain trusts for the disabled/chronically ill), not more than 10 years younger than the employee (or IRA owner), or a child of the employee (or IRA owner) who has not reached the age of majority. Generally effective for distributions by reason of a participant's death after December 31, 2019 (December 31, 2021 for governmental plans and certain collectively bargained plans). The requirements do not apply to a qualified annuity that is a binding annuity in effect on enactment.
- *Increase in Age for Required Beginning Date (Section 114).* The SECURE Act increases the age at which required minimum distributions must begin from 70 ½ to 72. Effective for individuals turning 70 ½ after December 31, 2019.
- *Child Birth or Adoption Withdrawals (Section 113)*. The SECURE Act permits individuals to take penalty-free withdrawals of up to $5,000 (on a controlled group basis) from their qualified defined contribution, 403(b), and governmental 457(b) plans and IRAs for expenses related to the birth or adoption of a child for up to one year following the birth or legal adoption. Effective for distributions after December 31, 2019. Subject to certain requirements, these distributions may be recontributed to an applicable eligible retirement plan to which a rollover can be made.
- *Limits on Loans through Credit Cards (Section 108).*The SECURE Act prohibits plan loans made through credit cards. Effective for loans made after the date of enactment.
- *Reduced Minimum Age for In-Service Distributions (Section 104 of Division M)*. To raise revenue to offset the cost of the inclusion of the Bipartisan American Miners Act provisions (summarized below), the Act allows in-service distributions under a pension plan or governmental section 457(b) plan at age 59 ½ (rather than age 62 that was permitted for pension plans or age 70 ½ that was permitted for 457(b) plans). Effective for plan years beginning after December 31, 2019.

D. Changes Affecting Plan Administration

- *Part-Time Employees (Section 112)*. The SECURE Act requires that 401(k) plans permit participation by long-term, part-time employees who work at least 500 hours in three consecutive 12-month periods (and have reached age 21). The provision provides nondiscrimination and top-heavy testing relief with respect to long-term, part-time employees, as no employer contributions are required for these employees. For vesting purposes, a year of service is a 12-month period during which the part-time employee earned at least 500 hours of service. Generally effective for plan years beginning after December 31, 2020.
- *Increase on Limit on Automatic Enrollment QACA Safe Harbor Default Rate (Section 102).*The automatic enrollment safe harbor to the 401(k) plan nondiscrimination rules imposes a 10 percent limit on default automatic contribution rates. The SECURE Act increases this limit to 15 percent (10 percent cap during the participant's first year of participation). Effective for plan years beginning after December 31, 2019.
- *Nonelective 401(k) Safe Harbor Changes – Applicable To Traditional and QACA Safe Harbors (Section 103).*The SECURE Act makes the following changes to the rules that apply to nonelective contribution 401(k) safe harbor plans: (1) eliminates the safe harbor notice requirement with respect to nonelective 401(k) safe harbor plans; (2) permits a plan to be amended to become a nonelective 401(k) safe harbor plan at any date before the 30th day before the close of the plan year; and (3) permits a plan to be amended to become a nonelective 401(k) safe harbor plan after the 30th day before the close of the plan year if the plan is amended to provide for a nonelective contribution of at least four percent of compensation for all eligible employees and the amendment is made by the last day for distributing excess contributions for the plan year (i.e., generally by the close of the following plan year). Effective for plan years beginning after December 31, 2019.
- *Consolidation of Reporting (Section 202).*The Act directs the IRS and DOL to work together to modify Form 5500 so that all members of a group of plans may file a consolidated Form 5500. In general, a group of plans would be eligible for a consolidated form if all the plans in the group (1) are defined contribution plans (or individual accounts); (2) have the same trustee, the same

named fiduciary(ies), and the same administrator; (3) use the same plan year; and (4) provide the same investments or investment options to participants and beneficiaries. Effective for plan years beginning after December 31, 2021.

- *Increased Penalties for Failure to File Retirement Plan Returns (Section 403).* The SECURE Act increases the Code penalties for failing to file a Form 5500 to $250 per day (but not to exceed $150,000). It increases the penalties for failing to provide a required withholding notice (which applies to qualified plans and IRAs) to $100 per failure (but not to exceed $50,000 maximum in penalties per year). It also increases penalties for failures to file a registration statement for deferred vested benefits or file a required notification of change generally to $10 per day (but not to exceed $50,000 and $10,000, respectively). Effective for returns due after December 31, 2019.
- *Increase in Penalty for Failure to File (Section 402)*. The Act increases the Code minimum penalty for a late tax return to the lesser of $435 (adjusted for inflation) or 100 percent of the amount required to be shown as tax on the return. Effective for returns with due dates (including extensions) after December 31, 2019.
- *Remedial Amendment Period (Section 601)*. The Act includes a special remedial amendment period that provides anti-cutback relief and an extended amendment deadline until no earlier than the end of the 2022 plan year (2024 for governmental and collectively bargained plans).

E. Defined Benefit Plan Provisions

- *Community Newspaper Plans (Section 115)*. The SECURE Act permits certain frozen "community newspaper plans" to elect to apply alternative funding rules to the plan and other plans sponsored by members of the controlled group. Effective retroactively to plan years ending after December 31, 2017.
- *PBGC Premiums for CSEC Plans (Section 206).* The SECURE Act sets Pension Benefit Guaranty Corporation insurance premiums for cooperative and small employer charity ("CSEC") plans at $19 per participant and $9 for each $1,000 of unfunded vested benefits. Effective for plan years beginning after December 31, 2018.
- *Nondiscrimination Flexibility for Frozen Plans (Section 205).* The SECURE Act provides nondiscrimination, minimum coverage, and 401(a)(26) relief with respect to benefit accruals and benefits, rights, and features for a closed class of participants under a defined benefit plan that has been closed for new hires, provided that the plan satisfies certain requirements. This change is particularly important to "soft" frozen plans with more mature, highly compensated participant populations. Generally effective upon enactment.

F. Changes Affecting Only IRAs

- *Repeal of Maximum Age for Traditional IRA Contributions/Deductions (Section 107).* The SECURE Act repeals the prohibition on contributions (and deductions) to a traditional IRA for individuals who have attained age 70 ½ by the end of a year. Effective for contributions made for taxable years beginning after December 31, 2019.
- *Stipends and Difficulty of Care Payments Treated as Compensation (Sections 106 and 116).* The SECURE Act treats as compensation amounts includible in income and paid to aid individuals in their pursuit of graduate or postdoctoral study or research for IRA contribution purposes. Similarly, the SECURE Act permits qualified foster care payments excludable under the Code section 131 "difficulty of care" exemption to be treated as compensation for purposes of making contributions to a defined contribution plan (as after-tax contributions) or IRA. Stipend provision effective for taxable years beginning after December 31, 2019. Difficulty of care provision effective for plan years beginning after December 31, 2015 for defined contribution plans, but for IRAs it applies to contributions after the date of enactment.

G. Other Provisions Affecting Specific Plan Types

- *529 Plans (Section 302).* The SECURE Act allows tax-free distributions from 529 plans for certain apprenticeship program expenses and qualified student loan repayments of up to $10,000 per individual. Effective for distributions made after December 31, 2018.
- *Treatment of 403(b) Custodial Accounts upon Plan Termination (Section 110)*. The SECURE Act provides that the Secretary will issue guidance that will provide that, if an employer terminates a 403(b) plan, the account can be distributed in kind to a participant

or beneficiary. The individual custodial account will be maintained on a tax-deferred basis as a 403(b) custodial account until paid out, subject to compliance with the 403(b) rules in effect at the time that the individual custodial account is distributed. Retroactively effective for plan years beginning after December 31, 2008.

- *Clarification of Church Plan Rules (Section 111).* The SECURE Act clarifies that employees of nonqualified church-controlled organizations may be covered under a Code section 403(b) plan that consists of a retirement income account. Effective for years beginning before, on, or after enactment.
- *Benefits for Volunteer Firefighters and Emergency Medical Responders (Section 301).* The SECURE Act reinstates, for one year, the exclusions for state or local tax benefits and qualified reimbursement payments provided to members of volunteer emergency response organizations. Effective for taxable years beginning after December 31, 2019.
- *Benefits for Children of Military Members and First Responders Killed in the Line of Duty (and other parents with unearned income of minor children) (Section 501).* The SECURE Act reverses a provision that resulted in unexpectedly high taxes for parents with unearned income of minor children, particularly children of military members and first responders killed in the line of duty. Optionally retroactively effective for tax years beginning after December 31, 2017.

II. Repeal of Affordable Care Act Health Taxes (*Division N)*

- *Repeal of Medical Device Excise Tax (Section 501)*. The Act fully repeals the ACA medical device excise tax. The 2.3 percent excise tax on the value of medical devices sold domestically went into effect in 2013 but was suspended by Congress twice, and was not in effect during the period beginning on January 1, 2016 through December 31, 2019. The Joint Committee on Taxation ("JCT") estimates that repeal of the medical device excise tax will cost $25.5 billion over ten years. Effective for sales after 2019.
- *Repeal of Annual Fee on Health Insurance Providers (Section 502).* The Act also fully repeals the ACA annual fee on health insurance providers ("HIT"). The HIT imposes a fee on each covered entity engaged in the business of providing health insurance for United States health risks. The HIT applies to policies in the individual and small group markets, insured employer plans, Medicaid managed care, Medicare Part D, and Medicare Advantage plans. The fee is divided among health insurers based on their market share and their premiums written. The fee was effective beginning in 2015 but was under a moratorium for 2017 and 2019. JCT estimates that the repeal of the HIT will cost almost $151 billion over ten years. Effective for calendar years beginning after 2020.
- *Repeal of Excise Tax on High Cost Employer-Sponsored Health Coverage (Section 503)*. The Act repeals the much-maligned ACA excise tax on high-cost employer medical plans, widely referred to as the "Cadillac Tax." The Cadillac Tax was intended to curtail the preferred treatment of employer-sponsored health plans and reduce excess health spending. The tax was equal to 40 percent of the value of health benefits exceeding certain statutory thresholds, which were projected to be $11,200 for single coverage and $30,150 for family coverage in 2022. The Cadillac Tax would have applied to both employers' and employees' share of the cost of health coverage, as well as to contributions to health saving accounts, health reimbursement arrangements, and medical flexible spending accounts. Originally scheduled to become effective in 2018, the tax was delayed numerous times by Congress and most recently was set to take effect in 2022. JCT estimates that repeal of the Cadillac Tax will cost almost $197 billion over ten years. Effective for taxable years beginning after 2019.

III. Extension of Certain Expiring Provisions and Other Tax Provisions (*Division Q)*

- *Reduction in Medical Expense Deduction Floor (Section 103).* The Act extends until December 31, 2020, the lower threshold of 7.5 percent of adjusted gross income for medical expense deductions. The ACA changed the specified amount of adjusted gross income from 7.5 percent to 10 percent. For 2017 and 2018, however, the threshold amount was lowered to 7.5 percent. The Act keeps the lower (7.5 percent) threshold in place for 2019 and 2020. JCT estimates that the reduction in the medical expense deduction floor will cost a total of $3.7 billion over ten years.
- *Above the Line Deduction for Qualified Tuition and Related Expenses (Section 104).* Individuals are allowed a deduction equal to their qualified tuition and related expenses, including amounts paid for tuition, fees and other related expense for an eligible student that are required for enrollment or attendance at an eligible educational institution. The deduction was scheduled to sunset at the end

of 2017, but the Act retroactively extends the deduction until the end of 2020. JCT estimates that the extension of the deduction for qualified tuition and related expenses will cost $664 million over ten years.

- *Employer Credit for Paid Family and Medical Leave (Section 142).* The 2017 Tax Cuts and Jobs Act established new Section 45S of the Code, which provides a business tax credit for certain employer-paid family and medical leave. The paid family and medical leave credit ranges from 12.5 percent to 25 percent of the amount of wages paid to qualifying employees for 2 to 12 weeks of family and medical leave annually, where such wage payments are at least 50 percent of the wages normally paid to an employee. The paid family and medical leave credit was originally available for wages paid in 2018 and 2019. The Act extends the credit through 2020. JCT estimates that the extension of the credit will cost $2.2 billion over ten years.
- *Credit for Health Insurance Costs of Eligible Individuals (Section 146).* The Health Coverage Tax Credit ("HCTC") is a refundable tax credit that subsidizes most of the cost of qualified health insurance for eligible taxpayers and their family members. Eligibility for the HCTC is limited to individuals who are eligible for Trade Adjustment Assistance (TAA) allowances because they experienced qualifying job losses and to individuals whose defined-benefit pension plans were taken over by the Pension Benefit Guaranty Corporation because of financial difficulties. The HCTC has a sunset date of January 1, 2020, but the Act extends it by one year. JCT estimates that the extension of the HCTC will cost $43 million over ten years.
- *Disaster Relief (Sections 202 through 205).* The Act provides several forms of tax relief to individuals and businesses affected by major disasters. The relief applies to major disasters declared in the period from January 1, 2018 through the 60th day after the measure's enactment. California areas affected by wildfires that have already received aid are excluded. Among other relief measures, the Act modifies several retirement plan rules for individuals in areas affected by disasters by allowing affected individuals to: (1) take temporary withdrawals or loans of as much as $100,000 from their retirement accounts without penalty with withdrawals treated as tax-free rollovers if repaid within three years; (2) pay back loans that were outstanding over an extra year; (3) recontribute certain withdrawals taken for homes in the disaster area; (4) make it easier for those affected by disasters to obtain the earned income tax credit and refundable portion of the child tax credit by basing their eligibility on their income from the previous year; and (5) provide an automatic extension to certain retirement plan deadlines applicable to those affected by disasters. These provisions will generally be effective on the date of enactment. JCT estimates that the disaster relief provisions will collectively cost $12.8 billion over ten years.
- *Repeal of Increase in Unrelated Business Taxable Income for Certain Fringe Benefit Expenses (Section 302).* The Act repeals a provision of the 2017 Tax Cuts and Jobs Act that subjected tax-exempt organizations to unrelated business income tax on the value of qualified parking and transportation fringe benefits provided to employees. The repeal of the provision is retroactive to the 2017 law's enactment. JCT estimates that the repeal of the unrelated business taxable income provision costs $1.87 billion over ten years.

IV. American Miners Act Provisions *(Division M)*

The Act includes the provisions from the American Miners Act (S. 27) that provides federal funding for certain coal miner pension and healthcare benefit plans. Under the provisions, the Department of the Treasury must transfer additional funds to the 1974 United Mine Workers of America ("UMWA") Pension Plan to pay pension benefits required under that plan if the annual limit on transfers under the Surface Mining Control and Reclamation Act of 1977 exceeds the amount required to be transferred for existing obligations of the Abandoned Mine Reclamation Fund. The Act also increases the annual limit on transfers from $490 million to $750 million. To raise revenue to offset some of these costs to the Federal government, the Act also reduces the minimum age for in-service distributions in pension plans and 457(b) plans (summarized above).

V. Prohibited Transaction Exemption on Pharmacy Benefit Services *(Title XIII of Division P)*

The Act provides a temporary, five year exemption from the prohibited transaction rules for the offering of pharmacy benefit services to (or the purchase of pharmacy benefit services by participants of) a group health plan sponsored by an organization that is tax-exempt under Code section 501(c)(5) and that was established in Chicago, Illinois on August 12, 1881, or one sponsored by a regional council, local union or other labor organization affiliated with such entity. The exemption applies to any arrangement where the entity or related organization provides pharmacy benefit services that include prior authorization and appeals, a retail pharmacy network, pharmacy benefit administration, mail order fulfillment, formulary support, manufacturer payments, audits, and specialty pharmacy and goods, to the group health plan, provided that certain conditions, including oversight by an independent fiduciary, are satisfied.