SECURE 2.0 Act: New Retirement Savings Rules for 2023 and Beyond

The SECURE 2.0 Act was enacted late in 2022 to supplement changes that were put in place by the SECURE Act of 2019 to enhance retirement savings opportunities. The Act contains many provisions that will have at least some impact on IRAs and most employer retirement plans, and some may need to take proactive steps in the future. Many of the provisions will need guidance issued by regulators to iron out the details. Notable provisions include:

- Increasing the required minimum distribution (RMD) age from 72 to 73, then 75
- Reducing the penalty for failure to take an RMD
- Changing the amount and tax treatment of catch-up contributions
- Permitting new employer plan design features, including certain student loan matching programs and in-plan emergency savings accounts
- Requiring certain new 401(k) and 403(b) plans to include automatic enrollment and automatic escalation features
- Allowing 529 account beneficiaries to transfer balances to a Roth IRA

Below is a summary of the provisions by their effective date.

Changes Effective 2023

Minimum Distribution Age Increased and Penalties Decreased

The age at which you must begin minimum distributions from your retirement account is increased to 73 for 2023, and then to age 75 in 2033. Individuals born in 1950 or earlier are unaffected by this change and must take any RMDs due for 2022 and later years.

If you fail to take your RMD for 2023 and future years, the IRS penalty has been reduced from 50% to 25%. If you correct the failed RMD and file a correct tax return in a timely manner, the penalty is reduced to 10%. "Timely" is generally within 2 years of the year-end for the failed RMD.

QCD limits increased

The IRA qualified charitable distribution provision is increased to allow for a one-time, $50,000 distribution to charities through charitable gift annuities, charitable remainder unitrusts, and charitable remainder annuity trusts. In addition, the annual IRA charitable distribution limit of $100,000 will be inflation adjusted going forward. IRA owners must be at least age 70 ½ to be eligible for a QCD.

Penalty-free early distributions

An additional 10% tax typically applies to early distributions (pre-59 ½) from retirement accounts. The following exceptions now apply.

Penalty-free early distributions (continued)

1. Distributions to a terminally ill individual are exempted. An illness is considered terminal if a physician certifies that the illness is reasonably likely to result in death within 84 months.
2. Public sector firefighters may take penalty-free premature distributions beginning at age 50, and now private sector firefighters are also eligible.
3. Permanent rules allow the penalty-free distribution of up to $22,000 in the case of a federally declared disaster. Such distributions may be taken into account as gross income over 3 years. Distributions may also be repaid to a tax preferred retirement account. Amounts distributed prior to the disaster to purchase a home can be recontributed, and an employer may allow larger plan loans and additional time for loan repayment by affected individuals.

Increased tax credits for small employer retirement plan startup costs

The credit is a complete offset of the startup administration costs for the first three years of a new plan's establishment. The Act increases the credit from 50% to 100% for employers with up to 50 employees (employers with 51 to 100 employees still receive a 50% credit), although dollar limitations apply such that no more than $5,000 may be credited annually.

An additional credit is now made available that is a percentage of what is contributed by the employer on behalf of employees, up to a per-employee cap of $1,000. This additional credit is limited to employers with 50 or fewer employees and phased out for employers with between 51 and 100 employees. The applicable percentage is 100% in the first and second years, 75% in the third year, 50% in the fourth year, 25% in the fifth year – and no credit for tax years thereafter.

Qualified Longevity Annuity Contract (QLAC) enhancements

The 25% cap that limited how much retirement savings could be allocated to the purchase of a QLAC is eliminated, and the maximum aggregate limit on the purchase of QLACs is increased from $125,000 to $200,000. The payments from QLACs generally begin toward the end of life expectancy, and do not have typical RMD requirements.

Sole proprietors may establish 401(k)s after year-end and make retroactive deferrals

An employer may establish a new 401(k) plan after the end of the taxable year, but before the employer's tax filing date. Employer contributions may be made up until the tax filing date, but when sponsored by an individual who is a sole proprietor or otherwise taxed as self-employed, the salary deferral for the individual may be made up until tax filing date as well.

SIMPLE and SEP Roth IRAs

SIMPLE IRAs may now accept Roth contributions. In addition, employers may allow employees to treat employee and employer SEP contributions as Roth (in whole or in part). Updates to plan documents, regulations, and guidance for administration will be necessary before these Roth contributions may be made.

Optional Roth treatment for employer matching or nonelective contributions

Employers with defined contribution plans (e.g. 401(k) and profit sharing) may allow participants to receive matching and profit sharing contributions on a Roth basis.

Changes Effective in 2024

Index IRA catch-up contribution limit for inflation

Individuals age 50 and older may contribute up to $1,000 more in an IRA contribution each year, but in the past the amount has not been adjusted for inflation. Inflation adjustments will now be made going forward.

Student loan payments treated as salary deferrals for 401(k) matching contributions

An employer now has the option to make matching contributions under a 401(k), 403(b), or SIMPLE IRA plan with respect to “qualified student loan payments”, with no requirement that the employee make an actual salary deferral to the plan. The same eligibility and vesting requirements must apply to matching for both salary deferrals and qualified student loan payments.

529 plan rollovers to Roth IRAs

Beneficiaries of 529 college savings accounts may roll over up to $35,000 over the course of their lifetime from any 529 account in their name to their Roth IRA. These rollovers are subject to Roth IRA annual contribution limits, and the 529 account must have been open for at least 15 years.

Employers allowed to replace SIMPLE IRAs with safe harbor 401(k) plans during a year

An employer may replace a SIMPLE IRA plan with a safe harbor 401(k) during a plan year. Previously, a change could only be made from a SIMPLE IRA at year-end.

Penalty-free early distributions

An additional 10% tax typically applies to early distributions (pre-59 ½) from retirement accounts. The following exceptions will apply.

1. Distributions used for emergency expenses, which are unforeseeable or immediate financial needs. Only one distribution is allowed per year of up to $1,000. They individual may repay the distribution within three years. No further emergency distributions are allowed during the repayment period unless repaid in full.
2. Distributions in case of domestic abuse maybe be made up to the lesser of $10,000 (indexed for inflation) or 50% of the participant’s plan account balance. The individual has the opportunity to repay the withdrawn money over three years.

Emergency Savings Accounts in Defined Contribution Plans

Employers may offer emergency savings accounts to non-highly compensated employees as part of their 401(k) plan, 403(b) plan, or governmental 457(b) plan. Participants may contribute up to $2,500, which will be treated as Roth contributions to the plan. If the employer makes matching contributions to the plan, the employee’s emergency savings contributions must be matched at the same rate as other deferrals, but must not be placed in the emergency savings account.

Highly compensated pre-tax deferrals limited to regular contribution limit

Individuals who are 50 or older at year-end may currently make catch-up contributions to a qualified retirement plan on a pre-tax or Roth basis. For those who made $145,000 or more in the previous year, catch-up contributions will be subject to Roth tax treatment, with no pre-tax option.

Additional SIMPLE IRA employer contributions permitted

Employers that sponsor a SIMPLE IRA generally must contribute either 2% of compensation or match up to 3% of employee contributions to the plan each year. Starting in 2024, additional contributions may be made in a uniform manner to each employee eligible for the plan, provided the contribution does not exceed the lesser of 10% of compensation or $5,000.

Contribution limit for SIMPLE plans

The annual deferral and the catch-up contribution limit at age 50 is increased by 10%, versus what would otherwise be required, in the case of an employer with 25 or less employees. An employer with 26 to 100 employees will be permitted to provide higher deferral limits too, but only if the employer provides either a 4% matching or a 3% employer contribution (more than what would otherwise be required).

Starter 401(k) plans for employers with no retirement plan

An employer that does not sponsor a retirement plan may establish a starter 401(k) plan that would generally require all employees be default enrolled in the plan at a 3 to 15% of compensation deferral rate. The limit on annual deferrals would be the same as the IRA contribution limit, which for 2023 is $6,500 with an additional $1,000 in catch-up contributions beginning at age 50. No employer contributions would be made, but all discrimination testing would automatically be passed.

Roth plan distribution rules

RMDs are not required from Roth IRAs until after the death of the original IRA owner, but required for participants with a Roth balance in a retirement plan. The Act eliminates the pre-death RMD requirement for Roth accounts in employer plans.

Surviving spouse election to be treated as employee

A surviving spouse may elect to treat their deceased spouse's IRA as his or her own, which may allow for favorable distribution treatment.

For more information, please contact your Oppenheimer Financial Professional.

Oppenheimer & Co. Inc.
85 Broad Street
New York, NY 10004
800-620-OPCO • 212-668-8000
www.oppenheimer.com
5439762.1 RBI

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