

INVESTMENTS & WEALTH MONITOR

A reprinted article from September/October 2023

Highlights of the SECURE 2.0 Act

By Tim Steffen, CPA/PFS, CFP®, CPWA®



INVESTMENTS & WEALTH INSTITUTE®

Highlights of the SECURE 2.0 Act

By Tim Steffen, CPA/PFS, CFP®, CPWA®

When Congress passed the original version of the Setting Every Community Up for Retirement Enhancement (SECURE) Act in late 2019, the primary focus was to expand access to retirement accounts for employers and employees alike. And although the bill took several steps forward in that area, almost immediately after its passage work began on a follow-up to the bill, which quickly became known as SECURE 2.0. Shortly afterward, however, Congress had to deal with the implications of a worldwide pandemic, an economic meltdown, and a variety of social crises, not to mention a presidential campaign and competing legislation such as the Build Back Better bill. As a result, supporters of the SECURE 2.0 Act had to bide their time until its provisions found their way into a year-end spending bill in late 2022.

The road to enactment for SECURE 2.0 was very similar to its predecessor's, but the content and its impact are likely to be much different. Beyond all the changes to retirement plan access, the original bill included a massive change in the way beneficiaries of inherited retirement accounts access their funds by virtually eliminating the old stretch rules and replacing them with a new "10-year rule." The 2.0 version doesn't include anything as significant as that change, but it does have a few items that will provide important planning opportunities for advisors. In addition, most individual taxpayers are likely to be impacted by one or more of its many other provisions. In fact, in terms of the number of provisions, 2.0 is much larger than the original.

... Congress had to deal with the implications of a worldwide pandemic, an economic meltdown, and a variety of social crises, not to mention a presidential campaign and competing legislation such as the Build Back Better bill.

Despite the sheer volume of provisions in SECURE 2.0, however, there was one topic advisors were hoping would be addressed in this bill that was left out. The 10-year rule provision in the original SECURE Act left some ambiguity about how the rule would be applied in some cases, and subsequent pronouncements from the Internal Revenue Service (IRS) since then have only created more confusion. The hope was that 2.0 would provide the clarity advisors and beneficiaries have been looking for, but that clarity didn't come, leaving advisors to deal with proposed regulations and hope for more clarity in the future.

Following is a summary of the key provisions in the SECURE 2.0 Act.

INCREASE IN THE REQUIRED MINIMUM DISTRIBUTION (RMD) AGE

Building on a key part of the original SECURE Act, this bill again changed the age at which retirement account owners must begin taking withdrawals from

those accounts. Just a few years ago RMDs began at age 70½, and for 2020–2022 it was age 72; starting in 2023, those forced distributions can be delayed until the year the account owner turns 73. Therefore, account owners who turn 72 in 2023 will receive a one-year reprieve from having to take a distribution. Conversely, IRA owners who turn 73 this year would have turned 72 in 2022, and therefore already were subject to RMDs last year. As a result, there won't be any "new" RMD takers from IRAs this year.

Because this update was enacted late in 2022, it's possible some individuals turning 72 in 2023 mistakenly thought they were subject to RMDs this year and took a distribution they were not required to take. To help those individuals, IRS Notice 2023-54 (issued in July 2023) provides an extension to the normal 60-day rollover window, subject to limitations:

- This only applies to IRA owners born in 1951 (who would have turned 72 in 2023) or their surviving spouses.
- Only withdrawals from January 1, 2023, through July 31, 2023, are eligible for the rollover extension.
- This extension applies only to distributions that would have been RMDs had the starting age not changed to 73. Presumably, any withdrawals beyond the RMD amount are not eligible for this extension.
- The deadline for this extended rollover is September 30, 2023.
- This rollover opportunity is available even if the account owner or surviving spouse had already completed a

60-day rollover during the prior 12 months. However, taking advantage of this opportunity will preclude a second 60-day rollover in the following 12 months.

In addition, there will be a further extension of this RMD age to 75 in the future. A drafting error in the bill led to some confusion around the age-75 implementation, with it appearing that RMDs actually could begin at age 74. However, in May Congress notified the Treasury Department that a technical corrections bill will be introduced to clear up this confusion. Congress's intent was to have the age-75 rule apply to those who turn 73 in 2033, meaning this new rule will first apply in 2035 (see table 1).

As when the RMD originally was extended to 72, these extensions to 73 and 75 do not impact any of the other rules related to RMDs:

- The first distribution from a plan can be delayed to April 1 of the year after being subject to RMDs. All subsequent RMDs are due by December 31 of the applicable year.
- The “still working” exception allows RMDs from employer plans to be further deferred until the year of retirement. This exception does not apply to IRAs, however.
- Qualified charitable distributions can still be made from an IRA after the owner turns age 70½.

This RMD delay will further expand the “trough period” for retirees—that period of time between the end of their working years and the beginning of forced IRA distributions. During this window, retirees often have complete control over the source and amount of their income, which can allow them to take advantage of unique planning opportunities. For example, maybe this window of time when income is low could be ideal for taking advantage of the 0-percent tax rate on long-term capital gains. For 2023, this 0-percent rate

Table 1

RMD STARTING AGE BASED ON BIRTHDATE

Birthdate	Age
Before July 1, 1949	70½
July 1, 1949–December 31, 1950	72
January 1, 1950–December 31, 1959	73
January 1, 1960, or later	75

applies to married couples with taxable income below \$89,250 (singles below \$44,625).

Another option would be to do a Roth conversion. The trough period can be an ideal time to withdraw IRA funds at a perhaps temporarily lower tax cost, and then move those funds into a Roth IRA where they can serve as a source of tax-free income later in life. Roth accounts are not subject to RMDs, meaning those dollars can be left in the account past the owner's death and go to the heirs free of income tax.

529 PLAN ROLLOVER TO ROTH IRA

The 529 plan account has been a popular way to save for college education for many years, but one concern among some savers is what to do with money left in the account after a student finishes school. Tax laws allow for transfers to siblings, or to use the funds for adult education courses later in life, but withdrawals for non-education purposes can trigger a tax penalty. Now, Congress is offering another use for those excess funds; and although it's a welcome change, the details of the new rule will stifle the excitement somewhat.

Beginning in 2024, funds in a 529 account can be rolled into a Roth IRA, subject to several limitations:

- The Roth must be opened for the same person who was the beneficiary of the 529 plan. Parents shouldn't necessarily view this as a way to reclaim funds that were set aside for a child.
- The maximum annual rollover amount is limited to the Roth contribution

limit for that year, reduced by any other direct Roth contributions. For 2023, that limit would be \$6,500.

- To be eligible for the rollover, the recipient must otherwise be eligible for a Roth contribution, meaning they must have compensation income. However, the maximum income limitation that prevents higher-income individuals from making a direct Roth contribution does not apply to these rollovers.
- There is maximum lifetime rollover of \$35,000.

Maybe most significantly, the 529 plan must have been open for at least 15 years as of the date of the rollover, and any amount contributed to the account within five years of the rollover is ineligible. This means that in order to do a rollover on July 1, 2024, for example, the 529 plan must have been established before July 1, 2009, and any contributions since July 1, 2019, can't be rolled. In other words, individuals can't begin loading up 529 plans now with the hopes of rolling those to a Roth IRA next year. Any contributions made in 2023 would have to wait until at least 2028 to be rolled, and to 2038 if the 529 is just opened this year.

One area of uncertainty has to do with changing the beneficiary on an existing 529. Say a parent has a 529 that meets the requirement for a rollover next year, but the value exceeds the \$35,000-lifetime conversion maximum. One thought is to change the beneficiary on the remaining balance of the account to someone else, who would have their own \$35,000 limit. But it's unknown if changing a beneficiary triggers a new 15-year clock. IRS guidance will be needed before we know the validity of this strategy.

ENHANCED QUALIFIED CHARITABLE DISTRIBUTION RULES

As mentioned in the RMD discussion, the age at which an IRA owner can make a qualified charitable distribution (QCD) remains 70½, but there were other changes made to these rules. For

example, the annual QCD limit of \$100,000, which has been in place since QCDs were first introduced in 2006, will finally be adjusted for inflation beginning in 2024.

More meaningfully, donors are now able to make these gifts to “split interest” entities, in particular charitable remainder trusts (CRTs) and charitable gift annuities (CGAs). As with rolling a 529 to a Roth, though, the details of the rules make this strategy less attractive than planners might think:

- These gifts are subject to a lifetime maximum of \$50,000 per donor and can be done only one time. In other words, if someone makes a transfer of just \$30,000 from an IRA to a CRT or CGA, the ability to ever transfer the remaining \$20,000 is gone. The limit will be adjusted annually for inflation, but once someone has made the gift, future inflation adjustments are irrelevant.
- The gift from the IRA to the CRT or CGA can be the only gift into that account—no other contributions are allowed. Spouses can combine their gifts into one account, but the maximum combined contribution can't exceed \$100,000. That might be acceptable for the CGA option, but it seems unlikely that someone will create a CRT knowing it can receive a gift of only up to \$100,000.
- The donor also must be the income beneficiary of either the CRT or CGA. For the annuity option, payments must be at least 5 percent of the principal and must begin within one year of its funding.
- All payments from the account to the income beneficiary are taxed as ordinary income.

These restrictions may limit the appeal of these new QCD options; however, donors can at least view this as a crack in the door to perhaps further expansion of QCDs in the future. Allowing donor-advised funds to receive these

gifts may be too much to hope for, but increases to the gift amount or changing the eligibility age could be more realistic future enhancements.

PLAN CATCH-UP CONTRIBUTION CHANGES

The bill provides a new way for older workers nearing retirement to save additional funds in their employer plans. Current rules allow participants in 401(k) and 403(b) plans to contribute an additional \$7,500 (for 2023) beginning the year they reach age 50. Beginning in 2025, in the year a participant reaches ages 60 through 63, the catch-up will increase to the greater of \$10,000 or 150 percent of the age 50 catch-up amount. In the year the participant reaches 64, this enhanced catch-up goes away, although the base catch-up is still allowed.

These restrictions may limit the appeal of these new QCD options; however, donors can at least view this as a crack in the door to perhaps further expansion of QCDs in the future.

A similar catch-up enhancement will be available to participants in SIMPLE IRAs, with their catch-up amount increasing from \$3,500 (for 2023) to the greater of \$5,000 or 150 percent of the age-50 amount in 2025. The \$5,000 and \$10,000 amounts will be inflation-adjusted beginning in 2026.

No increases were made to the catch-up amount for traditional or Roth IRAs, although the current \$1,000 catch-up will be inflation-adjusted beginning in 2024.

One of the themes of SECURE 2.0 is “Rothification”—the idea that Congress

is encouraging, or even requiring, taxpayers to use Roth-style retirement accounts over traditional accounts. One example is the 529 rollover to Roth accounts discussed earlier; another applies to catch-up contributions.

The original language in the bill required that, beginning in 2024, “highly compensated” employees must make any catch-up contributions to the Roth-style account in their employer plans—meaning there will be no tax benefit in the year of the contribution but future qualified withdrawals will be tax-free. “Highly compensated” is defined as someone who earned more than \$145,000 in the prior calendar year from the same employer. This “same employer” rule means someone who changes employers during the year automatically will be exempt from this requirement for that year and possibly even for the next year depending on earnings in that first stub year.

There is a flip side to this, though. Employers who don't offer a Roth option won't have a way to accept catch-up contributions from these highly compensated employees. This bill says in those cases where some employees are not allowed to make catch-up contributions, then no employees are eligible to make them. Employers who don't currently offer a Roth option will want to revisit their plan designs before this rule takes effect next year. Because of concerns from plan sponsors and others over implementing this for 2024, the IRS announced in Notice 2023-62 a two-year “administrative transition” before mandating this rule. Plans will now be required to follow this provision by 2026.

ADDITIONAL ROTH CHANGES

SECURE 2.0 includes several other changes involving Roth plans. Although some of these changes are effective now, many plan custodians and employers are waiting for further guidance before offering these new features.

- Beginning in 2023, retirement plan custodians can offer Roth-style SEP and SIMPLE IRAs.
- Also in 2023, employers can amend their defined contribution plans to allow employees to designate an employer match to the plan to go to their plan's Roth accounts. These Roth contributions would be considered taxable income to the recipient, however, unlike matches that go to a traditional plan.
- Lastly, participants in Roth 401(k), Roth 403(b), and Roth 457(b) plans no longer will be subject to the RMD rules in 2024, bringing these plans in-line with Roth IRAs. This does not affect RMDs that were scheduled to be withdrawn for 2023, however.

CHANGES AFFECTING EMPLOYERS

In addition to creating new ways for individuals to save for retirement, SECURE 2.0 included a variety of changes affecting employers specifically. This includes expanded ways to add to employees' accounts, as well as entirely new savings vehicles. It could be argued that simpler rules around retirement savings would be more beneficial than more account types; regardless, employers should be aware of these options and how they fit into an employee benefits package.

Student loan matching payments. To support workers who are balancing saving for retirement with paying down student loans, employers can treat a qualified student loan payment made by the employee as a plan contribution when determining eligibility for a matching contribution. This provision, beginning in 2024, applies to participants in 401(k), 403(b), governmental 457, or SIMPLE IRA plans.

Additional employer contributions to SIMPLE IRAs. Beginning in 2024, employers can make a new, non-elective contribution to a SIMPLE plan for qualified employees of up to 10 percent of their income, with a maximum

NEW EXCEPTIONS TO 10-PERCENT EARLY WITHDRAWAL PENALTY

The SECURE 2.0 Act included several new exceptions to the 10-percent penalty for early withdrawals from a retirement plan, which are summarized below. Each of these penalty exceptions may be subject to specific limitations or other rules.

Effective Date*	Provision
December 2022	<ul style="list-style-type: none"> • Disaster-related withdrawals • Withdrawals by those diagnosed with a terminal illness • Withdrawals of earnings related to withdrawing an excess contribution
January 2024	<ul style="list-style-type: none"> • Withdrawals by a victim of domestic abuse • Withdrawals for emergency personal expenses • Splitting an IRA that is subject to a SOSEPP will not cause a penalty as long as the SOSEPP continues from both the old and new accounts.

* Effective date refers to tax years beginning on this date or later.

contribution of \$5,000 (adjusted for inflation in 2025). This is in addition to the regular contributions employers already are making.

Increased contribution limit for SIMPLE IRAs. For employers with no more than 25 employees, the annual salary deferral limit as well as the age-50 catch-up contribution amount is increased by 10 percent beginning in 2024. Employers with 26-100 employees also may offer these same higher deferral limits provided the employer makes either a 3-percent contribution or a 4-percent matching contribution (as opposed to the current 2-percent and 3-percent thresholds, respectively).

New starter 401(k) plan. Also beginning in 2024, a new "starter 401(k)" plan can be offered by employers who don't otherwise offer a retirement plan. This new plan would include an automatic deferral feature of 3-15 percent of earnings (although employees can opt out), with a maximum contribution of \$6,000, plus a \$1,000 catch-up option for those age 50 or older.

Pension-linked emergency savings account. Also in 2024, employers can offer a new pension-linked emergency

savings account, a short-term savings vehicle for eligible employees ("highly compensated" individuals are excluded from participating). Contributions to this Roth-style account are non-deductible, but earnings would be tax-free upon withdrawal. Employee contributions are allowed up to the point where the account balance reaches the maximum value allowed by the employer but no more than \$2,500, and contributions are to be invested in a way that preserves the principal of the account. Withdrawals from the account can occur at any time the employee requests.

CHANGES TO PENALTIES APPLICABLE TO RETIREMENT PLANS

Individuals who fail to withdraw the entire RMD from their plans have been subject to a 50-percent excise tax on the unwithdrawn amount. That tax is reduced to 25 percent immediately, and it is further reduced to 10 percent for those who make a corrective distribution within a specified period of time and who submit a tax return reflecting that 10-percent tax. The IRS generally has been lenient in waiving this penalty for taxpayers who show the shortfall was due to reasonable error and are taking steps to remedy it. Early signs indicate

the IRS will continue that policy despite the reduced penalty amount.

On the other hand, withdrawals from a retirement plan before age 59½ generally are subject to a 10-percent early withdrawal penalty, although several types of withdrawals are exempt from that penalty (see sidebar). One such exemption is the “series of substantially equal periodic payments,” or SOSEPP, which allows a plan participant to take specific withdrawal amounts for a minimum length of time and avoid the penalty. The SOSEPP rules are notoriously rigid, but this bill provides a bit of flexibility. Beginning in 2024, a rollover from a plan that is part of a SOSEPP to a new plan no longer constitutes a change in the withdrawal as long as the total withdrawal from the old and new plans is the same as what would have been taken from just the old plan.

... effective immediately, withdrawals of earnings attributable to excess contributions to a plan, when withdrawn before age 59½, are exempt from the early withdrawal penalty.

Other new penalty exceptions include the following:

- Beginning in 2024, victims of domestic abuse may withdraw the lesser of 50 percent of the account value or \$10,000 (adjusted for inflation) penalty-free. The withdrawal must occur within one year of the date the individual is a victim of abuse.
- Beginning immediately, an individual who is certified by a physician as having a terminal illness expected to result in death in 84 months or less may take a penalty-free early withdrawal from a qualified plan.

Documentation must be provided to the plan administrator and there is no limit on the size of the withdrawal.

- Beginning immediately, withdrawals of up to \$22,000 made within 180 days of a federally declared disaster (in an area that includes the recipient’s primary residence) are exempt from the 10-percent penalty. The taxable portion of any such distribution will be included in income ratably over three years, beginning with the year of the withdrawal, unless individuals choose to report it as fully taxable in the first year.
- Beginning in 2024, plan participants may take an early, penalty-free withdrawal to cover emergency personal expenses for themselves or their families. Withdrawals are limited to the lesser of \$1,000 or the plan balance over \$1,000.

Each of these four withdrawal types also can be repaid to the original plan within three years and be exempt from tax. The original SECURE Act created a similar payback option for qualified birth or adoption expenses, except that no deadline for repayment was ever established. Now, any such withdrawals made before SECURE 2.0 can be returned any time through 2025, and any new withdrawals are also subject to the three-year limit for repayment.

Lastly, effective immediately, withdrawals of earnings attributable to excess contributions to a plan, when withdrawn before age 59½, are exempt from the early withdrawal penalty.

LATEST ON INHERITED RETIREMENT ACCOUNTS

The SECURE 2.0 Act also contains many other provisions such as a revised saver’s tax credit, expanded eligibility for ABLE Accounts (tax-advantaged savings accounts for individuals with disabilities and their families), allowing S Corp owners to sell to an employee stock ownership plan (ESOP), limits on

conservation easements, and more. Not included, however, is any further clarification on the original SECURE Act’s 10-year rule for beneficiaries of inherited retirement accounts.

The IRS issued proposed regulations in February 2022 that said some, but not all, beneficiaries of these inherited accounts must take RMDs in each of the first nine years they own the account and requiring the account to be fully depleted in the 10th year. When these regulations were published, though, some beneficiaries already were well into their second year of ownership (when owners died in 2020), meaning many had likely missed their first RMD for 2021. In October 2022, the IRS issued Notice 2022-53 that said it would waive any penalties on missed RMDs in these cases for both 2021 and 2022—even though 2022 still had nearly three months to go.

That position left many wondering whether the IRS was ever going to finalize those rules or perhaps come up with something else entirely. In Notice 2023-54 (July 2023), the IRS further kicked the can down the road by waiving penalties on these missed RMDs for 2023 as well, choosing to delay any further action on these regulations until at least 2024. As of publication, the IRS has not issued any further updates. Proposed regulations are not binding until they’re finalized, but they do represent the IRS’s position on a topic. Affected beneficiaries should prepare—at a minimum—to take their RMDs for 2024 if the account owner died in 2020-2023. As for those beneficiary RMDs for years when the penalty was waived, it’s unknown how the IRS ultimately will handle those. Regardless, the 10-year rule seems here to stay, so taking withdrawals over each of those 10 years may prove to be a prudent tax management strategy.

Continued on page 51 →

HIGHLIGHTS OF THE SECURE 2.0 ACT

Continued from page 48

EFFECTIVE DATE OF KEY PROVISIONS OF SECURE 2.0 ACT

The effective date for provisions of the SECURE 2.0 Act vary depending on the specific provision. This table provides a summary of the effective dates for many of the key provisions.

Effective Date*	Provision
December 2022	Penalty for missed RMD reduced to 25 percent (10 percent if corrective distribution is made)
December 2022	New limitations on gift value of conservation easements
January 2023	First RMD age increases to 73
January 2023	Employer matching contributions can be designated to a Roth account
January 2023	Retirement plan custodians can offer Roth SEP and Roth SIMPLE IRAs
January 2023	QCD can be made to split-interest entities
January 2024	\$100,000 annual QCD, \$50,000 lifetime split-interest QCD limitations now eligible for inflation adjustment
January 2024	529 account can be rolled to Roth IRA
January 2024	RMDs no longer required from Roth 401(k) plans
January 2024	Traditional and Roth IRA catch-up contribution amount now eligible for inflation adjustment
January 2025	Qualified plan, SIMPLE IRA catch-up contribution limits increase
January 2026	"Highly compensated" employees must make catch-up contributions to a Roth-style account
January 2027	Saver's credit replaced by new saver's match
January 2028	ESOP rules expand to include sales of S Corporations
January 2033	First RMD age increases to 75

* Effective date generally refers to tax years beginning on this date or later.

CONCLUSION

The SECURE 2.0 Act contains a variety of provisions, mostly—but not entirely—focused on improving taxpayers' ability to save for retirement. Its provisions have effective dates that stretch out as far

2033 (see sidebar), so employers, employees, and advisors will feel the effects of this bill for many years to come. ●

Tim Steffen, CPA/PFS, CFP®, CPWA®, is the director of advanced planning for Baird. He earned a BS in accounting from

the University of Illinois. Follow him on Twitter @TimSteffenCPA.

CONTINUING EDUCATION

To take the CE quiz online, go to www.investmentsandwealth.org/IWMquiz



INVESTMENTS & WEALTH INSTITUTE®

5619 DTC Parkway, Suite 600
Greenwood Village, CO 80111
Phone: +1 303-770-3377
Fax: +1 303-770-1812
www.investmentsandwealth.org

© 2023 Investments & Wealth Institute®. Reprinted with permission. All rights reserved.

INVESTMENTS & WEALTH INSTITUTE® is a registered mark of Investment Management Consultants Association Inc. doing business as Investments & Wealth Institute. CIMA®, CERTIFIED INVESTMENT MANAGEMENT ANALYST®, CIMC®, CPWA®, CERTIFIED PRIVATE WEALTH ADVISOR®, RMA®, and RETIREMENT MANAGEMENT ADVISOR® are registered certification marks of Investment Management Consultants Association Inc. doing business as Investments & Wealth Institute.