“Just the FACTS”

A Legislative Update from Your Friends at FACTS, Inc.

1st Quarter 2020

The SECURE Act

The SECURE Act went into effect January first of this year, and with it came fairly substantive changes. We always welcome your questions and encourage you to reach out to your TPA but as a summary by section, here are the FACTS of the SECURE Act.

Section 104 - Increase in credit limitation for qualified plan start-up costs for “Eligible Employers”

The term "eligible employer" means, with respect to any year, an employer which *had no more than 100 employees who received at least $5,000 of compensation from the employer for the preceding year.*

The small employer pension plan start-up cost credit determined under this section for any taxable year is an amount equal to 50 percent of the qualified startup costs paid or incurred by the taxpayer during the taxable year. The old rule said

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Client Secure Portal

Still Have Questions?

Access to your plan documents, valuations, employee statements, IRS filings, employee notices, and the ability to upload participant census information has been live for four months now. As we progress through our year-end requests, we would like your feedback. It’s important to remember that we created the client portal to improve efficiency and security. The portal also allows you to access stored items and view participant census data at any time on-demand, so be sure to take full advantage of these features. If you still have questions, please know that we always welcome your call. Be sure to reach out to your TPA as they will be happy to help in any way they can.

Did you buy another company or practice this year?

Did you or your business partner decide to buy into another business? Depending on the new ownership structure, you *may* or *may not* be required to include that new business as part of your retirement plan. If, as a result of the purchase, you form what the IRS refers to as a “controlled group”, the staff of that new business will need to be included for testing purposes of your existing plan. If you, your business partner, or a family member has made a business purchase, let your TPA know. They can help you determine if a controlled group now exists and explain the impacts to your existing plan.

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50% up to $500. In other words, the most an employer could get was $500 regardless of what their costs were. The new calculation uses the same 50% but the $500 cap has now been replaced with the following:

(1) $500, or
(2) the *lesser* of: (a) $250 for each employee of the eligible employer who is not a Highly Compensated Employee and who is eligible to participate in the eligible employer plan maintained by the eligible employer, *or* (b) $5,000. The credit applies for up to three years.

Example 1: Startup 401(k) for a 3-person machine shop. Two owners plus 1 employee who is not considered highly compensated.

Credit cap= Greater of $500, ***or,*** 50% of cost up to $250 ($250x1)

If the plan had startup and admin costs totaling $1,000 in year one and administrative costs of $700 each year thereafter, the year one credit would be $500. Credits in years two and three would be $500 each ($500 minimum).

Example 2: Same machine shop which now employs 20 non-highly compensated employees (22 employees total).

Credit cap = Greater of $500 ***or*** 50% of admin cost up to $5,000 (20x$250)

In this example, the credit cap is $5,000 per year for the next three years. If the plan had startup plus admin costs of $3,400 in year one and administrative costs of $2,100 per year thereafter, the year one credit would be $1,700. Years two and three would have credits of $1,050 each.

Question
Which costs are eligible?

Answer
A: IRS describes them as “qualified startup costs” and defines them as any ordinary and necessary expenses of an eligible employer which are paid or incurred in connection with the establishment or administration of an eligible employer plan, including the retirement-related education of employees with respect to such plan.

Section 45T – Automatic enrollment tax credit for retirement savings options provided by eligible employers

The retirement auto-enrollment credit is an amount equal to $500 for any taxable year occurring during the credit period. The credit period with respect to any Eligible Employer is the 3-taxable-year period beginning with the first taxable year for which the employer includes an eligible automatic contribution arrangement.

Question
If an employer elects to make auto-enrollment as part of their plan design, and keeps it as part of their plan design for three years, they will get the $500 each year for 3 three years or $1,500 total?

Answer
Correct, and as we currently understand, it is *not* a reduction against qualified startup costs like the Section 104 credit. Assume you had a plan with 20 non-highly compensated employees that also elected auto enroll. If the plan had startup and admin costs of $3,400 in year one and administrative costs of $2,100 per year thereafter, the year one credit would be $2,200 ($1,700+$500) and years two and three would have credits of $1,550 ($1,050+$500) each.

Question
Is this credit available to new plans, existing plans or both?

Answer
Both new ***as well as*** existing plans can adopt this provision. If your client has an existing 401(k) plan, they could adopt this provision and receive the credit. Auto-enrollment, if adopted, needs to be ***thoroughly*** explained to employees to avoid uncomfortable conversations in the future.

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Section 111 - Allowing Long-term Part-time Workers to Participate in 401(k) Plans

When an employee has three or more consecutive years of employment during which he/she completes at least 500 hours of service, they now need to be included in the plan. *The owner may elect to exclude such employees from testing under the nondiscrimination and coverage rules, and from the application of the top-heavy rules**. Applies to plan years beginning after Dec. 31, 2020; service periods beginning before Jan. 1, 2021 shall not be taken into account***

Question

So this means I now need to include people whom I did not have to include before?

Answer

Quite possibly. If you have an employee who has worked at least 500 hours per year for the last two consecutive years and you are fairly certain they will work 500 or more hours this year, chances are you will need to allow them to make salary deferrals into the 401(k) plan. You will not have to make any employer contributions on their behalf (matching or profit sharing), nor will their participation impact any the compliance tests you must pass at the end of the year. For most sponsors, the only impact they will see is a *slight* increase in their annual administrative fees as their head-count could increase.

Section 112 - Penalty-free Withdrawals from Retirement Plans for Individuals in Cases of Birth or Adoption

The legislation provides for penalty-free withdrawals from retirement plans for any "qualified birth or adoption distributions." These distributions may be made (capped at $5,000) within 12 months after the adoption is finalized. Unlike hardship withdrawals, these amounts may be fully repaid to the plan at a later date. Further guidance will be issued on the repayment timing.

Section 403 - Increased Penalties for Failure to File Retirement Plan Returns

For any of your solo(k) clients, keep eye on the $250K limit. Once a solo(k) reaches $250K in assets, they need to file a 5500. We have also seen multiple cases where a solo(k) owner adds their child to the business when assets are *under $250K* creating the need to file a 5500. Penalties for not filing have more than doubled as a result of this legislation.

Section 114 - Community Newspapers Pension Funding Relief

Community newspapers are generally family-owned, non-publicly traded, independent newspapers. This provision provides pension funding relief for community newspaper plan sponsors by increasing the interest rate to calculate those funding obligations to 8%. Additionally, this bill provides for a longer amortization period of 30 years from 7 years. These two changes would reduce the annual amount struggling community newspaper employers would be required to contribute to their pension plans.