

## Publications

# Tax-Exempt and Church Plan Highlights From SECURE 2.0

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## PUBLISHED

03/13/2023

## SOURCE

Groom Publication

## SERVICES

Employers & Sponsors

- Fiduciary & Plan Governance
- Retirement Programs

The wide-ranging [SECURE 2.0 Act of 2022](#) (“SECURE 2.0”) radically altered the retirement plan landscape, and is likely to create a significant number of action items for sponsors of retirement plans for tax-exempt entities and church plans.<sup>[1]</sup> This alert briefly summarizes some of the most significant changes impacting these plan sponsors.

As discussed in more detail below, SECURE 2.0, among other things, updated 403(b) plan rules to conform more closely with 401(k) plan rules, and made a number of key changes specific to 457(b) plans (although many of those changes only apply to governmental 457(b) plans). Further, church plans that do not elect to be subject to ERISA (“Non-Electing Church Plans”) were also impacted by a number of the changes made in SECURE 2.0. (Note that “electing” church plans are generally treated the same as other qualified plans and are beyond the scope of this alert). Church retirement accounts under Internal Revenue Code (“Code”) section 403(b)(9) are generally treated as 403(b) annuity contracts.

## I. Key Changes Specific to 403(b) Plans

### A. Multiple Employer 403(b) Plans

SECURE 2.0 permits 403(b) plans to participate in multiple employer plans (“MEPs”) and pooled employer plans (“PEPs”). SECURE 2.0 further directed the Department of Treasury (“Treasury”), in consultation with the Department of Labor (“DOL”), to publish model plan language for multiple employer 403(b) plans. The legislation also directs Treasury to issue regulations providing relief from the “one bad apple” rule for 403(b) plans. This provision does not appear to apply to Non-Electing Church Plans.

The provision is effective for plan years beginning after December 31, 2022.

## B. Long-Term, Part-Time Workers

Prior to the enactment of SECURE 2.0, the Setting Every Community Up for Retirement Enhancement Act, or SECURE Act (“SECURE 1.0”) had generally required 401(k) plans to permit an employee to contribute to a plan if that employee worked at least 500 hours a year with the employer for at least three consecutive years and met the minimum age requirement (21) by the end of the three consecutive year period.<sup>[2]</sup> Notably, section 403(b) plans were not subject to this rule for “long-term part-time workers.” SECURE 2.0 extended this coverage rule to 403(b) plans subject to ERISA, and reduced from three years to two years the required years of service before long-term, part-time employees are eligible to contribute to a plan. These provisions are generally effective for 403(b) plans for plan years beginning after December 31, 2024.

## C. Enhanced 403(b) Plans

SECURE 2.0 amended the Code to permit 403(b) plans with custodial accounts to invest in collective investment trusts (i.e., Revenue Ruling 81-100 group trusts), in addition to mutual funds, effective upon enactment of SECURE 2.0 (December 29, 2022). Unfortunately, this section did not address the Investment Company Act of 1940, which generally prohibits collective investment trusts from accepting 403(b) plan assets. Plan sponsors should remain cautious regarding these investments and seek legal counsel until further guidance is issued.

## D. Hardship Withdrawal Rules for 403(b) Plans

SECURE 2.0 updated the hardship distribution rules for 403(b) plans to conform with the 401(k) plan hardship distribution rules. Prior to the enactment of the Bipartisan Budget Act of 2018 (“BBA”), the hardship withdrawal rules for 401(k) plans and 403(b) plans were generally the same. However, the BBA created some key differences, primarily permitting 401(k) plans to make hardship withdrawals from more contribution sources (such as qualified nonelective contributions and safe harbor matching contributions), and earnings on elective deferrals. Now, the 403(b) plan hardship withdrawal rules have been updated to generally conform with the 401(k) plan rules. The provision also clarified that a distribution will not be treated as failing to be made upon the hardship of an employee solely because the employee does not take a loan under the plan. These provisions become effective for plan years beginning after December 31, 2023.

# II. Impact of Other Key Changes on Tax-Exempt and Church Plans

## A. Increase in the Age Date for Required Minimum Distributions (“RMDs”)

Section 107 of SECURE 2.0 increased the RMD age from 72 to: (i) 73 for an individual who attains age 72 after December 31, 2022 and age 73 before January 1, 2033, and (ii) 75 for an individual who attains age 74 after December 31, 2032. Previously SECURE 1.0 had increased the age of RMDs from 70 ½ to 72. Distributions from 403(b) plans and applicable Non-Electing Church Plans will be subject to these new changes. These changes also apply to RMDs for tax-exempt 457(b) plans, but note that Code section 457(d)(1)(A)(i), which addresses the earliest date on which plan amounts may be made available, was not amended. This provision is effective for distributions required to be made after December 31, 2022 for individuals who reach age 72 after that date.

## B. Automatic Enrollment

SECURE 2.0 requires newly created 401(k) and 403(b) plans to automatically enroll participants, as well as implement a contribution escalation feature starting with the 2025 plan year. As part of automatic enrollment, the plan must implement a minimum contribution deferral percentage with a default rate of between 3% and 10%, and must increase to a contribution rate of between 10% and 15%. Notably, governmental plans and Non-Electing Church Plans are exempt from this provision.

## C. Higher Catch-Up Limits at 60, 61, 62, and 63

Section 109 of SECURE 2.0 increased the catch-up contribution limits applicable to a number of plans, including 403(b) plans, and Non-Electing Church Plans. For taxable years beginning after December 31, 2024, the catch-up limit increased for individuals aged 60 to 63 to the greater of (i) \$10,000, or (ii) 150% of the regular catch-up amount for 2024, indexed for inflation. Note that these increased catch-ups must be Roth contributions (see paragraph H), if the participant earned at least \$145,000 in the prior year.

## D. Treatment of Student Loan Payments as Elective Deferrals for Purposes of Matching Contributions

Section 110 of SECURE 2.0 permits employer contributions made on behalf of employees for “qualified student loan payments” to qualify as a matching contribution. This provision applies broadly to defined contribution plans, including 403(b) plans, tax-exempt 457 plans, and Non-Electing Church Plans. Further, Treasury has been directed to issue implementing regulations on this provision. The provision is effective for contributions made for plan years beginning after December 31, 2023.

## E. “*De Minimis*” Financial Incentives

Section 113 of SECURE 2.0 permits participants to receive *de minimis* financial incentives for contributions to a 403(b) plan (as well as a 401(k) plan), effective with the 2023 plan year. This *de minimis* financial incentive must not be paid for with plan assets. Examples of potential financial incentives include low-value gift cards.

## F. Overpayment Recovery

Section 301 of SECURE 2.0 created special rules addressing the recovery of plan overpayments. Because this provision amends the Code and ERISA, it impacts a broad spectrum of plans, including 403(b) plans and Non-Electing Church Plans. Prior to the enactment of SECURE 2.0, plan fiduciaries that had mistakenly overpaid participants were required to take reasonable steps to recoup overpayments, such as collecting the overpayment from the participant or employer, in order to maintain the tax-qualified status of the plan and comply with ERISA (where applicable). Under the new law, a 403(b) plan (as well as certain other qualified plans, including a Non-Electing Church Plan), will not jeopardize the plan’s tax-qualified status because the plan fails to recover an “inadvertent benefit overpayment” made by the plan, or if the plan sponsor amends the plan to increase past, or decrease future, benefit payments to affected participants and beneficiaries in order to adjust for prior inadvertent benefit payments.

Further, for plans subject to ERISA, plan fiduciaries will not violate ERISA if the fiduciary determines, in the exercise of its discretion, not to seek recovery of all or part of the overpayment from (A) any participant or beneficiary, (B) any plan sponsor or contributing employer to an individual account plan (subject to certain requirements), or a defined benefit plan (unless failure to recover all or part of the overpayment would materially affect the plan’s ability to pay benefits to other participants or beneficiaries), or (C) any fiduciary of the plan, other than a fiduciary whose breach of its fiduciary duties resulted in the overpayment (provided that if the plan established prudent procedures to prevent and minimize overpayments and those procedures were followed by the fiduciary, an inadvertent benefit payment will not give rise to a breach of fiduciary duty). If a plan fiduciary does decide to seek recovery, certain restrictions on recovering the overpayment apply. Note, however, that because Non-Electing Church Plans are not subject to ERISA, restrictions under ERISA will not be applicable to those plans.

## G. Expansion of Employee Plans Compliance Resolution System

Previously, plan sponsors of qualified plans (including 401(a) plans (such as applicable Non-Electing Church Plans) and 403(b) plans) had only limited opportunities to self-correct plan errors under the Employee Plans Compliance Resolution System (“EPCRS”). Under Section 305 of SECURE 2.0, eligible plan sponsors will be permitted to self-correct any eligible inadvertent qualification failure, except if (1) the failure was identified by Treasury prior to the commencement of self-correction, or (2) the self-correction is not completed within a reasonable period after the failure is identified. Under the new law, the loan error that is an eligible inadvertent failure may be self-corrected under EPCRS, and DOL must treat the self-correction as meeting the requirements of DOL’s Voluntary Fiduciary Correction Program (although it may impose reporting or other procedural requirements). Further, Treasury is directed to

revise Revenue Procedure 2021-30 (or any successor guidance) for this change no later than 2 years after the date of enactment (*i.e.*, by December 29, 2024).

## H. Changes to Catch-Up Contributions for High Earners

SECURE 2.0 provided new rules governing regular catch-up contributions to certain qualified plans, including 401(a) plans (including Non-Electing Church Plans) and 403(b) plans. Under prior law, catch-up contributions to 403(b) plans could be made on a pre-tax or Roth basis. Now, beginning after December 31, 2023, if a participant's wages exceed \$145,000 (adjusted for cost of living after 2024), regular catch-up contributions must be made on a Roth basis. Note that this change does not apply to the special catch-up provisions for 403(b) and 457(b) plans (that are based on service, not on age); those catch-up contributions can still be made on a pre-tax basis.

## I. Optional Roth Treatment of Employer Matching or Nonelective Contributions

Section 604 of SECURE 2.0 permits plan sponsors to allow employer matching or non-elective contributions to be treated as Roth contributions. Under prior law, employer matching contributions or nonelective contributions were not permitted to be made on a Roth basis. Now, effective as of the date of enactment (December 29, 2022), plan sponsors of 401(a) plans (including Non-Electing Church Plans) and 403(b) plans, and other qualified plans, are permitted (but not required) to allow employer matching contributions or nonelective contributions on a Roth basis. This provision does not apply to a 457(b) plan sponsored by a tax-exempt organization.

**GROOM INSIGHT:** This provision appears to be administratively challenging to implement, and until further guidance is issued, plan sponsors would be wise to tread carefully before adopting this provision. In the meantime, plan sponsors may be able to accomplish substantially similar objectives by allowing Roth in-plan conversions.

## III. Next Steps

Many SECURE 2.0 changes are highly technical and complex, and will likely require more guidance before they can be implemented. Churches and tax-exempt entities will want to consider the impact of these changes on their retirement plans. Groom can assist plans in evaluating this. If you have any questions, please contact your regular Groom attorney.