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MEMORANDUM

To: Defined Benefit Fund Clients

From: Slevin & Hart, P.C.

Date: February 21, 2023

Re: The Setting Every Community Up for Retirement Enhancement 2.0 Act of 2022

The Setting Every Community Up for Retirement Enhancement 2.0 Act ("SECURE 2.0 Act") was enacted on December 29, 2022 and changes many of the rules governing defined benefit retirement plans.

Below is a list of action items, a summary of the most significant changes made by the SECURE 2.0 Act, and a more in-depth analysis of the provisions that affect defined benefit plans. We will discuss specific changes to affected plan operations and plan amendments with you as the federal agencies issue guidance.

Action Items

As explained in more detail below, in preparation for the provisions of the Act that have or will soon take effect, plans should do the following:

- **Decide whether to make the <u>optional</u> change to raise the required beginning date age to 73 for all or some participants who turn 72 after December 31, 2022.** This would require a plan amendment and notice to participants. While there are technical issues for discussion if the plan begins required minimum distributions ("RMDs") for active employees while they are still working, these concerns don't apply for inactive participants. Even without a change, the explanation of the excise tax in participant notices regarding RMDs will need to be updated to inform participants that the penalty for failure to take RMDs has been decreased from 50% to 25% of the required amount not distributed.

- **Determine whether changes are needed to the plan's overpayment policies** to comply with new limitations on the plan's overpayment recovery process, effective as of December 29, 2022.

- **Decide whether to Increase Plan's Involuntary Cash-out Limit**: The Act increases the maximum amount that can be distributed without participant or spousal consent from $5,000 to $7,000 effective for distributions beginning in 2024.

- **Review information collected for the Department of Labor's (DOL) "Lost and Found" registry**: The DOL is required to establish a new retirement lost and found website by 2025 for participants to search for lost retirement assets and plans will be required to report information for the lost and found. Additional guidance from the DOL is expected regarding the manner and format of reporting. In the meantime, plans should begin confirming that the plan is collecting the necessary information.

- **Update the Fund's Annual Funding Notice:** While a DOL model is expected to be issued, in the meantime, plans should begin confirming that the necessary information described below, currently is being collected, beginning with the 2024 plan year.

Summary

- **Required Minimum Distributions ("RMDs")**. The SECURE 2.0 Act delays the required beginning date by which minimum benefit payments in the form of RMDs must commence by increasing the age from age 72 to 73 for participants who turn 72 after December 31, 2022, and from age 73 to 75 for participants who reach age 74 after December 31, 2032. In addition, the SECURE 2.0 Act permits a surviving spouse to elect to be treated as if the spouse were the participant for the purpose of determining the amount and required beginning date of RMDs. Effective for taxable years beginning after December 29, 2022, the Act decreases the excise tax on participants for failure to take RMDs from 50% to 25%, and to 10% if the failure is remedied within two years. This may require changes to participant notices regarding RMDs.

- **Discretionary Recovery of Retirement Plan Overpayments.** Current law generally requires that fiduciaries attempt to recoup inadvertent overpayments as part of their fiduciary duties. Under the Act, pension plan fiduciaries are not required to attempt to recover overpayments, as long as the plan has established procedures to prevent and minimize the overpayment of benefits and such procedures have been followed. Additionally, the Act places restrictions on pension plans' ability to recoup overpayments from participants and beneficiaries. For example, pension plans cannot recoup overpayments made to deceased participants from their beneficiaries, collect interest on overpayments, reduce payments by more than 10% of the amount of the overpayment per year, or recoup any amount if the first overpayment was made more than three years before the participant is first notified of the overpayment, unless the participant or beneficiary made a misrepresentation that led to the overpayment or knew the amount was materially in excess of the correct amount.

- **Increases Involuntary Cash-out Limit**: The Act increases the maximum amount that can be distributed without participant or spousal consent from $5,000 to $7,000 effective for distributions beginning in 2024. However, since the requirement to provide a rollover for any distributions above $1,000 remains unchanged, these additional amounts still would need to be rolled over to an IRA established by the plan.

- **"Lost and Found" Registry Information.** The Act establishes a retirement savings "lost and found" database to be created by the DOL by 2025, which will allow participants and beneficiaries to search for plans under which they may have a benefit. Beginning in 2025, plan administrators must submit information for the registry to the DOL.

- **Annual Funding Notice.** The Act requires single employer and multiemployer defined benefit plans to include additional information on the annual funding notice due 120 days after the end of each plan year, effective for plan years beginning after December 31, 2023.

- **Reporting and Disclosure**. The Act requires that, unless the plan is following existing electronic disclosure rules, or the participant has elected otherwise, defined benefit plans must send all participants at least one pension benefit statement in paper form every three years.

- **Expansion of the EPCRS**. The SECURE 2.0 Act expands the Employee Plans Compliance Resolution System ("EPCRS") to allow more types of errors to be self-corrected, including certain plan amendment errors.

- **Plan Amendments**. The Act requires plans to adopt plan amendments incorporating the provisions of the Act before the end of the first plan year starting in 2025, or the first plan year starting in 2027 for collectively bargained plans. Plans must operate in accordance with the provisions of the Act as of the applicable effective date.

Analysis

Provisions Affecting all Retirement Plans

1. **Required Minimum Distributions:** The SECURE 2.0 Act makes a number of significant changes to the RMD rules.

A. Required Beginning Date As background, the definition of "required beginning date" under the Internal Revenue Code ("Code") has changed several times over the years. Generally, prior to 1999, the Code required that qualified plans commence distributions no later than the April 1 following the calendar year in which the participant reaches age 70½, regardless of whether the participant kept working. In 1999, the Code was amended to require qualified plan benefits to begin no later than the April 1 following the later of the calendar year in which (1) the participant reaches age 70½; or (2) retires. At the time of those changes, plans were permitted to retain the pre-1999 rule and many plans did so. As a result, some plans have required distributions to commence at age 70½ even if the participant still is working, while other plans have allowed participants to delay distributions until they retire. More recently, as described in our February 21, 2020 memorandum, the SECURE Act of 2019 increased the maximum age for determining a participant's required beginning date from 70½ to age 72.

Effective for individuals who reach age 72 after December 31, 2022, the SECURE 2.0 Act increases the maximum age for determining a participant's required beginning date from age 72 to age 73. For individuals who reach age 74 after December 31, 2032, the Act further increases the applicable age to 75. However, individuals born in 1959 will fall into both categories, attaining age 73 in 2032, and age 74 in 2033. While not an urgent concern, an amendment or technical correction on this point is expected.

Like the RMD provisions of the SECURE Act of 2019, the corresponding provisions of the SECURE 2.0 Act appear to be optional for plans. Therefore, it appears that plans wishing to continue using age 70½ or 72 are permitted to do so. However, plans that retain a required beginning date based on an age other than the maximum age set by the Internal Revenue Code should review the plan procedures regarding eligible rollover distributions. Specifically, any payments made under the plan's required beginning date rule that precede the required beginning date as defined in the Code (for example, under a plan that retains age 70½) are treated as eligible rollover distributions, including mandatory 20% withholding and the provision of a rollover notice.

Because the Act specifies that this change applies to participants who reach age 72 after December 31, 2022, plans should continue to apply their existing rule to participants who reach age 72 on or before December 31, 2022 (with payment required by April 1, 2023). Plans that adopt a change to their required beginning date should review their plan document, summary plan description, distribution notices and forms for necessary changes.

B. Reduction in the Excise Tax for RMD Failure: Effective January 1, 2023, the Act decreases the excise tax on participants for failure to take RMDs under the Code from 50% of the required amount not distributed to 25%. The amount of the excise tax is further decreased to 10% if the failure is remedied within two years of the RMD not being distributed. This may require changes to participant notices regarding RMDs.

C. Surviving Spouse May Elect to Be Treated as the Participant Effective for taxable years after 2023, the Act permits a surviving spouse to elect to be treated as if the spouse were the employee for the purposes of RMDs. This rule provides surviving spouses greater flexibility in deciding how and when to take RMDs. Consequently, a surviving spouse may delay the payment of RMDs if the participant was younger than the surviving spouse by using the participant's age, rather than the spouse's age, for the RMD date. Beneficiaries are still required to take RMDs after the participant's death.

2. **Recovery of Overpayments**: As of December 29, 2022, the Act provides relief for retirement plans from the general requirement to recoup inadvertent benefit overpayments. Under the law in effect prior to the Act, when plans inadvertently overpay benefits to a participant or beneficiary, fiduciaries are required, consistent with their duties under the Employee Retirement Income Security Act ("ERISA"), to take reasonable measures to recoup the amount of the overpayment. In doing so, the plan may incur legal and administrative costs and needed to balance these costs against the amount of the overpayment and whether recovery is likely.

The Act amends ERISA and the Code to provide that retirement plan fiduciaries do not violate their fiduciary duties and plans do not lose qualified status merely because they determine not to seek recovery of an overpayment, provided that the plan has established prudent procedures to prevent and minimize overpayment of benefits and such procedures have been followed with respect to the overpayment. The changes regarding overpayments apply only to retirement plans, therefore health plans and other welfare plans are not affected and presumably can continue to collect overpayments under existing law. In determining whether to seek of recoupment or how much to recoup, plan fiduciaries may take into account the hardship that recoupment would likely impose on the participant or beneficiary.

Participants who are notified of a benefit overpayment and who repay the overpaid amount to the plan are permitted to treat the repaid amount as a contribution of an eligible rollover distribution to the plan and the plan is treated as permitting such a transfer. This appears to mean that a plan is required to accept the return of the overpaid amount. The Act never states, however, that the repayment must be tracked or otherwise treated as a rollover distribution. Therefore, it appears that the purpose of the provision is to make the amount repaid not treated as taxable income to the participant. Guidance on this issue would be helpful.

Under the Act, pension plans that do pursue recoupment of a benefit overpayment after December 29, 2022, are subject to the following restrictions:

- No interest or additional amounts may be sought on overpayments being recouped for any period.
- With respect to benefit overpayments made in the form of an annuity, the amount recouped by offset of future benefit payments each calendar year must not exceed 10% of the total amount of the overpayment, and the participant's future benefits payments must not be reduced below 90% of the correct amount.
- Efforts to recoup overpayments may not be made through a collection agency, or similar third party, unless the participant or beneficiary ignores or rejects efforts to recoup the overpayment following either a final judgment in Federal or State court or a settlement between the participant or beneficiary and the plan authorizing such recoupment. Fund counsel does not appear to be "similar to a collection agency" and the reference to obtaining judgment in court suggests that plans could still have counsel pursue overpayments, provided the other requirements are followed, although guidance would be helpful on this.
- Demands for repayment may not include threats of litigation, unless the plan fiduciary determines that such litigation is likely to recover an amount greater than the cost of recovery.
- A plan may not seek recovery of past overpayments made to a participant from any beneficiary of the participant, including a spouse, surviving spouse, former spouse, or other beneficiary. This appears to mean that if a participant was overpaid, and the spouse receives benefits through a joint and survivor annuity, the plan could not recoup such overpayments from the surviving spouse. Guidance on this issue would be helpful.
- No recoupment may be sought if the earliest overpayment occurred more than three years before the participant or beneficiary is first notified in writing of the error, except in the case of fraud or misrepresentation by the participant. This appears to mean that a plan cannot recoup at all if the mistake is not identified and the recipient notified within three years of the first payment that is overpaid.

None of these restrictions apply in situations where the participant or beneficiary is "culpable," such as where their misrepresentations or omissions led to the overpayment, or if they knew that the overpayments were materially in excess of the correct amount. However, the Act provides that an individual is not culpable simply because he or she asked an authorized plan representative whether the payment was the correct amount and the plan representative advises that the payment was correct. Affected participants and beneficiaries are entitled to contest all or part of the recoupment under the plan's claims and appeals procedures and the plan's appeal procedures should be included in the plan letter seeking recoupment.

With respect to overpayments that occurred before December 29, 2022, the Act provides that plan fiduciaries are entitled to rely on a reasonable, good faith interpretation of then-existing guidance. In addition, fiduciaries are not required to reevaluate prior determinations not to pursue all or part of an overpayment. Any installment payments to repay an overpayment and any offset of future benefits that began before December 29, 2022 may continue. However, it is not clear whether or how this applies to recovery efforts that began before December 29, 2022 but did not progress to actual recovery (by installment payments or offset).

3. **Expansion of the Employee Plans Compliance Resolution System ("EPCRS")**: The IRS's EPCRS helps keep qualified retirement plans compliant with Code requirements by allowing plan sponsors to correct plan errors as soon as they are detected. Under the current EPCRS, certain failures can be self-corrected by the plan without notice to or approval by the IRS. (Failures that are not eligible for self-correction require plans to submit to a process with the IRS.)

The Act expands a plan's ability to self-correct failures by providing that there is no specific deadline to self-correct as long as a failure is not identified by the IRS before the plan takes actions that demonstrate its commitment to correct the error and the self-correction is completed within a reasonable period after the failure was identified. Under the current EPCRS, failures had to be identified and corrected within specified time periods, limiting the ability to self-correct many failures.

The Act also expands the kind of failures that can be self-corrected to include virtually any "eligible inadvertent failure", so as long as the plan has established practices and procedures reasonably designed to promote and facilitate overall compliance with applicable Code requirements. These procedures must be routinely followed, and the failure must have occurred through an oversight or mistake in applying them, or through a reasonable insufficiency in the procedures. Eligible inadvertent failures appear to include plan document failures, which previously were unavailable for self-correction in most cases, as well as operational failures. It is unclear whether the concept extends to plan demographic or eligibility failures, which traditionally have not been eligible for self-correction. The Secretary of the Treasury is directed within two years to issue revised guidance on the EPCRS in light of the Act, which may clarify these issues.

4. **Modified Reporting and Disclosure Requirements**: The Act makes changes to the way plans report information to participants. For defined benefit plans, effective for plan years beginning after December 31, 2025, unless the plan is following the DOL's existing electronic disclosure rules or a participant has elected otherwise, defined benefit plans must provide at least one pension benefit statement in paper form at least every three years. Currently, defined benefit plans can send either (1) an annual notice of the participant's right to request a paper statement, or (2) send a benefit statement every three years. However, the Act only references the benefit statement, which must be sent every three years. Therefore, the first option, to send participants an annual notice of their right to request a paper statement, appears to remain valid, but guidance to confirm that would be helpful. In addition, the Act requires the DOL to update the ERISA

electronic disclosure regulations by December 31, 2024 to include an option for plans to give initial paper notices to new plan participants and beneficiaries but to provide documents electronically after that. To take advantage of this, plans must provide participants and beneficiaries who become eligible to participate in the plan, or eligible for benefits under the plan, respectively, after December 31, 2025, with a one-time initial paper notice of their right to request that all documents required to be disclosed under Title I of ERISA be furnished on paper before giving further notices in electronic form.

5. **"Lost and Found" Registry**: The Act requires the DOL to establish a retirement savings "lost and found" database by 2025. This online database will allow participants and beneficiaries to search for the contact information for plans in which the participant or beneficiary may have a benefit. To facilitate this database, beginning in 2025, plan administrators will be required to submit the following information to the DOL:

- The name of the plan,
- The name and address of the plan administrator,
- Any change in the name of the plan,
- Any change in the name or address of the plan administrator, the termination of the plan, or the merger or consolidation of the plan with any other plan or its division into two or more plans,
- The name and taxpayer identification number of each participant in the plan -
    - who, during the plan year, separated from the service covered by the plan,
    - who is entitled to a deferred vested benefit under the plan as of the end of such plan year, and
    - with respect to whom retirement benefits were not paid under the plan during such plan year.
- The name and taxpayer identification number of each participant in the plan –
    - who, during the current plan year or any previous plan year, was a reported participant in the plan,
    - whose benefits were paid in full during the plan year, or
    - who had any amount distributed as an eligible rollover distribution, or
    - to whom a deferred annuity contract was distributed.
- The nature, amount, and form of the deferred vested benefit to which each participant is entitled, and
- Such other information as the Secretary may require.

The DOL is expected to issue guidance regarding the manner and format of these required reports.

6. **Increase in Cash-out Limit**: Currently, plans are permitted to distribute a participant's benefit without participant or spousal consent if the present value is between $1,000 and $5,000. Any present value over $1,000 can only be distributed in an automatic rollover to an IRA established by the plan in the participant's name, while a present value under $1,000 can be distributed directly to the participant. The Act increases the maximum amount that can be distributed without consent to $7,000 effective for distributions beginning in 2024. The requirement to provide an automatic rollover to an IRA for any distributions with a present value of more than $1,000 remains unchanged.

7. **Native American Tribal QDROs**: Starting after December 31, 2022, plans are required to recognize domestic relations orders (DROs) issued by tribal governments to the same extent as DROs issued by other courts. This includes any orders that are submitted for reconsideration after the effective date.

8. **Plan Amendments**: The Act requires plans to adopt plan amendments pursuant to the Act by the end of the 2025 plan year, or the end of the 2027 plan year for collectively bargained plans, as long as the plan operates in accordance with the amendments as of the effective date of the applicable requirement. The plan amendment dates of the SECURE Act, the CARES Act, and the Taxpayer Certainty and Disaster Tax Relief Act of 2020 have also been extended to these dates.

9. **Treasury Guidance on Rollovers**: By January 1, 2025, the Secretary must simplify, standardize, facilitate, and expedite the rollover process by developing and releasing sample forms for rollovers of eligible rollover distributions from employer-sponsored retirement plans to another such plan or IRA.

Provisions Affecting Only Defined Benefit Plans

10. **Revisions to Annual Funding Notice**: The Act amends the single employer and multiemployer annual funding notice requirements to include additional investment and participant information. Effective for plan years beginning after December 31, 2023 (the notice sent no later than 120 days after the end of the plan year to which the notice relates), plan administrators must provide the following additional information:

- The number of participants who are (a) retired or separated from service and receiving benefits, (b) retired or separated from service and entitled to future benefits, and (c) active under the plan for the two plan years preceding the plan year, in addition to the plan year to which the notice relates.

- Average return on assets for the plan year.

In addition to the items above, the Act also requires single employer plans to include the following in the annual funding notice:

- Instead of reporting the annual funding target attainment percentage, plans must report the percentage of plan liabilities funded, calculated as the ratio between the value of the plan's assets and liabilities, for the plan year to which the notice relates and for the two preceding plan years.

- A statement as to whether the percentage of plan liabilities funded for the plan year to which the notice relates is at least 100%, and if not, the actual percentage, including the plan's assets, liabilities, and funded status of the plan for the plan year to which the notice relates and for the two preceding plan years.

- A statement that if plan assets are determined to be sufficient to pay vested benefits that are not guaranteed by the PBGC, participants and beneficiaries may receive benefits in excess of the guaranteed amount, and that such a determination generally uses assumptions that result in a plan having a lower funded status compared to the disclosed funded status.

11. **Single Employer PBGC Premiums**: Single employer defined benefit plans are required to pay a variable rate premium to the Pension Benefit Guaranty Corporation (“PBGC”). Currently, this premium is $52 per $1,000 of unfunded benefits, indexed for inflation. As of December 29, 2022, the premium is no longer indexed, and is set permanently to the present rate.

Further guidance is expected on implementing many of these rules, and we will continue to monitor and advise you accordingly.

We look forward to discussing these issues with you.

cc: co-counsel (if any)

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