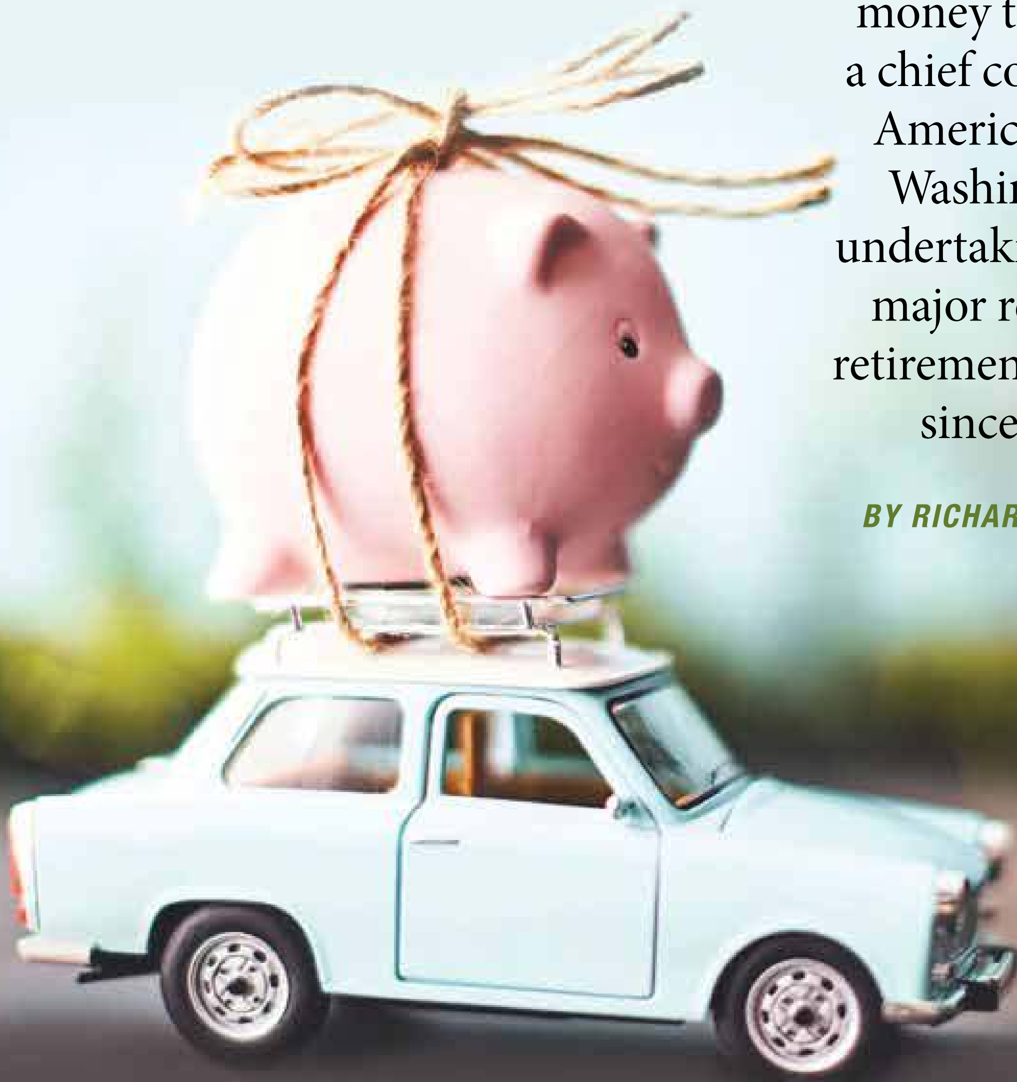
THE SECURE ACT
A RETIREMENT SOLUTION?

Having enough money to retire is a chief concern for Americans, and Washington is undertaking its first major reform of retirement accounts since 2006.

BY RICHARD KONRAD



The National Institute on Retirement Security recently commissioned a study titled "Retirement Insecurity 2019: Americans' Views of the Retirement Crisis." Among the findings is that three-quarters of Americans believe the nation is facing a retirement crisis. Some 70% say the average worker cannot save enough on his or her own to guarantee a secure retirement, and 65% say it's likely they will have to work past retirement age to have enough money to retire.

According to the study: "When all working individuals are included – not just individuals with retirement accounts – the median retirement account balance is $0 among all working individuals. Even among workers who have accumulated savings in retirement accounts, the typical worker has a modest balance of just $40,000.

Washington has undertaken its first major reform of retirement accounts since the Pension Protection Act of 2006, with a particular focus on 401(k) plans. Many employers view these plans with angst, largely because of their perceived complexity and their administrative and reporting rules and requirements. Many are asking whether these proposed changes are going to simplify and help the process.

IRAs and defined contribution plans have become a common feature of the U.S. retirement landscape. More than half of total U.S. retirement assets are held in such accounts, and a majority of U.S. households have a portion of their assets invested in them. According to Investment Company Institute, as of March 31, 2019, 401(k) plans held an estimated $5.7 trillion in assets and represented more than 19% of the $29.1 trillion in U.S. retirement assets, which includes employer-sponsored retirement plans (both defined benefit and defined contribution plans with private- and public-sector employers), individual retirement accounts (IRAs) and annuities. In comparison, in 2010, 401(k) assets were $3.1 trillion and represented 17% of the U.S. retirement market.

At the end of May, the House of Representatives passed the SECURE Act (Setting Every Community Up for Retirement Enhancement), but the path ahead for the bill remains unclear as the Senate is now focused on its version of retirement legislation, called the RESA Act (Retirement Enhancement and Security). Due to strong bipartisan support in both the Senate and House, it is anticipated that some form of RESA will pass, that the two bills will be reconciled and will subsequently become law.

The SECURE Act aims to make it easier for many Americans to save for retirement. Most of the provisions provide more flexibility to employers and reduce administrative costs regarding creation and implementation of employer-related retirement plans. These reforms may allow employers to create more robust retirement plans and encourage employees to participate in such plans.

Among the key changes in the SECURE Act are several adjustments that may make it easier for workers to save for retirement, boost the amounts they save and create income streams once they retire. Some of the changes contemplated:

1. Delay withdrawals (required minimum distributions) from both IRAs and 401(k)s
2. Facilitate the creation of Multiple Employer Plans (MEP)
3. Remove annuity roadblocks
4. Boost contribution rates
5. Additional eligibility for part-time employees
6. Greater flexibility in administration and setup.

Let's take a look at each of these provisions and their impact on retirement planning.

DELAYED WITHDRAWALS

This feature recognizes that Americans are living and working longer and consequently should not be forced to take money out of their plans prematurely.

MEET THE MEPS

Many small businesses do not have the resources to offer their employees a workplace retirement plan due to the costs and complexity involved to administer such a plan. Multiple Employer Plans allow multiple businesses to participate in a single qualified plan to benefit from economies of scale.

Currently, rules for creating a Multiple Employer Plan are somewhat restrictive and prevent unrelated employers from joining together solely to participate in an MEP (known as the "commonality" requirement). This requires employers to be part of a common group or association with substantial business purposes other than the MEP.

In addition, under current regulations, if one employer in the MEP fails to comply with tax, fiduciary or other rules, all of the employers faced potential liability (known as the "one bad apple" rule).

The SECURE Act would let a plan operate for workers of totally unrelated businesses, allowing open MEPs for employers that don't share common traits. In addition, the SECURE Act protects small employers in open MEPs from penalties if other members are found to have engaged in wrongdoing.

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REMOVE ANNUITY ROADBLOCKS

Unlike defined benefit plans, defined contribution plans are oriented toward building a lump sum rather than providing lifetime income during retirement. This is done through providing an option to purchase or invest in an annuity. Employers have been concerned about being sued for breach of fiduciary duties if the selected annuity provider fails and about what the fiduciary responsibilities are for ongoing monitoring and oversight of that provider.

The SECURE Act creates a safe harbor that employers can use when choosing a group annuity to include as an investment option within a defined contribution plan, according to new provider selection rules.

Plan sponsors would be required to disclose annually an estimate of monthly payments participants would receive if their total account balance were used to purchase an annuity.

In addition, the SECURE Act allows for portability of annu-

ity investments to another 401(k) or IRA without surrender charges.

BOOSTED CONTRIBUTION RATES

The bill increases the cap limit on contributions for safe harbor 401(k) plans from 10% to 15% of pay.

ADDITIONAL ELIGIBILITY FOR PART-TIME WORKERS

Currently, employers may exclude part-time workers (defined as those who work fewer than 1,000 hours annually) when providing a defined contribution plan.

The SECURE Act will require employers maintaining a 401(k) plan to have a dual eligibility requirement, in which an employee must complete either of the following to participate:

a.) Have one year of service and have worked at least 1,000 hours

b.) Have three consecutive years of service during which the employee works at least 500 hours.

FLEXIBILITY IN ADMINISTRATION AND SETUP

The SECURE Act allows employers more flexibility to retroactively adopt retirement plans. Currently, the plan is considered to have been established within the tax year that the plan is adopted. The SECURE Act allows qualified retirement plans adopted before the due date of the tax return for any taxable year to treat the plan as having been adopted as of the last day of the tax year.

In addition, it increases the tax credit for plan start-up costs, making it more affordable for small businesses to set up retirement plans.

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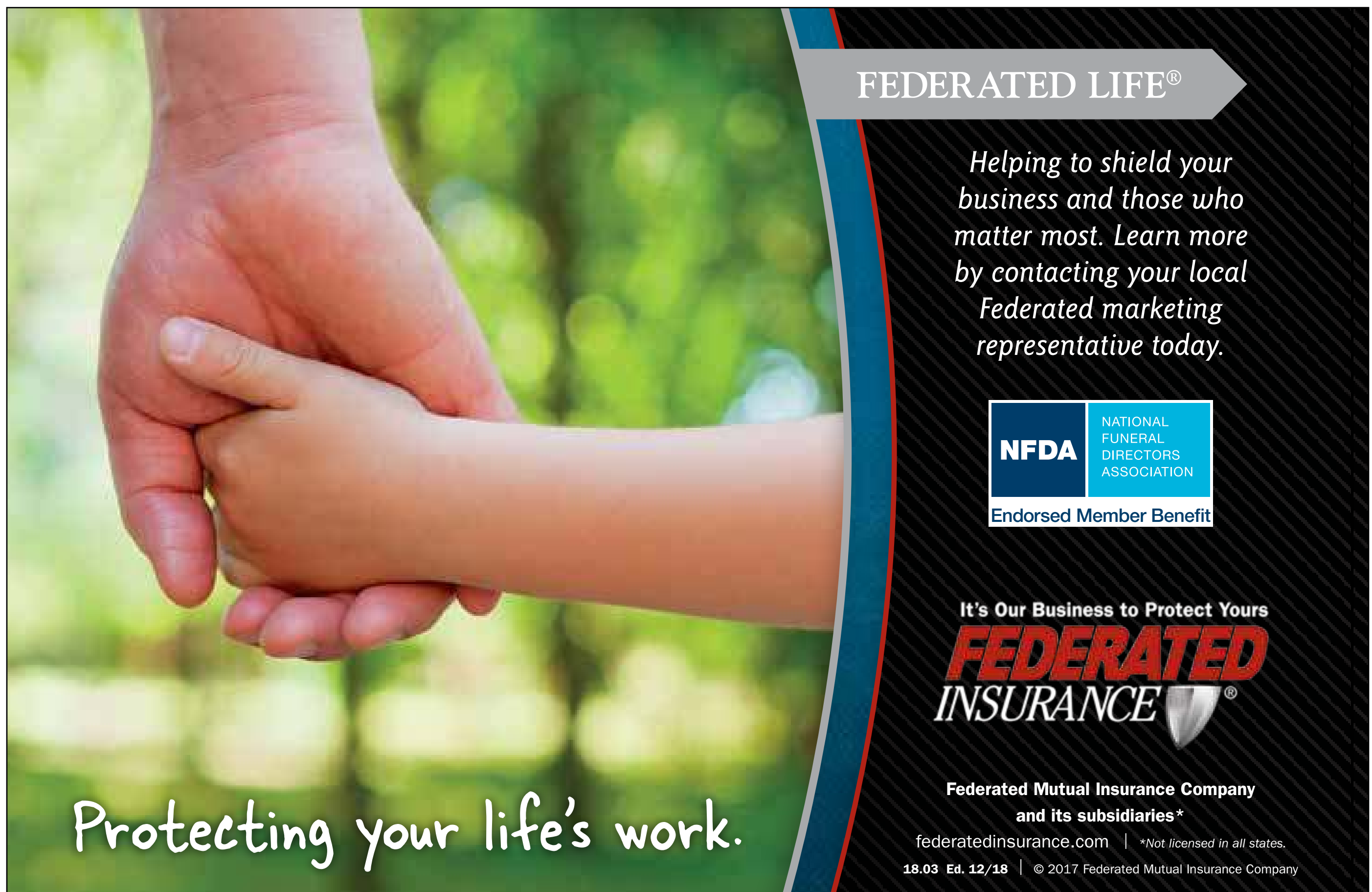
CONCLUSION

Many aspects of the SECURE Act simplify and encourage the creation of qualified retirement plans and encourage auto enrollment and higher savings.

But not all is likely positive. Although the SECURE Act's focus is on employer-related retirement plans, there are some potential negative provisions to the transfer of qualified retirement assets upon death, known as "stretch" provisions. Currently, beneficiaries who inherit such assets can elect to receive distributions from these plans over their remaining lifetimes.

Under the SECURE Act, instead of stretching the distributions over a lifetime, the beneficiary must withdraw all assets from the plan within 10 years of the decedent's death. This would accelerate the tax realization on the plan assets.

There are certain exceptions – spousal inheritance, for example – but investors with large qualified retirement account balances may want to consider whether any adjustment to their designated beneficiaries is warranted. Life insurance will like-



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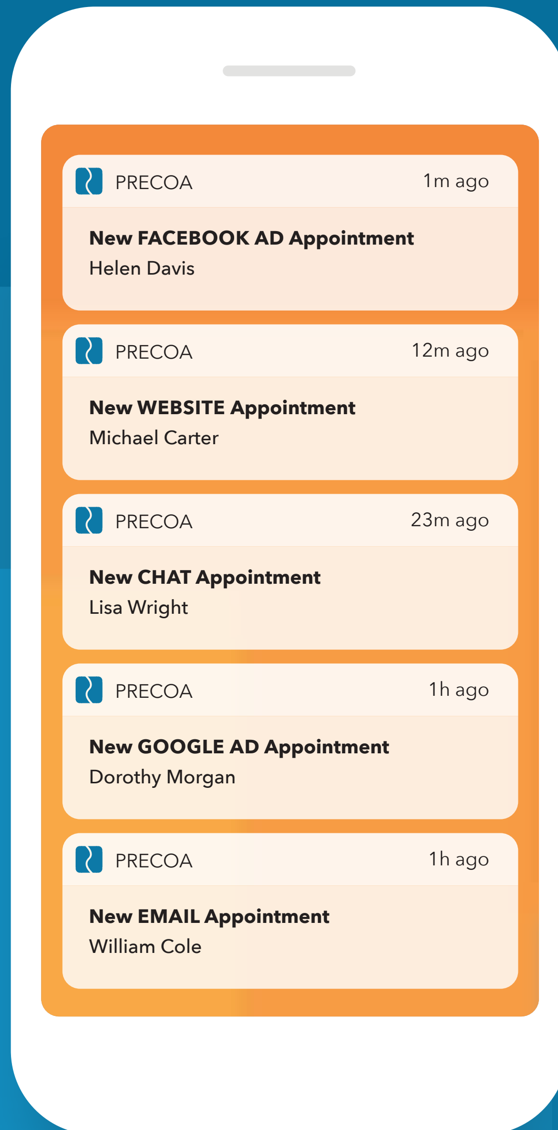

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ly become a more important planning tool as people may need a way for minor children to pay the income taxes without further eroding their inheritance. Roth IRAs and Roth 401(k)s may also provide a better way to pass wealth tax-free to younger generations.

The provisions for part-time employees may be problematic for some employers. Part-time employees working nine and a half hours per week will be mandated to receive employer-matching and profit-sharing contributions in order to satisfy non-discrimination provisions of qualified plans. As a result, some employers may decide to terminate these plans.

A potential solution lies in defined benefit plans, but these carry significant costs and liabilities. The SECURE Act and RESA only make changes to 401(k) and profit-sharing plans. Under the current proposals, there are no changes being proposed to defined benefit plans. Thus, to exclude part-time employees from a retirement plan, employers may wish to consider implementing a defined benefit plan instead of a defined contribution plan. There are significant advantages to a defined benefit plan, including higher contribution limits and the ability to make tax-free distributions for medical expenses, assuming the defined benefit plan has a 401(k) component (also known as a DB(k) plan or eligible combined plan). But DB(k) plans are costly, requiring separate administration for each part of the plan. They also place the investment risks associated with market fluctuations and investment decision-making responsibility on the employer instead of the employee.

But all is not likely positive. There are some potential negative provisions to the transfer of qualified retirement assets upon death, known as "stretch" provisions.

At this point, we think it makes sense for employers to consult their investment and retirement advisors, as well as estate planners, to prepare for the final form of this legislation. Even with the potential negatives, the proposed bill includes features that may be substantially beneficial for both plan sponsors and participants who want to increase retirement income security. ≡

Richard Konrad is director of value strategy at Roosevelt Investments. Prior to joining Roosevelt, he served as managing partner and CIO for Value Architects Asset Management and as a partner of Blueprint Financial Planning. Konrad, who has more than 40 years of experience, earned a master's degree in finance from Northeastern University and completed the Harvard Business School Executive Program on behavioral investing. He also holds the Chartered Financial Analyst and Certified Financial Planner designations. In his free time, Konrad is an adjunct instructor of retirement planning at NYU. He can be reached at 646-452-6721.

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