WELLS FARGO ADVISORS

The SECURE Act — Altering the Retirement Landscape

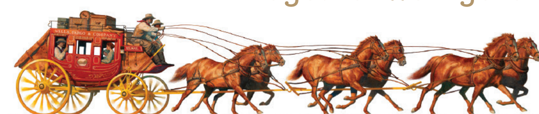
The Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019 (the "Act"), viewed by some as the most significant piece of retirement legislation in over a decade, was signed into law by President Trump on December 20, 2019. The Act is intended to promote retirement savings by making it easier and more cost effective for employers, particularly small employers, to start and maintain plans, and by giving more American workers access to retirement planning vehicles. It also encourages increased savings by incentivizing the adoption of automatic enrollment and escalation provisions in plans and encouraging workers to save for more years before accessing their retirement funds. Furthermore, the Act promotes the use of lifetime income options in qualified retirement plans (QRPs).

One controversial provision reduces the use of the stretch IRA strategy, which will require modified financial planning considerations.

The effective date of the Act is January 1, 2020; however, as we note in specific sections below, not all the provisions will become effective as of that date. The Act will be subject to significant interpretation and guidance from regulatory agencies and, as such, it is our recommendation that you work closely with your Financial Advisor, tax, and legal professionals.

The Act covers a wide variety of retirement topics. This paper highlights the changes that likely have the greatest impact on IRA owners, plan providers and participants, and is organized by broad topics for easy reference. As implementation of the Act's provisions move forward, and their impact becomes clear, you can expect further analysis from Wells Fargo Advisors on the most significant changes.

Together we'll go far



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Impacts Specific to Individual Retirement Accounts (IRAs)

Repeals Age Limit on Traditional IRA Contribution Eligibility (Sec. 107)

Prior to the Act—the law did not permit Traditional IRA owners to make contributions for the year they turn age 70½ and beyond.

The Act—repeals the age limit and permits Traditional IRA owners to make contributions past age 70½ so long as the individual has earned income at least equal to the contribution. Individuals can continue to save even if they are simultaneously taking RMDs from their Traditional IRAs.

Roth IRA contributions have never been subject to an age limitation. The Act does not affect Roth IRA contribution eligibility.

Effective: This applies to Traditional IRA contributions made for taxable years beginning after December 31, 2019.

Reduces Use of the Stretch IRA Strategy (Sec. 401)

Prior to the Act—RMD rules for an inherited IRA generally permitted a designated beneficiary to distribute the remaining account balance over that beneficiary's own life expectancy. This option allowed beneficiaries to stretch out their inherited IRA over their life expectancy, which potentially reduced their annual tax liability and allowed investments to continue their tax advantaged growth potential. The stretch IRA strategy has been an important financial planning approach for some investors.

The Act—greatly reduces the stretch IRA strategy by requiring beneficiaries to distribute all assets in the inherited IRA by the end of the 10th calendar year following the year of the account owner's death. The Act does not require any withdrawals during the first nine years; rather, it only requires that the account be emptied by the end of 10th year after the year of the owner's death. Exceptions are provided to certain eligible beneficiaries such as: surviving spouses; disabled or chronically ill individuals; children who have not reached the age of majority; and those who are less than 10 years younger than the original account owner.

While proponents of this section argued that most inherited IRAs don't last more than 10 years, the stretch IRA strategy has been used as an accepted planning tool for many retirement savers. This provision will impact estate planning approaches for IRA owners who plan to leave their IRAs to their children as well as how beneficiaries manage the tax implications of their inherited IRAs.

This rule change also applies to defined contribution (DC) retirement plan beneficiaries.

Effective: This provision is effective with respect to QRP participants and IRA owners who die after 2019. Those who became beneficiaries due to a death in 2019 or earlier may continue to take RMDs as permitted under prior law.

Planning Tip: Account owners can use this opportunity to review beneficiary designations with their Financial Advisor and structure a legacy plan.

Impacts to Both IRAs and QRPs

Increases Required Minimum Distribution (RMD) Age (Sec. 114)

Prior to the Act—the law required qualified plan participants who are retired and Traditional, SEP, and SIMPLE IRA account owners to begin taking annual RMDs when they reach age 70½.

The Act—raises the RMD starting age to 72, which means individuals have until April 1st of the year following the year they turn age 72 to take their first RMD. This provides additional time for individuals to amass tax-deferred potential gains in their retirement accounts. This section also provides more time during "gap" years to execute larger and more tax-efficient Roth conversions. The Act still allows participants in a QRP who are still employed and less than a 5% owner to delay RMDs, if permitted in the plan document.

The Act does not change the eligibility age for Qualified Charitable Distributions (QCDs), which is still age 70½.

Effective: This section is effective for individuals turning 70½ after December 31, 2019. Individuals who reach age 70½ on or before December 31, 2019, must start and/or continue taking RMDs at age 70½.

Planning Tip: Individuals can use this opportunity to review their retirement income needs with their Financial Advisor and make sure they understand their RMD beginning date.

Creates Penalty-Free Distributions for Qualified Birth or Adoption Expenses (Sec. 113)

Prior to the Act—one generally must be 59½ years old to distribute funds from a qualified retirement plan or IRA without incurring a 10% early distribution tax, unless an exception applies. Exceptions to this rule for IRAs include distributions taken due to death of the IRA owner, eligible medical expenses greater than 10% of adjusted gross income, a disability, qualified first-time homebuyer, and qualified higher education expenses, to name a few. (Slightly different exceptions apply for qualified plan distributions.)

The Act—adds a new penalty exception to permit parents to withdraw up to $5,000 from an IRA or retirement plan for qualified birth and adoption expenses, for up to one year after birth or adoptions. An eligible adoptee means any individual, other than a child of the taxpayer's spouse, who has not attained age 18 or is physically or mentally incapable of self-support. Individuals may also recontribute the amount distributed for this reason to an eligible retirement plan or IRA. Individuals who exercise this option should be aware that it will reduce tax-deferred potential growth in their account if they are not able to repay the savings they withdrew.

Effective: This provision is effective for distributions made after December 31, 2019.

Impacts Specific to Qualified Retirement Plans

Incentives for Small Businesses to Start a Retirement Plan

Small businesses, those with 100 or fewer employees, are one of the largest and fastest growing employment sectors in the United States.[1] However, many small businesses don't offer retirement plans because of the cost, and many employees lack the access or knowledge to research savings alternatives. The following provisions make it easier for small businesses to sponsor a retirement plan by creating scale and reducing administrative costs. Some commentators estimate that this provision will add between 600,000 to 700,000 new retirement accounts.[2]

Expands Pooled MEPs (Sec. 101)

Prior to the Act—a Multiple Employer Plan (MEP) was a qualified retirement plan that could be adopted by multiple unrelated employers. The MEP structure was designed to reduce the fiduciary, administrative, and cost burden for participating employers. Employers generally had to have some commonality or relationship to participate in a single plan. Only 401(k) plans were allowed, and there were detailed compliance requirements for participating employers that could easily render the entire plan noncompliant. For example, a rule commonly referred to as the "one bad apple" rule states that if even one participating employer did not meet a compliance requirement, the IRS could deem the entire plan noncompliant.

The Act allows an Open MEP to be a single plan for all purposes for employers without any commonality.

The Act—aims to make it easier for employers to participate in MEPs by (1) allowing MEPs to be IRA-based plans, as well as 401(k)s, (2) removing the "one bad apple" plan disqualification where one or more employers are noncompliant, and (3) eliminating the commonality requirement to be considered one plan for all purposes. The Act creates open MEPs by eliminating the "commonality" requirement and establishing a new type of MEP called a "Pooled Employer Plan" (PEP), which must be sponsored by a "pooled plan provider" (PPP). To have a PEP, the only commonality that is required between employers is the plan itself. The plan provider must register as a PPP with the Secretary of Treasury and be designated by the PEP as its named fiduciary, ERISA Section 3(16) plan administrator, and person responsible to perform all administrative duties. (Section 202 of the Act provides that when a PEP is properly created, that plan can file a consolidated Form 5500 return, which will further reduce administrative costs.) Each employer participating in a PEP retains responsibility for selecting and monitoring the PPP. There are also provisions addressing noncompliant employers, including a method for withdrawal by noncompliant employers from the PEP.

Effective: This provision applies to plan years beginning after December 31, 2020.

Planning Tip: Employers may want to use this opportunity to consult with a Financial Advisor to evaluate the benefits and considerations of implementing a retirement plan for their business, including whether a PEP may be an option and whether the small employer start-up cost tax credit under section 104 is available for their business.

Extends Deadline to Establish Qualified Retirement Plan (Sec. 201)

Prior to the Act—the deadline to establish a retirement plan for a tax year was the last day of the business year (typically December 31).

The Act—extends the deadline to establish a retirement plan until the business's tax-filing deadline, plus extensions. This means that a sole proprietor may have until October 15, 2021, to establish and fund a retirement plan for tax year 2020.

Elective salary deferrals may not be made retroactively.

Effective: This section applies to taxable years beginning after December 31, 2019.

Increases Small Employer Start-Up Cost Tax Credits (Sec. 104)

Prior to the Act—under current regulations, small businesses are eligible to receive a $500 tax credit for starting a new retirement plan.

The Act—increases the credit to up to $5,000 per year, depending on the number and type of employees, and extends the receipt of the credit for three years. As such, an employer might receive a maximum credit of $15,000 over three years.

Effective: This section applies to taxable years beginning after December 31, 2019.

Incentives to Increase Tax Savings and Access to Plans

The following provisions of the Act aim to promote increased tax-deferred retirement savings by incentivizing employers and giving them more flexibility to adopt plan provisions that allow both employers and employees to put more money into eligible employees' retirement savings accounts. These provisions also expand access to retirement vehicles for a broader class of employees and allow savers more years to grow tax-deferred savings before they must begin taking Required Minimum Distributions (RMDs). People are living and working longer, so encouraging more savings and allowing longer periods of time to amass tax-free investments is critical to helping people avoid outliving their retirement funds.

Increases Automatic Escalation Cap for Employee Deferrals (Sec. 102)

Prior to the Act—before passage of the Act, an automatic enrollment safe harbor plan could not permit automatic escalation of employee salary deferrals past 10% of compensation.

The Act—raises the cap on automatic contribution increases from 10% to 15% of compensation after the first year of participation. As with the current regulations, the Act requires eligible plans to provide matching contributions, while maintaining the flexibility for employees to choose a different rate.

Effective: This section applies to plan years beginning after December 31, 2019.

Eases Safe Harbor 401(k) Election Rules (Sec. 103)

Prior to the Act—when converting from a traditional 401(k) to a safe harbor, to satisfy the nondiscrimination testing rules, an employer must amend an existing plan before the end of the plan year to add a minimum 3% nonelective contribution for the following plan year. An annual notice must be provided to eligible employees at least 30 days prior to the beginning of the new plan year.

The Act—eliminates the notice requirement and gives employers the flexibility to switch to a nonelective safe harbor 401(k) arrangement in the middle of a plan year. The Act permits amendments to nonelective status at any time prior to the 30th day before the close of the plan year if a 3% nonelective contribution for eligible participants is made. And, it expands the amendment deadline to as late as the close of the following plan year provided the employer makes a 4% nonelective contribution for eligible participants. The Act also maintains the current requirement to allow employees to make or change an election at least one time per year.

Effective: This section applies to plan years beginning after December 31, 2019.

Creates Automatic Enrollment Tax Credit (Sec. 105)

The Act—provides a new $500 per year tax credit for up to three years for start-up costs for small employers (100 or fewer employees) that establish a 401(k) or SIMPLE IRA retirement plan that automatically enrolls eligible employees. This credit is in addition to the small plan start-up tax credit. Participants can choose to opt out of such automatic enrollment.

This credit is available to employers that set up a new plan as well as to those that add automatic enrollment to an existing plan.

Effective: This section applies to taxable years beginning after December 31, 2019.

Planning Tip: Small business employers who sponsor a plan or who are considering sponsoring a plan should consult with their Financial Advisor about whether adding an automatic enrollment feature to a new or existing plan is right for their business and their employees.

Provides Retirement Plan Access to Part-Time Workers (Sec. 112)

Prior to the Act—part-time employees who didn't work at least 1,000 hours per year could be excluded from participating in an employer's retirement plan.

The Act—permits employees to participate in the plan if they have completed one year of service with at least 1,000 hours worked and adds a new eligible class of employees for those who have completed three consecutive years of service with at least 500 hours each year. The Act allows employers to exclude this new eligible class of employees for nondiscrimination and top-heavy testing purposes, and it does not require employers to make matching or other employer contributions for this new eligible class. This provision does not apply to collectively bargained plans. The Act specifically notes that women are more likely than men to work part-time, so this provision should directly benefit them.

Effective: This provision is effective for plan years beginning after December 31, 2020, except that for purposes of the new eligible class, the 12-month periods beginning before January 1, 2021, are not to be considered.

Planning Tip: Plan sponsors should work with their third-party administrators to develop procedures to track the hours of part-time employees to determine whether part-time employees have met the 500-hours-per-year threshold each year.

Promotion of Lifetime Income

Prior to the Act—retirement planning for American workers has traditionally focused on the accumulation of retirement assets, with less attention paid to how workers can use their savings to create income to last throughout their lifetime after retiring. Historically, including lifetime income investment options in a Defined Contribution (DC) retirement plan has been viewed as too complex, expensive, and risky for plan fiduciaries, which has limited the use of lifetime income products in retirement plans. For example, under current law, if a participant switches plans, or a lifetime income option is no longer authorized to be held as an investment option, it is almost impossible for participants to preserve these options and avoid surrender charges and fees. The following provisions make the selection of providers and use of lifetime income vehicles easier and less risky, which should incentivize employers to include them as options to assist employees in managing their retirement income needs.

Adds Lifetime Income Portability (Sec. 109)

The Act—provides that if a participant leaves their job or if their lifetime income option is no longer authorized to be held under a covered plan (e.g., the plan sponsor eliminates it as an option) they can transfer that investment to another retirement plan or IRA without surrender charges or fees.

Effective: This provision applies to plans effective for plan years beginning after December 31, 2019.

Requires Lifetime Income Disclosures (Sec. 203)

The Act—creates a requirement for DC retirement plans to deliver lifetime income disclosures to participants at least once every 12 months. Today, retirement plan statements provide an account balance, but no indication of how long the participant's account balance will last or the amount of income that may be generated in retirement.

The new disclosures will include an estimate of the monthly amount a participant could receive as a single or joint life annuitant in retirement, based on the participant's total current account balance. The Act requires the Department of Labor (DOL) to provide the assumptions plans can use to create the projections and issue a model disclosure. Importantly, the Act ensures that employers are not liable for lifetime income estimates derived in accordance with the assumptions, guidance, or model disclosure. While this provision will require additional paperwork from administrators and plan sponsors, including developing a disclosure template and documenting compliance, it will give participants greater perspective on how their savings could translate to monthly income in retirement, as well as time to adjust their savings rates if needed to better prepare for their retirement income needs.

Effective: This provision applies to statements furnished 12 months after the later of the DOL issuing interim final rules, model disclosures, or assumptions.

Planning Tip: Plan sponsors should monitor DOL regulations and work with their third-party administrator (TPA) and legal counsel to craft a compliant lifetime income disclosure. Plan participants should use this opportunity to review their retirement income needs with their Financial Advisors.

Expands Lifetime Income Selection Safe Harbor (Sec. 204)

The Act—provides plan fiduciaries with an optional safe harbor to satisfy the prudence requirement when selecting insurers for guaranteed retirement income contracts and shields plan fiduciaries from liability for any losses that may result due to an insurer's inability to satisfy its financial obligations. Importantly, there is no requirement to select the lowest cost option, but fiduciaries must determine if an insurance contract is appropriate and the fees reasonable. To meet their fiduciary requirements, plan sponsors should choose an annuity provider that's in good standing with state regulators.

Effective: This section applies to existing plans as of the Act's effective date, January 1, 2020.

Impacts Specific to 529 Plans

Expands 529 Plan Qualified Expenses (Sec. 302)

Prior to the Act—529 education plan assets may have been used tax- and penalty-free to pay for tuition, fees, books, supplies, equipment, and qualified room and board at an accredited college, university, or vocational school, as well as up to $10,000 for tuition at an elementary, secondary, or religious school.

The Act—expands the use of plan assets to cover the costs of (1) qualified student loan repayments (up to $10,000 lifetime, not annual), including those for siblings, and (2) registered apprenticeships.

Effective: This section applies to distributions made after December 31, 2018.

Next Steps

Many of the changes made by the Act will have far-reaching effects on employers, employees, IRA owners, service providers, and the retirement plan industry. Despite the very short lead time to the effective date for many of these provisions, some of these changes are complex and require additional analysis before all potential ramifications can be identified. The IRS and the DOL will likely release regulatory guidance to help plan sponsors and service providers fully implement changes and individual account owners fully understand the impact on their savings objectives.

In the meantime, individuals and business owners can use this window of change as an opportunity to conduct a thorough review of all retirement and savings plans to make sure they are utilizing the benefits available and preparing for the rule changes. For more information on the specific changes as time passes and the details become clearer, contact your Financial Advisor at Wells Fargo Advisors.

SECURE ACT To-Do List	
IRA owners and Plan Participants	• Review the beneficiaries named on your retirement savings accounts and seek advice on how the SECURE Act will affect your beneficiary planning. • If you are nearing retirement or the age at which you must begin taking distributions from your retirement savings, review your retirement income needs and be sure you understand when you must begin taking RMDs.
Business owners without a retirement plan	• Consult with your Financial Advisor about the retirement plan opportunities available to your business through the Act and consider implementing a retirement plan for your employees. • You now have an extended time to analyze your options as you have until your tax return deadline to establish a plan for the year (beginning for tax year 2020). • For small business plans, extra tax credits are available to help with plan start-up costs and as an incentive to automatically enroll eligible employees into the plan.
Plan Sponsors	• Consider whether adding an automatic enrollment feature might be beneficial to your existing plan. If you are a small employer, you have a tax credit available to help offset the costs of adding the new feature. • Discuss with your Financial Advisor the benefits of being in a safe harbor 401(k) plan. You now have additional time to add the safe harbor feature if you provide nonelective contributions. • After the DOL issues regulations or a model notice, work with your Financial Advisor and plan providers to construct a compliant lifetime income disclosure for your participants.

[1] U.S. Small Business Administration Office of Advocacy, 2018 Small Business Profile, https://www.sba.gov/sites/default/files/advocacy/2018-Small-Business-Profiles-US.pdf
[2] Rep. Richard Neal (D-MA), Neal Opening Statement at Markup of Retirement, Tax Administration, and Reemployment Services Legislation, April 2, 2019, https://neal.house.gov/press-releases/neal-opening-statement-markup-retirement-tax-administration-and-reemployment-services

Wells Fargo Advisors is not a tax or legal advisor. Although this summary is not intended to replace discussions with your tax and legal advisors, it may help you to comprehend the tax implications of your investments and plan efficiently going forward.

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