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SECURE Act Provisions

June 10, 2019

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Major changes in federal law are in the works that could significantly impact employers' qualified retirement plans, which could require amending such plans to reflect mandatory and elective changes. The U.S. House of Representatives recently passed the Setting Every Community Up for Retirement Enhancement (SECURE) Act by a margin of 417 to 3. A similar bill, the Retirement Enhancement and Savings Act (RESA), is up for consideration in the U.S. Senate. With what appears to be bipartisan support, the SECURE Act – or some compromise between the SECURE Act and RESA – could soon be signed into law. If passed, such legislation would provide for the most significant changes impacting qualified retirement plans since the Pension Protection Act of 2006.

Below is a brief summary of SECURE Act provisions that may be of most interest to employers that sponsor qualified retirement plans:

1. Required minimum distribution age increase for qualified retirement plans:

Current law requires that participants in qualified retirement plans start receiving required minimum distributions from their qualified retirement plans by April 1 of the calendar year in which the participant (i) reaches age 70.5 or (ii) retires. The SECURE Act, in recognition of the fact that Americans are living longer and working until later in life than previously, raises that minimum age requirement to age 72.

2. Required inclusion of long-term part-time employees in 401(k) plans:

Current laws allow employers to exclude their part-time employees (i.e., employees with fewer than 1,000 hours of service in a given year) from 401(k) plans. Under the SECURE Act, employers would be required to permit a part-time employee to participate in their 401(k) plans if the employee has at least 500 hours of service a year for three (3) consecutive years. Such participants are not required to be made eligible for the plan's matching and profit-sharing contributions and special rules regarding application of non-discrimination testing under the tax laws are proposed to account for this exclusion.

3. Annuity selection safe harbor for defined contribution plans:

Most 401(k) plans do not offer annuities as a form of distribution. One concern has always been that if plan fiduciaries select an annuity provider and such provider later cannot make payments under the annuity as anticipated, such fiduciaries could be exposed to liability under ERISA for, among other things, failure to fulfill their duties of prudence (including continued monitoring of the service provider).

The SECURE Act seeks to encourage employers to add annuities to 401(k) plans by creating a safe harbor that provides for satisfaction of the ERISA prudence requirement in selecting annuity providers if, among other things, the plan fiduciaries (i) engage in an objective, thorough, and analytical search for the purpose of identifying annuity providers, (ii) consider the financial capability of such annuity provider to satisfy its obligations under the annuity, (iii) consider the cost (including fees and commissions) of the annuity in relation to the benefits and product features, and (iv) based on such consideration, conclude that, at the time of the selection of the annuity provider, that particular annuity provider is financially capable of satisfying its obligations under the annuity and the relative cost of the annuity is reasonable.

4. Lifetime income disclosures required for defined contribution plan account balances:

The SECURE Act requires benefit statements to be delivered to participants every 12 months that include a disclosure estimating monthly payments the participant would receive if the total account balance were used to provide, alternatively, a qualified joint and survivor annuity and a single life annuity. The DOL would be required to develop a model notice and also provide actuarial assumptions that, if used, would provide a safe harbor from liability as a result of relying on such assumptions. This disclosure requirement applies even if the defined contribution plan does not otherwise provide annuities as an optional form of distribution.

5. Increased maximum automatic contribution percentage for safe harbor 401(k) plans:

Currently, the maximum percentage of employee compensation that may be deferred under a 401(k) plan that includes a "qualified automatic contribution arrangement" (QACA), unless the participant affirmatively elects otherwise, is 10% of eligible compensation. The SECURE Act would raise this maximum to 15%.

6. Elimination of notice requirement for non-elective contribution safe harbor 401(k) plans:

Currently, safe harbor 401(k) plans, whether the employer safe harbor contribution is satisfied by a matching contribution or a non-elective (i.e., profit-sharing) contribution, are required to provide an annual notice to participants apprising them of their rights and obligations under the plan. The SECURE Act would eliminate the requirement to provide such notices with respect to safe harbor 401(k) plans that satisfy the employer safe harbor contribution with non-elective contributions. The notice requirement remains in place with respect to plans that use matching contributions to meet the safe harbor requirements.

7. In-Service Distributions for Child Birth and Adoption Expenses

The SECURE Act would permit a distribution of up to $5,000 for "qualified birth or adoption distributions." Such distributions would not be subject to the 10% tax on early distributions from qualified retirement plans. A "qualified birth or adoption distribution" would be defined to mean any distribution during the one-year period beginning on the date on which the child is born or adopted.

Bracewell will provide further updates in this area as the legislation moves forward through Congress.