

ELIZABETH THOMAS DOLD is a Principal at Groom Law Group, Chartered in Washington, DC.

DAVID N. LEVINE is a Principal at Groom Law Group, Chartered in Washington, DC.

Employee Benefits Corner

IRS Issues Favorable Initial PLESA Guidance on Match Restrictions

By Elizabeth Thomas Dold and David N. Levine

Notice 2024-22 brings important initial guidance on appropriate matching restrictions for Pension-Linked Emergency Savings Accounts (PLESAs), which was added to the Internal Revenue Code by Section 127 of SECURE 2.0, and is effective this year (*i.e.*, plan years beginning after December 31, 2023). This guidance was mandated by the Act to address the historic churning/abuse concerns with these types of in-service withdrawals that have an employer match. The idea goes, the employee saves into the account, the employer matches the savings, then the employee takes out his savings and recontributes it and gets another employer match on the same funds (and so on) – *i.e.*, churning. The Internal Revenue Service (IRS) has addressed this issue over the years and provides guidance under two key Revenue Rulings—Rev. Rul. 74-55 and Rev. Rul. 74-56. This Notice provides a nice summary of the PLESA accounts and addresses the appropriate procedures to address the churning issue.

As more fully discussed below, employers can place no restrictions or take no action to address this churning risk and still have a good PLESA. This simplification of the rules is a helpful first step for employers and recordkeepers to offer this feature, which is optional.

PLESA Overview

Section 127 of the SECURE 2.0 Act amends title I of the Employee Retirement Income Security Act of 1974 and Code Sec. 402A to provide for the creation of PLESAs. These accounts are short-term savings accounts established and maintained in connection with a defined contribution plan and are treated as a type of designated Roth account. The devil is in the details of these accounts, as the Act places a lot of rules on these accounts:

- *Roth Account.* The account is generally treated as a designated Roth account and funded by the employee with after-tax dollars (no tax deduction or exclusion from income for making a deposit into the account).
- *Participation.* Enrollment can be done by either (1) an offer to enroll an eligible participant in a PLESA or (b) automatically enroll an eligible participant in a PLESA pursuant to an automatic contribution arrangement.
- *Accounting.* The plan must separately account for contributions to the PLESA (and any earnings thereon), maintain separate recordkeeping with respect to

each PLESA, and allow withdrawals from the PLESA at the participant's discretion, in whole or in part, at least once per month.

- **Eligibility.** An eligible participant means an individual, without regard to whether the individual otherwise participates in the plan, who meets any age, service, and other eligibility requirements of the plan and is not a highly compensated employee (HCE; as defined in Code Sec. 414(q)).
- **HCE Withdrawal.** An eligible participant on whose behalf a PLESA is established who thereafter becomes a HCE cannot make further contributions to the PLESA but must retain the right to withdraw any account balance upon termination of employment or plan termination.
- **Account Limit.** Subject to certain excess contribution rules, no contribution shall be accepted to a PLESA to the extent such contribution would cause the portion of the account balance attributable to participant contributions to exceed the lesser of (i) \$2,500 or (ii) an amount determined by the plan sponsor of the PLESA.
- **Employer Match.** If an employer makes any matching contributions to a defined contribution plan of which a PLESA is a part, the employer must make matching contributions on behalf of an eligible participant on account of the participant's contributions to the PLESA.
 - The matching contributions must be at the same rate as any other matching contribution on account of an elective contribution by the participant.
 - The matching contributions will be made to the participant's account under the defined contribution plan that is not the PLESA.
 - The matching contributions on account of contributions to the PLESA must not exceed the maximum account balance for the plan year.
 - For purposes of any applicable limitation on matching contributions, any matching contributions made under the plan are treated first as attributable to the elective deferrals of the participant other than contributions to a PLESA.
 - A plan of which a PLESA is a part may employ reasonable procedures to limit the frequency or amount of matching contributions with respect to contributions to such account, solely to the extent necessary to prevent manipulation of the rules of the plan to cause matching contributions to exceed the intended amounts or frequency. A plan of which a PLESA is a part is not required to suspend matching contributions following any participant withdrawal of contributions,

including elective deferrals and employee contributions, whether or not matched and whether or not made pursuant to an automatic contribution arrangement. The Act provides that the Secretary of the Treasury, in consultation with the Secretary of Labor, shall issue regulations or other guidance not later than 12 months after the date of the enactment of the SECURE 2.0 Act with respect to the anti-abuse rules described in Code Sec. 402A(e)(12). This is the focus of this Notice.

- **Withdrawal.** A PLESA generally must allow for withdrawal by the participant on whose behalf the account is established of the account balance, in whole or in part, at the participant's direction, at least once per calendar month. The distribution of such a withdrawal by the participant must be made as soon as practicable after the date on which the participant elects to make such withdrawal.
 - A distribution from a PLESA is treated as a qualified distribution for purposes of Code Sec. 402A(d) and treated as a distributable event (*i.e.*, meeting the requirements of Code Secs. 401(k)(2)(B)(i), 403(b)(7)(A)(i), 403(b)(11), and 457(d)(1)(A)).
 - The 10-percent additional tax on early distributions from qualified retirement plans under Code Sec. 72(t)(1) does not apply to distributions from a PLESA.
 - For purposes of Code Sec. 72, contributions to a PLESA (and any income allocable thereto) may be treated as a separate contract.
- **Anti-Cutback Relief.** Notwithstanding Code Sec. 411(d)(6), a plan that includes a PLESA may cease to offer such accounts at any time.

Anti-Abuse Procedures

The Notice highlights several statutory provisions to which a plan might look to limit the ability of participants to manipulate the rules of the plan to cause matching contributions to exceed the intended amounts or frequency.

- **Order of Matching Contributions.** The Code provides that any matching contributions made under the plan are treated first as attributable to a participant's elective deferrals other than PLESA contributions. As a result, any elective deferrals a participant makes under the underlying defined contribution plan will be matched first and will lower the availability of matching contributions that will be made on account of participant contributions to their PLESA.
- **Limitation on Annual Matching Contributions.** The Code provides that matching contributions on

account of contributions to the PLESA cannot exceed the maximum account balance for the plan year. The Code permits a plan sponsor to set a lower PLESA balance limit than the \$2,500 limit. A lower limit on the portion of the PLESA balance attributable to participant contributions would result in a correspondingly lower cap on annual matching contributions. An employer can view these provisions as sufficient anti-abuse provisions and therefore decide not to impose any other restrictions meant to prevent manipulation of matching contributions. Importantly, in such a case, for example, an employer may consider a participant as not manipulating the matching contribution rules if the participant made a \$2,500 contribution in one year, received the matching contribution on such amount, and then took \$2,500 in distributions that year and repeated that pattern in subsequent years.

- **Withdrawal Restrictions.** As plans are not required to permit participants to take more than one distribution per month, plan sponsors may view the option of limiting the number of permissible withdrawals to a maximum of once per month as a sufficient constraint on the potential to manipulate the matching contribution rules.

Therefore, a plan of which a PLESA is a part may, but is not required to, employ reasonable procedures to limit the frequency or amount of matching contributions with respect to contributions to a PLESA. If an employer is still concerned, additional reasonable procedures to prevent abuse are permitted solely to the extent necessary to prevent manipulation of the rules of the plan to cause matching contributions to exceed the intended amounts or frequency. The Notice provides that a reasonable anti-abuse procedure is one that balances the interests of participants in using the PLESA for its intended purpose with the interests of plan sponsors in preventing manipulation of the plan's matching contribution rules. The Notice recognizes that employers may find it challenging to identify participants engaging in manipulative practices because those participants may be able to adapt their pattern of contributions and distributions to replicate patterns of participants making contributions and taking periodic distributions for legitimate purposes, such as unexpected expenses.

The Notice provides examples of anti-abuse procedures that are *not* reasonable and thus may *not* be used to limit the frequency or amount of matching contributions made to the account.

- **Forfeiture of Matching Contributions.** A plan may not provide that matching contributions already made on account of participant contributions to the PLESA

will be forfeited by reason of a participant's withdrawal from a PLESA.

- **Suspension of Participant PLESA Contributions.** A plan may not suspend a participant's ability to contribute to the participant's PLESA on account of a withdrawal from the PLESA.
- **Suspension of Matching Contributions.** A plan may not suspend matching contributions made on account of participant elective deferrals to the underlying defined contribution plan.

Impact of 1974 Revenue Rulings

The Notice expressly addresses the prior guidance set forth in Rev. Rul. 74-55 and Rev. Rul. 74-56 to PLESAs. Rev. Rul. 74-55 provides that a plan that allows for immediate withdrawal of employee contributions on which employer contributions are based can be reasonably expected to result in impermissible manipulation and is not permitted. Rev. Rul. 74-56 provides for a six-month suspension on contributions after a withdrawal and is a permissible restriction to prevent abuse. The ruling also permits forfeiture of match on a withdrawal request. The Notice states that these revenue rulings are not applicable in the context of PLESAs, regardless of whether the contributions are matched.

Comments Requested

The IRS welcomes any comments on PLESAs to be submitted on or before April 5, 2024. In particular, comments on the 1974 rulings and issues related to reasonable anti-abuse procedures are invited in order to explore further examples of what may be reasonable—balancing the policy of incentivizing emergency savings while discouraging potentially abusive practices.

Conclusion

IRS and Department of Labor (DOL) guidance on the application of the PLESA is necessary for this rather complex but beneficial plan feature that will allow tax-free withdrawals for emergencies, while still facilitating savings for retirement. This guidance is the first step into making these accounts viable, providing for allowable and prohibited restrictions for anti-abuse measures. But there remain a number of complexities and open issues to be addressed for these accounts that would benefit from simple, flexible rules, with a good faith implementation standard to bring these accounts into existence for 2024.

This article is reprinted with the publisher's permission from Taxes The Tax Magazine®, a monthly journal published by CCH Incorporated. Copying or distribution without the publisher's permission is prohibited. To subscribe to Taxes The Tax Magazine® or other journals, please call 1-800-344-3734. All views expressed in this publication are those of the author and not necessarily those of the publisher or any other person.



Wolters Kluwer