Morgan Stanley

SECURE 2.0 Act of 2022

The SECURE 2.0 Act of 2022 (“SECURE 2.0”) was signed into law on December 29, 2022, as part of the Consolidated Appropriations Act of 2023. This legislation builds upon the Setting Every Community Up for Retirement Enhancement Act (the “SECURE Act”) enacted in 2019, which was wide ranging legislation impacting retirement savings. SECURE 2.0, similar to SECURE Act, is a significant piece of retirement legislation that is intended to make it easier for businesses to offer retirement plans and for individuals to save for retirement.

Over the next several years, SECURE 2.0 puts in place numerous provisions designed to enhance your ability to save for retirement through increased contribution opportunities, changes to rules affecting distributions from retirement accounts and benefits to establishing retirement savings. Collectively, these changes may influence how you save and use your savings over time.

This document does not reflect all the provisions of the SECURE 2.0 Act of 2022.

Effective in 2023

Key SECURE 2.0 provisions effective in 2023 include the following:

FOR INDIVIDUALS:

Increase in Age for Required Beginning Date for Mandatory Distributions

Increases the age at which required minimum distributions (“RMDs”) from IRAs or qualified retirement plans generally must commence from age 72 to age 73 in 2023 and then to age 75 in 2033[1] . Those born in 1950 and before are not affected by this change

Reduction in Excise Tax for Failure to Take RMD

Reduces the excise tax penalty for failure to take RMDs from 50% to 25% of the shortfall. Such excise tax is further reduced to 10% if the individual properly corrects the shortfall during a 2-year window.

Notes:

[1] An apparent drafting error in the statutory language makes it unclear when age 75 starts to apply in lieu of age 73, but it appears age 75 is intended to apply to those born after 1959.

One-time Election for Qualified Charitable Distribution (“QCD”) to Split-interest Entity; Increase in Qualified Charitable Distribution Limitation

Allows an individual to make a one-time election to treat up to $50,000 (as indexed for inflation) in IRA distributions paid directly to certain split interest entities (i.e., certain charitable remainder annuity trusts, charitable remainder unitrusts and charitable gift annuities) during a single tax year as qualified charitable distributions, provided certain requirements are met. Additionally, the annual IRA qualified charitable distribution limit of $100,000 will also be indexed for inflation.

Repayment of Qualified Birth or Adoption Distributions Limited to 3 Years

Imposes a 3-year time constraint on period during which a qualified birth or adoption distributions (“QBAD”) may be repaid and still qualify as a rollover contribution. Specifically, the repayment for a QBAD up to $5,000 must occur within 3 years to qualify as a rollover contribution. For any distributions taken prior to enactment of SECURE 2.0 the repayment period ends on December 31, 2025.

Exception to Penalty Tax on Early Distributions from Qualified Plans and IRAs for Individuals with a Terminal Illness

Creates an exception to the 10% early withdrawal penalty tax for those plan participants or IRA owners with a terminal illness. Requires a physician to certify that such participant or IRA owner has an illness or condition that is reasonably expected to result in death within 84 months.

Special Rules for use of Retirement Funds in connection with Qualified Federally Declared Disasters

Establishes permanent special rules governing IRA and qualified retirement plan distributions and qualified retirement plan loans in cases of qualified federally declared disasters. Permits up to $22,000 to be distributed from employer retirement plans or IRAs for affected individuals. Creates an exemption to the 10% early distribution penalty tax for such distributions. Effective for disasters occurring on or after January 26, 2021.

SIMPLE and SEP Roth IRAs

Permits SEP and SIMPLE IRAs to be designated as Roth IRAs and accept Roth contributions under the SEP or SIMPLE IRA plan, which was previously prohibited. Effective for taxable years beginning after December 31, 2022. However, in practice, this provision will not become available until a later date, as additional guidance from the IRS is required before implementation.

FOR BUSINESSES:

Modification of Credit for Small Employer Pension Plan Startup Costs:

Increases the tax credit available to small employers with 50 or fewer employees starting a new plan from 50% to 100% per year for the first 3 years, capped at $5,000. An additional credit for certain small employers starting a new plan (excluding new defined benefit plans) is also available for the first 5 years (up to $1,000 per employee equal to the applicable percentage of employer contributions to an eligible employer plan). This full additional credit is available to employers with 50 or fewer employees and is phased out for employers with between 51 and 100 employees.

Optional Treatment of Employer Matching or Nonelective Contributions as Roth Contribution

Allows a 401(a) qualified plan, 403(b) plan, or governmental 457(b) plan to provide participants with the option of treating employer matching and non-elective contributions as Roth contributions.

Effective in 2024

Key SECURE 2.0 provisions effective in 2024 include the following:

FOR INDIVIDUALS:

Special Rules for Certain Distributions from Certain 529 Qualified Tuition Programs to Roth IRAs

Permits tax-free and penalty tax-free rollovers of certain assets held in a 529 qualified tuition plan to a Roth IRA maintained for the benefit of the designated beneficiary of that 529 plan (subject to certain requirements/limitations, including the annual Roth IRA contribution limits and an overarching $35,000 lifetime limit). Such rollovers are only permitted from 529 accounts that have been established and maintained for at least 15 years and requires that the IRA owner have compensation equal or above the amount of the rollover.

Penalty Tax-Free Withdrawal from Retirement Plans for Individual in Case of Domestic Abuse

Allows a domestic abuse victim to take certain penalty tax-free withdrawals up to the lesser of (i) $10,000 (indexed for inflation), or (ii) 50% of their IRA or vested account value under certain qualified retirement plans with the option to repay such amounts within a 3-year timeframe.

Withdrawals for Certain Emergency Expenses

Allows one penalty tax-free withdrawal from an IRA or certain qualified retirement plans during a calendar year of up to $1,000 for “unforeseeable or immediate financial needs relating to personal or family emergency expenses” (“emergency personal expense distribution”). Such withdrawal may be repaid within the 3-year repayment period (which begins the day after such withdrawal). No subsequent withdrawals made during the 3 calendar years immediately following the calendar year of an emergency personal expense distribution (1st distribution) may be treated as an emergency personal expense distribution, unless the 1st distribution is repaid during the 3-year repayment period.

Indexing IRA Catch-up Limit

Indexes IRA catch-up contributions for inflation in $100 increments in the same manner as regular IRA contributions.

Roth Plan Distribution Rules

Eliminates the lifetime minimum distribution requirement for designated Roth accounts under qualified retirement plans (but the after-death required minimum distribution rules continue to apply). Under current law, such exemption was previously limited to Roth IRAs (but not designated Roth accounts held under 401(k) and other plans). Generally effective for tax years beginning after December 31, 2023, although not with respect to distributions required before January 1, 2024.

FOR BUSINESSES:

Allow Additional Nonelective Contributions to SIMPLE IRA and SIMPLE 401(k) Plans

Employers are permitted to make additional contributions to each plan participant in a uniform manner, provided such additional contribution does not exceed the lesser of 10% of a participant’s compensation or $5,000 (as indexed).

Contribution Limit for SIMPLE IRA Plans

Increases the annual deferral limit to 110% of the 2024 SIMPLE IRA plan limit (as indexed) and the catch-up contribution limit at age 50 to 110% of the 2024 SIMPLE IRA plan limit (as indexed) in the case of an employer with no more than 25 employees. Employers with 26 to 100 employees are permitted to provide these higher deferral limits, provided that the employer either provides a 4 % matching contribution or a 3% employer non-elective contribution.

Updating Dollar Limit for Mandatory Distributions

Increases the amount that employers may, without participant consent, distribute and rollover from a participant’s workplace retirement account into an IRA from $5,000 to $7,000.

Emergency Savings Accounts Linked to Individual Account Plans

Allows employers to offer their employees (excluding highly compensated employees) a pension-linked emergency savings account as part of a defined contribution plan. Employers may automatically opt employees into these accounts at no more than 3% of their salary, and the portion of an account attributable to the employee's contribution is capped at $2,500 (or lower as set by the employer). Contributions are made on a Roth-like basis and are treated as elective deferrals for purposes of matching contributions with an annual matching cap set at the maximum account balance ($2,500 or lower as set by the employer). Requires employer matching contributions be made to the individual's defined contribution plan account rather than to the emergency savings account. At separation from service, employees are permitted to roll the emergency savings account into a Roth defined contribution plan or an IRA.

Effective in 2025

Key SECURE 2.0 provisions effective in 2025 include the following:

FOR INDIVIDUALS:

Higher Catch-up Limit to Apply at Age 60, 61, 62 and 63

Increases the catch-up contribution limit for non-SIMPLE plans for individuals aged 60 to 63 to the greater of (i) $10,000 per year, or (ii) 150% of the regular catch-up contribution amount in 2024 (as indexed for inflation). The catch-up contribution limit for SIMPLE plans is similarly increased for individuals ages 60 to 63 to the greater of (i) $5,000 per year, or (ii) 150% of the regular catch-up amount in 2025 (as indexed for inflation).

FOR BUSINESSES:

Expanding Automatic Enrollment in Retirement Plans

Requires newly established 401(k) and 403(b) plans to automatically enroll eligible participants with an initial minimum enrollment amount of 3% (unless the participant affirmatively elects otherwise). Such new plans are also required to automatically increase (or escalate) such amounts by 1% each year with a cap at 15% (although plans are permitted to cease the annual automatic escalation at 10%). Exempt from these requirements are small businesses with 10 or fewer employees, SIMPLE Plans, new businesses that have been in business for less than 3 years, church plans and governmental plans.