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BULLETIN

TO: Pension Plan Clients

FROM: Saltzman & Johnson

DATE: February 6, 2024

RE: SECURE 2.0 Act Update – IRS Notice 2024-2

On December 20, 2023, the IRS issued Notice 2024-2 providing guidance with respect to certain provisions of the SECURE 2.0 Act of 2022 ("Act") in the form of questions and answers regarding certain sections of the Act. This notice discussed the following sections of the Act, which are relevant to collectively bargained pension plan clients:

- Section 326: Penalty free distributions for terminally ill individuals
- Section 348 - Interest crediting rate for cash balance plans; and
- Section 501 - Provisions relating to plan amendments

Below is a brief summary of the guidance on these provisions applicable to pension plan clients.

Section 326 – Penalty Free Distributions to Terminally Ill Individuals

Section 326 of the SECURE 2.0 Act allows qualified plans to offer distributions to terminally ill participants without a 10% early withdrawal penalty on or after the date a physician has certified the individual has a terminal illness. (IRS Notice 2024-2, Section F, page 30). IRS Notice 2024-2 provided the following guidance concerning distributions to terminally ill individuals:

- ➢ The term "terminally ill individual distribution" means any distribution from the plan to an employee who is a terminally ill individual that is made on or after the date upon which the employee has been certified as having a terminal illness. (*Id*., Q&A F-1).
- ➢ The following types of pension plans are eligible to make a terminally ill individual distribution:
    - IRC § 401(a) qualified plan (including a defined benefit plan), or profit-sharing plan
    - Annuity plans under IRC § 403(a);
    - Annuit contract under IRC § 403(b);
    - Individual retirement accounts under IRC § 408(a); or
    - Individual retirement annuity under IRC § 408(b). (*Id*., Q&A F-2).
- ➢ A terminally ill individual distribution is not subject to the 10% additional tax otherwise required for early distributions under IRC § 72(t). The distribution is taxable as gross income to the participant. (*Id*., Q&A F-3).

- The term "terminally ill individual" means the individual has been certified by a physician as having a condition which can reasonably be expected to result in death in 84 months or less from the date of certification. (*Id*., Q&A F-4).
- A physician capable of making a terminally ill certification is a doctor of medicine or osteopathy legally authorized to practice medicine and surgery in the State in which he works. (*Id*., Q&A F-5).
- A certification of terminal illness from a physician must include:
    - A statement that the individual's condition can reasonably be expected to result in 84 months or less as of the date of the certification;
    - A description of the evidence used to support the statement of illness or physical condition;
    - The name and contact information of the physician making the statement;
    - The date the physician examined the individual or reviewed the evidence, and the date the certification was signed by the physician; and
    - The signature of the physician making a statement with a declaration that the physician understands that by signing the document, they confirm they composed the description based on their own examination of the individual or the evidence provided. (*Id*., Q&A F-6).
- The certification must be made before the employee receives a terminally ill individual distribution. (*Id*., Q&A F-7).
- Generally, there is no limit on the amount an employee is permitted to receive a terminally ill individual distribution. (Q&A F-8)
- An employee may recontribute any portion of a terminally ill individual distribution to a qualified retirement plan in which the employee is a beneficiary and to which a rollover can be made. (*Id*., Q&A F-9).
- A qualified retirement plan is not required to permit terminally ill individual distributions. Amendments adopted to permit terminally ill distributions are discretionary amendments. (*Id*., Q&A F-10).
- If a plan chooses to amend the plan to permit terminally ill individual distributions, the deadline is consistent with the deadlines listed below for section 501. (*Id*., Q&A F-11).
- Terminally ill individual distributions provide an exception to the 10% additional tax, but the section <u>does not provide an exception to the distribution requirements</u>. As such, the employee must otherwise be eligible for a permissible in-service distribution. (*Id*., Q&A F-12).
- The documentation required for a terminally ill individual distribution includes the physician's certification described above. The underlying documentation upon which the certification is based does <u>not</u> need to be provided. Further, if the employee is a physician, they can not certify their own illness. The employee should retain the underlying documentation on which the certification is based, as well as a copy of the certification itself for tax purposes. (*Id*., Q&A F-13).
- An employee may not self-certify that they are terminally ill. (*Id*., Q&A F-14).

If a retirement plan does not permit terminally ill individual distributions, an employee may treat an otherwise permissible in-service distribution as a terminally ill distribution on their federal income tax return. They must claim on Form 5329 that the distribution is a terminally ill individual distribution. While the distribution is considered gross income, it will not be subject to the 10% additional tax. (*Id*., Q&A F-15)

Section 348 – Cash Balance

Section 348(a) of the Act amends the rule for applying the anti-cutback rules for applicable cash balance plans. Previously, the interest crediting rate in effect for a defined benefit plan was a reasonable projection of the variable interest crediting rate, not to exceed 6%.

Further, a defined benefit plan did not satisfy the accrued benefit requirements if the employee's benefit accrual was ceased, or their rate of benefit accrual was reduced due to the employee's age.

Finally, the defined benefit plan was treated as violating the accrued benefit requirements if any interest credit for any plan year was at a rate that was greater than a market rate of return.

IRS Notice 2024-2 provided the following guidance concerning an exception to the accrued benefits rules for variable interest crediting rates for cash balance plans:

- The effect of the enactment of Section 348 of the Act is that for cash balance plans that provide pay credits to participants that increase with a participant's age or service and provide a variable interest crediting rate, no longer risk violating the accrued benefits requirement of IRC § 411(b)(1) if the interest crediting rate falls below a certain point. (*Id*., Q&A H-1). Prior to the Act, a cash balance plan had to provide a fixed annual minimum interest crediting rate as part of its interest crediting rate to prevent a violation of the accrued benefits requirement. The fixed annual minimum interest crediting rate is no longer needed to avoid this type of violation.
- An amendment to a cash balance plan is made pursuant to this section only if:
  - The cash balance plan is currently providing for principal credits that increase with a participant's age or service, and the amendment is to change the plan's interest crediting rate, or
  - The plan is implementing a pattern of principal credits as part of the amendment. (*Id*., Q&A H-2).
- Cash balance plans may amend their plans pursuant to this section only for interest credits going forward, beginning with interest crediting periods after the later of:
  - The effective date of the amendment; or
  - The date the amendment is adopted. (*Id*., Q&A H-3).
- If the plan's interest crediting rate prior to the amendment is a fixed rate permitted by IRC regulations, and the amendment changes the interest crediting rate to any permitted variable rate, subject to a specified limit, then it will qualify for an exception from the anti-cutback rules of 411(d)(6). (*Id*., Q&A H-4).
- A plan that is not a cash balance plan (i.e, another type of statutory hybrid plan) cannot create an amendment pursuant to this section. (*Id*., Q&A H-5).

Section 501 – Extension of Deadlines for SECURE 2.0 Act Plan and other Amendments

Section 501 of the Act allowed collectively bargained plans to make amendments in accordance with SECURE 2.0 without failing the anti-cutback requirements of ERISA or pursuant to any regulation issued by the IRS or Department of Labor as long as:

1. The plan amendment is adopted before December 29, 2027; [1]
2. The amendment applied retroactively to the effective date of the applicable provision of the Act or for discretionary amendments, the effective date specified by the Plan; and
3. The plan operated as if the amendment were in effect during the period beginning with the effective date of the applicable provision of the Act.

IRS Notice 2024-2 extended the deadline for plan amendments for collectively bargained plans:

- The new deadline to amend a 401(a) collectively bargained plan to comply with the SECURE 2.0 Act is **<u>December 31, 2028</u>**. (*Id*., Q&A, J-1)
- Amendments may be made to the plan after the deadline, but the amendments will not receive the anti-cutback relief provided in this section. (*Id*., Q&A, J-1)

[1] For collectively bargained plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified before December 29, 2022.