Church Plans Under the SECURE Act

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Many of the provisions of the Setting Every Community Up for Retirement Enhancement Act of 2019 (the "SECURE Act") do not apply to non-electing church plans, but some do, notably those dealing with certain 403(b)(9) plans and distributions. This is to briefly summarize the most significant changes affecting church plans. Church plans should start considering what changes in plan terms, recordkeeping, reporting and communications may be necessary to reflect the new distribution rules.

Clarification That Non-Qualified Church-Controlled Organizations Can Participate in 403(b)(9) Retirement Income Accounts

As anticipated would happen at some point, the SECURE Act included a provision that clarifies that employees of a nonqualified church-controlled organization (often referred to as "Non-QCCOs") may be covered under a Code section 403(b)(9) retirement income account. Non-QCCOs are generally 501(c)(3) organizations controlled by or associated with a church which receive more than 25% of receipts from sales of goods or services or government grants – a definition that covers many church-related hospitals, nursing homes, colleges, universities and cemeteries. This was made effective for years beginning before, on, or after enactment.

Treatment of 403(b) Custodial Accounts Upon Plan Termination

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, and does not have to be distributed in cash. Such an 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. This essentially allows 403(b)(7) custodial accounts to follow rules similar to Rev. Rul. 2011-7 for 403(b) annuity contracts upon the termination of a 403(b) plan. This provision is retroactively effective for plan years beginning after December 31, 2008.

Treatment of Part-Timers Under 401(k) Plans Where the 410(b) Nondiscrimination Rule Applies

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. This is generally effective for plan years beginning after December 31, 2020. This change does not apply to 403(b) plans. Because this change is made to Code section 401(k) rather than to the coverage rules of Code section 410 (from which church plans are generally exempt, so long as they comply with pre-ERSIA coverage rules), this would technically appear to apply to church 401(k) plans.

Distribution Changes Affecting Church Plans

A. Changes for Both DB and DC Plans

1. Increase in RMD Age

The SECURE Act increases the age at which required minimum distributions (RMDs) must begin from 70 ½ to 72. This is effective for individuals turning 70 ½ after December 31, 2019. This is the main change for defined benefit plans.

2. In-Service Distribution Age Lowered

To raise revenue, the separate Bipartisan American Miners Act allows (but does not require) in-service distributions under a pension plan (e.g., a defined benefit or money purchase plan – but *not* 457(b) plans of tax-exempt entities, for example, for Non-QCCOs) at age 59 ½ rather than age 62. This is effective for plan years beginning after December 31, 2019.

B. Changes Affecting DC Plans Only

1. New 10 Year Deadline for Beneficiary Distributions

For non-defined benefit plans, the SECURE Act generally requires that all distributions after death to a designated beneficiary be made by the end of the 10th calendar year following the year of death. However, exceptions include if the designated beneficiary is, as of the date of death, a surviving spouse, disabled, chronically ill (including certain trusts for the disabled/chronically ill), not more than 10 years younger than the employee, or a child of the employee (or IRA owner) who has not reached the age of majority or payments under certain qualified annuities in effect on the date of enactment. This is effective for plan distributions because of a participant's death after December 31, 2019, though the deadline for certain collectively bargained plans is December 31, 2021.

2. Qualified Birth or Adoption Distributions

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 church 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. This is effective for distributions after December 31, 2019.

C. Amendment Deadline

The Act includes a special remedial amendment period until no earlier than the end of the 2022 plan year (2024 for collectively bargained plans).

D. What Are Some of the Issues in the Distribution Changes?

1. Shifting the RMD Commencement Age to 72: Fortunately, under the effective date rules, the distributions to any participant currently receiving RMDs or beginning RMDs by April 1, 2020 because they had attained age 70 and ½ on or before December 31, 2019 will not have to be changed. But for participants attaining age 70 and ½ in 2020 and thereafter, the plan will need to change its systems to not start automatically commencing benefits by the following April 1, and be reprogrammed to commence benefits by April 1 following the year in which the participant attains age 72. Such changes, and effectively running parallel distribution systems, may not be easy.
2. Reporting on the 1099-R. RMDs are not eligible for rollover and are subject to 10% voluntary withholding, while amounts that are not RMDs are generally eligible for rollover and are subject to mandatory 20% withholding. With the change in the RMD commencement age from 70 and ½ to 72, withholding and reporting will need to be adjusted for any distributions during this period, such as distributions not in the form of an annuity that may be eligible for rollover, from the 70 ½ distribution date to the age 72 distribution date.
3. Changing Distribution Rules for DC Plan Beneficiaries. Plans will need to comply with the 10-year rule (or one of its exceptions) for distributions to a designated beneficiary after death for participants dying after 2021.

E. Some Decisions May Need to be Made

Church money purchase and defined benefit plans may wish to consider the impact of lowering of the age permitting in-service distributions. Many church defined benefit plans do not allow in-service distributions at all, so it may be a moot point for them, but for church plans that do allow in-service distributions, it is something that may be considered. Church defined contribution plans may also wish to consider adding distribution options for birth or adoption.

Some Observations on Other Provisions

While we focus above on the retirement provisions likely to be of the greatest interest to churches, there are other provisions to be aware of with more general applicability, which you can find discussed in other Groom Law Group resources, including but not limited to:

- Repeal of the 2017 Tax Cuts and Jobs Act provision that subjected tax-exempt organizations to unrelated business income tax on the value of qualified parking and transportation fringe benefits provided to employees.
- Creation of a new type of multiple employer plan, known as the Pooled Employer Plan or "PEP".
- Increase to the small employer plan start-up credit.
- Lifetime income provisions (including some portability provisions).
- 401(k) safe harbor changes.
- Affordable Care Act changes, including repeal of the much-dreaded excise tax on high-cost employer medical plans known as the "Cadillac Tax."

Next Steps

Church plan sponsors will want to consider the impact of these changes on their DB and DC plans. Groom can assist plans in evaluating this. While amendments to plans may be required, changing administrative systems to accommodate the new rules could be a particular area of concern. Plan communication and form changes will also likely be necessary.

If you have any questions, please contact David Powell or your regular Groom attorney. More information is available at the Groom SECURE Act Resource Library.