DESCRIPTION OF H.R. ____, THE "SECURING A STRONG RETIREMENT ACT OF 2021"

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INTRODUCTION

The House Committee on Ways and Means has scheduled a committee markup on May 5, 2021 of H.R. ____, the "Securing a Strong Retirement Act of 2021." This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of the bill.

[1] This document may be cited as follows: Joint Committee on Taxation, *Description of H.R. ____, the "Securing a Strong Retirement Act of 2021"* (JCX-21-21), May 3, 2021. This document can also be found on the Joint Committee on Taxation website at www.jct.gov. All section references herein are to the Internal Revenue Code of 1986, as amended (herein "Code"), unless otherwise stated.

A. Expanding Coverage and Increasing Retirement Savings

1. Expanding automatic enrollment in retirement plans

Present Law

Section 401(k) plans

A section 401(k) plan is a type of profit-sharing or stock bonus plan that contains a qualified cash or deferred arrangement. Such arrangements are subject to the rules generally applicable to qualified defined contribution plans. In addition, special rules apply to such arrangements. Employees who participate in a section 401(k) plan may elect to have contributions made to the plan (referred to as "elective deferrals") rather than receive the same amount as current compensation.[2] The maximum annual amount of elective deferrals that can be made by an employee for a year is $19,500 (for 2021) or, if less, the employee's compensation.[3] For an employee who attains age 50 by the end of the year, the dollar limit on elective deferrals is increased by $6,500 (for 2021) (called "catch-up contributions").[4] An employee's elective deferrals must be fully vested. A section 401(k) plan may also provide for employer matching and nonelective contributions.

Section 403(b) plans

Tax-deferred annuity plans (referred to as section 403(b) plans) are generally similar to qualified defined contribution plans, but may be maintained only by (1) tax-exempt charitable organizations,[5] and (2) educational institutions of State or local governments (that is, public schools, including colleges and universities).[6] Section 403(b) plans may provide for employees to make elective deferrals (in pre-tax or designated Roth form), including catch-up contributions, or other after-tax employee contributions, and employers may make nonelective or matching contributions on behalf of employees. Contributions to a section 403(b) plan are generally subject to the same contribution limits applicable to qualified defined contribution plans, including the limits on elective deferrals.

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[2] Elective deferrals generally are made on a pre-tax basis and distributions attributable to elective deferrals are includible in income. However, a section 401(k) plan is permitted to include a "qualified Roth contribution program" that permits a participant to elect to have all or a portion of the participant's elective deferrals under the plan treated as after-tax Roth contributions. Certain distributions from a designated Roth account are excluded from income, even though they include earnings not previously taxed.

[3] Sec. 402(g).

[4] Sec. 414(v).

[5] These are organizations exempt from tax under section 501(c)(3). Section 403(b) plans of private, tax-exempt employers may be subject to ERISA as well as the requirements of section 403(b).

[6] Sec. 403(b).

Automatic enrollment

Section 401(k) plans and section 403(b) plans must provide each eligible employee with an effective opportunity to make or change an election to make elective deferrals at least once each plan year.[7] Whether an employee has an effective opportunity is determined based on all the relevant facts and circumstances, including the adequacy of notice of the availability of the election, the period of time during which an election may be made, and any other conditions on elections.

Section 401(k) plans, and section 403(b) plans that have salary reduction arrangements, are generally designed so that an employee will receive cash compensation unless the employee affirmatively elects to make elective deferrals to the plan. Alternatively, such plans may provide that elective deferrals are made at a specified rate (when the employee becomes eligible to participate) unless the employee elects otherwise (*i.e.*, affirmatively elects not to make contributions or to make contributions at a different rate). This alternative plan design is referred to as automatic enrollment.

Nondiscrimination test and automatic enrollment safe harbor

An annual nondiscrimination test, called the actual deferral percentage test (the "ADP" test) applies to elective deferrals under a section 401(k) plan.[8] The ADP test generally compares the average rate of deferral for highly compensated employees to the average rate of deferral for non-highly compensated employees and requires that the average deferral rate for highly compensated employees not exceed the average rate for non-highly compensated employees by more than certain specified amounts. If a plan fails to satisfy the ADP test for a plan year based on the deferral elections of highly compensated employees, the plan is permitted to distribute deferrals to highly compensated employees ("excess deferrals") in a sufficient amount to correct the failure. The distribution of the excess deferrals must be made by the close of the following plan year.[9]

The ADP test is deemed to be satisfied if a section 401(k) plan includes certain minimum matching or nonelective contributions under either of two plan designs (a "section 401(k) safe harbor plan"), as well as certain required rights and features, and satisfies a notice requirement.[10] One type of section 401(k) safe harbor plan includes automatic enrollment.

An automatic enrollment section 401(k) safe harbor plan must provide that, unless an employee elects otherwise, the employee is treated as electing to make elective deferrals at a default rate equal to a percentage of compensation as stated in the plan and at least (1) three percent of compensation for the first year the deemed election applies to the participant, (2) four

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[7] Treas. Reg. secs. 1.401(k)-1(e)(2)(ii); 1.403(b)-5(b)(2).

[8] Sec. 401(k)(3).

[9] Sec. 401(k)(8).

[10] Sec. 401(k)(12) and (13). If certain additional requirements are met, matching contributions under a section 401(k) safe harbor plan may also satisfy a nondiscrimination test applicable under section 401(m).

percent during the second year, (3) five percent during the third year, and (4) six percent during the fourth year and thereafter. Although an automatic enrollment section 401(k) safe harbor plan generally may provide for default rates higher than these minimum rates, the default rate cannot exceed 15 percent for any year.

Eligible automatic contribution arrangements

Plans that include eligible automatic contribution arrangements may allow participants to withdraw certain elective contributions ("permissive withdrawals").[11] For this purpose, an eligible automatic contribution arrangement is an arrangement under an employer plan[12] that meets the following conditions: (1) a participant under the arrangement may elect to have the employer make payments as contributions under the plan on behalf of the participant, or to the participant directly in cash; (2) the participant is treated as having elected to have the employer make such contributions in an amount equal to a uniform percentage of compensation provided under the plan until the participant specifically elects not to have such contributions made (or specifically elects to have such contributions made at a different percentage); and (3) the administrator of the plan meets certain notice requirements described below.[13]

A permissive withdrawal is an election by the employee to withdraw elective contributions described in clause (2) above (and earnings attributable thereto). Such withdrawals are excludable from the employee's gross income for that taxable year and are not subject to the 10-percent additional tax[14] on early distributions from a retirement plan. The employee's election to make a permissive withdrawal must be made no later than 90 days after the date of the employee's first elective contribution under the arrangement.

Under the notice requirements, the administrator must, within a reasonable period before each plan year, give to each employee to whom the eligible automatic contribution arrangement applies a notice of the employee's rights and obligations under the arrangement which (1) is sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and (2) is written in a manner calculated to be understood by the average employee to whom the arrangement applies. The notice must describe the level of the default electronic contributions that will be made on the employee's behalf if the employee does not make an affirmative election.[15] It also must include an explanation of the employee's right under the arrangement to elect not to have elective contributions made on the employee's behalf (or to elect to have such contributions made at a different percentage), as well as an explanation of how contributions

[11] For this purpose, elective contributions are elective deferrals under section 402(g) or contributions to certain governmental plans (as described in Treas. Reg. sec. 1.457-2(f)) that would be elective contributions if they were made under a qualified plan. Treas. Reg. sec. 1.414(w)-1(e)(4).

[12] The employer plan must be one of the following: a plan qualified under section 401(a); a section 403(b) plan; a governmental section 457(b) plan; a simplified employer pension ("SEP") under section 408(k)(6) that provides for a salary reduction arrangement; or a SIMPLE IRA, as defined in section 408(p).

[13] Sec. 414(w)(3).

[14] Under section 72(t).

[15] Treas. Reg. sec. 1.414(w)-1(b)(3)(ii).

made under the arrangement will be invested in the absence of any investment election by the employee. If the plan allows permissive withdrawals, it must explain the employee's right to make such a withdrawal and describe the procedures to elect such withdrawal. In addition, the employee must have a reasonable period of time after receipt of the notice and before the first elective contribution is made to make an election with respect to such contributions.[16]

Description of Proposal

The proposal generally requires existing section 401(k) plans and section 403(b) plans with salary reduction agreements to provide for automatic enrollment.[17] Such plans must include an eligible automatic contribution arrangement that allows employees to make permissive withdrawals,[18] and that meets requirements relating to the minimum contribution percentage and the investment of the employee's contributions.

Under the minimum contribution percentage requirements, the eligible automatic contribution arrangement must provide that the uniform percentage of compensation contributed by the participant during the first year of participation is at least three percent, and that such percentage increases by one percentage point each year to at least 10 percent (but no more than 15 percent), unless the participant specifically elects not to have such contributions made or to have them made at a different percentage. For a plan other than a section 401(k) safe harbor plan, the percentage of compensation contributed under the eligible automatic contribution arrangement (other than due to a participant's election to change such percentage) may not be greater than 10 percent in any plan year ending before January 1, 2025.

The percentage increase under the eligible automatic contribution arrangement must be effective as of the first day of the first plan year commencing after the completion of each year of participation. In addition, under the investment requirements, amounts contributed pursuant to such arrangement for which no investment is elected by the participant must be invested consistent with certain Department of Labor regulations under which a participant is treated as exercising control over the assets in the participant's account with respect to certain default investments.[19]

Certain plans are exempt from the requirements of the proposal. First, the proposal does not apply to plans established before the date of enactment. However, this grandfathering rule does not apply in the case of an employer adopting a multiple employer plan after the date of enactment. Second, governmental plans[20] and church plans[21] are exempt from the proposal. Third, the proposal does not apply to a plan while the employer maintaining the plan has been in

[16] Sec. 414(w)(4).

[17] SIMPLE section 401(k) plans (section 401(k)(11)) are not subject to the requirements of this proposal.

[18] As defined in section 414(w)(2).

[19] 29 C.F.R. sec. 2550.404c-5, or any successor regulations.

[20] Within the meaning of section 414(d).

[21] Within the meaning of section 414(e).

existence for less than three years. And fourth, the proposal does not apply to a plan earlier than the date that is one year after the close of the first taxable year with respect to which the employer maintaining the plan normally employed more than 10 employees. In the case of a multiple employer plan, the exemptions relating to new employers and to small employers apply separately with respect to each employer.

Effective Date

The proposal is effective for plan years beginning after December 31, 2022.

2. Modification of credit for small employer pension plan start-up costs

Present Law

Present law provides a nonrefundable income tax credit equal to 50 percent of the qualified start-up costs paid or incurred during the taxable year by an eligible employer[22] that adopts a new eligible employer plan[23], provided that the plan covers at least one nonhighly compensated employee.[24] Qualified start-up costs are expenses connected with the establishment or administration of the plan and retirement-related education of employees with respect to the plan. The amount of the credit for any taxable year is limited to the greater of (1) $500 or (2) the lesser of (a) $250 multiplied by the number of nonhighly compensated employees of the eligible employer who are eligible to participate in the plan or (b) $5,000. The credit applies for up to three consecutive taxable years beginning with the taxable year the plan is first effective, or, at the election of the employer, with the year preceding the first plan year.

An eligible employer is an employer that, for the preceding year, had no more than 100 employees, each with compensation of $5,000 or more.[25] In addition, the employer must not have had a qualified employer plan covering substantially the same employees as the new plan with respect to which contributions were made or benefits were accrued during the three years preceding the first year for which the credit would apply. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[26] All eligible employer plans of an employer are treated as a single plan.

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[22] An eligible employer has the meaning given such term by section 408(p)(2)(C)(i).

[23] An eligible employer plan means a qualified employer plan within the meaning of section 4972(d) and includes a section 401(a) qualified retirement plan, a section 403 annuity, any simplified employee pension ("SEP") within the meaning of section 408(k), and any simple retirement account ("SIMPLE") within the meaning of section 408(p). An eligible employer plan does not include a plan maintained by a tax-exempt employer or a governmental plan, as defined in section 414(d).

[24] A nonhighly compensated employee is an employee who is not a highly compensated employee as defined under section 414(q).

[25] As defined in section 408(p)(2)(C).

[26] Secs. 52(a) or (b) and 414(m) or (o).

No deduction is allowed for the portion of qualified start-up costs paid or incurred for the taxable year equal to the amount of the credit.

Description of Proposal

The proposal increases from 50 percent to 100 percent of qualified start-up costs, the amount of the nonrefundable income tax credit allowed to an eligible employer with no more than 50 employees.

The proposal also increases by an additional amount up to $1,000 per employee the credit allowed to any employer who is eligible, as determined in the first taxable year in which the plan is established. The additional amount of the credit is equal to the applicable percentage of employer contributions (not including any elective deferrals) by the employer to an eligible employer plan (not including a defined benefit plan). The applicable percentages are as follow:

Taxable Year	Applicable Percentage
Taxable year in which the plan is established	100
1st taxable year after the taxable year in which the plan is established	100
2nd taxable year after the taxable year in which the plan is established	75
3rd taxable year after the taxable year in which the plan is established	50
4th taxable year after the taxable year in which the plan is established	25
Any taxable years thereafter	0

In the case of an eligible employer which had more than 50 employees in the year preceding the taxable year in which the plan is established, the amount of the additional credit is reduced by an amount equal to two percent for each employee above 50 employees and is zero for eligible employers with 100 or more employees.

No deduction is allowed for the portion of qualified start-up costs paid or incurred or for the portion of employer contributions for the taxable year equal to the increased amounts of the credit.

Effective Date

The proposal applies to taxable years beginning after December 31, 2021.

3. Promotion of the Saver's Credit

Present Law

Present law provides a nonrefundable income tax credit for eligible taxpayers who make qualified retirement savings contributions.[27] Subject to AGI limits, the credit is available to individuals who are 18 or older, other than individuals who are full-time students or claimed as a dependent on another taxpayer's return. The AGI limits for 2021 (as indexed for inflation) are $66,000 for married taxpayers filing joint returns, $49,500 for head of household taxpayers, and $33,000 for single taxpayers and married taxpayers filing separate returns.

For purposes of the credit, qualified retirement savings contributions include (1) elective deferrals to a section 401(k) plan, a section 403(b) plan, a governmental section 457 plan, a SIMPLE IRA, or a SEP; (2) contributions to a traditional or Roth IRA; (3) voluntary after-tax employee contributions to a qualified retirement plan or annuity or a section 403(b) plan; (4) contributions to a 501(c)(18)(D) plan; and (6) contributions made to an ABLE account for which the taxpayer is the designated beneficiary. The maximum amount of qualified retirement savings contributions taken into account for purposes of the credit is $2,000. The amount of any contribution eligible for the credit is reduced by distributions received by the taxpayer (or by the taxpayer's spouse if the taxpayer files a joint return with the spouse) from any plan or IRA to which eligible contributions can be made during the taxable year for which the credit is claimed, the two taxable years prior to the year the credit is claimed, and during the period after the end of the taxable year for which the credit is claimed and prior to the due date for filing the taxpayer's return for the year. Distributions that are rolled over to another retirement plan do not affect the credit.

The credit is a percentage of the taxpayer's qualified retirement savings contributions up to $2,000. The credit percentage may be 10 percent, 20 percent, or 50 percent, depending on the AGI of the taxpayer, as shown in the table below. The credit is in addition to any deduction or exclusion that would otherwise apply with respect to the contribution. The credit offsets minimum tax liability as well as regular tax liability.

Table 1.–Credit Rates for Saver's Credit (for 2021)

Joint Filers	Heads of Households	All Other Filers	Credit Rate
$0 – $39,500	$0 – $29,625	$0 – $19,750	50 percent
$39,501 – $43,000	$29,626 – $32,250	$19,751 – $21,500	20 percent
$43,001 – $66,000	$32,251 – $49,500	$21,501 – $33,000	10 percent

[27] Sec. 25B.

Description of Proposal

Under the proposal, the Secretary shall take steps to increase public awareness of the benefits provided under this section and not later than 90 days after the date of enactment provide a report to Congress summarizing anticipated promotion efforts. The report will include a description of plans for the development and distribution of digital and print materials as well as the translation of such materials into the ten most commonly spoken languages as determined by data from the U.S. Census Bureau, American Community Survey.

Effective Date

The proposal applies to taxable years beginning after the date of enactment.

4. Enhancement of 403(b) Plans

Present Law

Tax-sheltered annuities ("section 403(b) plans")

Section 403(b) plans are a form of tax-favored employer-sponsored plan that provides tax benefits similar to qualified retirement plans. Section 403(b) plans may be maintained only by (1) charitable tax-exempt organizations, and (2) educational institutions of State or local governments (that is, public schools, including colleges and universities). Many of the rules that apply to section 403(b) plans are similar to the rules applicable to qualified retirement plans, including section 401(k) plans.

Contributions to 403(b) plans

Employers may make nonelective or matching contributions to such plans on behalf of their employees, and the plan may provide for employees to make pre-tax elective deferrals, designated Roth contributions (held in designated Roth accounts)[28] or other after-tax contributions.

Annuity contracts

Generally, section 403(b) plans provide for contributions toward the purchase of annuity contracts. The employee's rights under the annuity contract are nonforfeitable, except for a failure to pay future premiums.[29] Amounts contributed by an employer for an annuity contract are excluded from the gross income of the employee for the taxable year if certain requirements are satisfied.

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[28] Sec. 402A.

[29] Sec. 403(b)(1)(C).

Section 403(b) Custodial Accounts

Alternatively, such contributions may be held in custodial accounts established for each employee if those accounts satisfy certain requirements.

Contributions to a section 403(b) plan that are held in a custodial account are treated as contributions to an annuity contract[30] if the assets are (1) held by a bank[31] or another person who demonstrates, to the satisfaction of the Secretary, that the manner in which the assets will be held is consistent with the requirements for a qualified retirement plan[32] and (2) invested only in regulated investment company stock.[33]

In addition, assets of a section 403(b) custodial account cannot be commingled in a group trust with any assets other than those of a regulated investment company.[34] Contributions to a custodial account are not permitted to be distributed before: the employee dies; attains age 59½; has a severance from employment; becomes disabled;[35] with respect to lifetime income options, the date that is 90 days prior to the date such lifetime income investment no longer is held as an investment option and is distributed in the form of a qualified distribution;[36] or, in the case of elective deferrals, encounters financial hardship. Finally, a custodial account must contain a written statement that the assets held in a custodial account cannot be used for, or diverted to, purposes other than for the exclusive benefit of plan participants and their beneficiaries.[37]

Group trust

Under the Code, a trust created or organized in the United States and forming a part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of its employees or their beneficiaries constitutes a qualified trust if it provides that:

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[30] Sec. 403(b)(7).

[31] A "bank" is defined as any bank as defined in section 581, an insured credit union within the meaning of section 101, paragraph (6) or (7) of the Federal Credit Union Act, and a corporation which, under the laws of the State of its incorporation, is subject to supervision and examination by the Commissioner of Banking or other officer of such State in charge of the administration of the banking laws of such State. Sec. 408(n).

[32] Sec. 401(f)(2) and Treas. Reg. sec. 1.401(f)-1. A custodial account that satisfies the requirements of section 401(f)(2) is treated as an organization described in section 401(a) solely for purposes of subchapter F of chapter 1 of Subtitle A (secs. 501-530) and subtitle F (pertaining to procedure and administration) with respect to amounts received by the account and with respect to any income from the investment of those amounts.

[33] Sec. 403(b)(7) and Treas. Reg. sec. 1.403(b)-8(d)(2)(i).

[34] Treas. Reg. sec. 1.403(b)-8(d)(2)(ii).

[35] Within the meaning of sec. 72(m)(7).

[36] In accordance with section 401(a)(38).

[37] Treas. Reg. sec. 1.403(b)-8(d)(2)(iii).

- Contributions made to the trust by the applicable employer or employers, or both, are used for the purpose of distributing the corpus and income of the trust, in accordance with the terms of the plan, to such employees or their beneficiaries;[38]
- A trust described in section 401(a) is exempt from income tax;[39] and
- Under each trust instrument, it must be impossible, at any time prior to the satisfaction of all liabilities with respect to employees and their beneficiaries under the plan and trust, for any part of the corpus or income of the trust to be used for or diverted to purposes other than for the exclusive benefit of the employees or their beneficiaries.

A group trust is an arrangement under which individual retirement plan trusts pool their assets in a group trust (usually created for the purpose of providing diversification of investments), where the trust is declared to be part of each participating retirement plan and the trust instruments creating both the participating and group trusts provide that amounts are transferred from one trust to the other at the direction of the trustee of the participating trust.[40]

The tax status of the group trust is derived from the tax status of the entities participating in the group trust to the extent of the entities' equitable interests in such trust if the following requirements are satisfied:

- The group trust is itself adopted as a part of each adopting group trust retiree benefit plan;
- The group trust instrument expressly limits participation to pension, profit-sharing, and stock bonus trusts or custodial accounts qualifying under section 401(a) that are exempt under section 501(a); individual retirement accounts that are exempt under section 408(e); eligible governmental plan trusts or custodial accounts under section 457(b) that are exempt under section 457(g); custodial accounts under section 403(b)(7); retirement income accounts under section 403(b)(9); and section 401(a)(24) governmental plans;
- The group trust instrument expressly prohibits any part of its corpus or income that equitably belongs to any adopting group trust retiree benefit plan from being used for, or diverted to, any purpose other than for the exclusive benefit of the participants and beneficiaries of the group trust retiree benefit plan;
- Each group trust retiree benefit plan that adopts the group trust is itself a trust, a custodial account, or a similar entity that is tax-exempt under section 408(e) or section 501(a) (or is treated as exempt under section 501(a));

[38] Sec. 401(a)(1).

[39] Sec. 501(a).

[40] See Rev. Rul. 81-100, 1981-1 C.B. 326, as modified by Rev. Rul. 2004-67, 2004-2 C.B. 28; Rev. Rul. 2008-40, 2008-2 C.B. 166; Rev. Rul. 2011-1, 2011-2 I.R.B. 251 which was modified by Notice 2012-6, 2012-3 I.R.B. 293, January 17, 2012; and Rev. Rul. 2014-24, 2014-37 I.R.B. 529.

- Each group trust retiree benefit plan that adopts the group trust expressly provides in its governing document that it is impossible for any part of the corpus or income of the group trust retiree benefit plan to be used for, or diverted to, purposes other than for the exclusive benefit of the plan participants and their beneficiaries;
- The group trust instrument expressly limits the assets that may be held by the group trust to assets that are contributed by, or transferred from, a group trust retiree benefit plan to the group trust (and the earnings thereon), and the group trust instrument expressly provides for separate accounting to reflect the interest that each adopting group trust retiree benefit plan has in the group trust, including separate accounting for contributions to the group trust from the adopting plan, disbursements made from the adopting plan's account in the group trust, and investment experience of the group trust allocable to that account;
- The group trust instrument expressly prohibits an assignment by an adopting group trust retiree benefit plan of any part of its equity or interest in the group trust; and
- The group trust is created or organized in the United States and is maintained at all times as a domestic trust in the United States.

With respect to section 403(b)(7) custodial accounts, under Internal Revenue Service ("IRS") guidance, such an account fails to satisfy the requirements for a group trust if the assets of the account are invested other than in the stock of a regulated investment company, and any group trust in which the assets of a section 403(b)(7) custodial account is invested must comply with this restriction.[41] As a result of this investment restriction, the assets of a custodial account under section 403(b)(7) generally will be commingled in a group trust that solely contains the assets of other section 403(b)(7) custodial accounts.

Description of Proposal

The proposal provides that contributions to a section 403(b) plan that are held in a custodial account are treated as contributions to an annuity contract if the assets are to be held in that custodial account and invested in regulated investment company stock or a group trust intended to satisfy the requirements of IRS Revenue Ruling 81-100 (or any successor guidance). In other words, the proposal does not restrict a section 403(b)(7) custodial account to being invested solely in regulated investment company stock.

Effective Date

The proposal is applicable to amounts invested after December 31, 2021.

[41] Rev. Rul. 2011-1, 2011-2 I.R.B. 251.

5. Increase in age for required beginning date for mandatory distributions

Present Law

Required minimum distributions

Employer-provided qualified retirement plans and IRAs are subject to required minimum distribution rules.[42] A qualified retirement plan for this purpose means a tax-qualified plan described in section 401(a) (such as a defined benefit pension plan or a section 401(k) plan), an employee retirement annuity described in section 403(a), a tax-sheltered annuity described in section 403(b), and a plan described in section 457(b) that is maintained by a governmental employer.[43] An employer-provided qualified retirement plan that is a defined contribution plan is a plan that provides (1) an individual account for each participant and (2) for benefits based on the amount contributed to the participant's account and any income, expenses, gains, losses, and forfeitures of accounts of other participants which may be allocated to such participant's account.[44]

Required minimum distributions generally must begin by April 1 of the calendar year following the calendar year in which the individual (employee or IRA owner) reaches age 72. Prior to January 1, 2020, the age after which required minimum distributions were required to begin was 70½.[45] In the case of an employer-provided qualified retirement plan, the required minimum distribution date for an individual who is not a five-percent owner of the employer maintaining the plan may be delayed to April 1 of the year following the year in which the individual retires, if the plan provides for this later distribution date. For all subsequent years, including the year in which the individual was paid the first required minimum distribution by April 1, the individual must take the required minimum distribution by December 31.

For IRAs and defined contribution plans, the required minimum distribution for each year generally is determined by dividing the account balance as of the end of the prior year by the number of years in the distribution period.[46] The distribution period is generally derived from the Uniform Lifetime Table.[47] This table is based on the joint life expectancies of the individual and a hypothetical beneficiary 10 years younger than the individual. For an individual with a spouse as designated beneficiary who is more than 10 years younger, the joint life expectancy of

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[42] Secs. 401(a)(9) and 408(a)(6).

[43] The required minimum distribution rules also apply to section 457(b) plans maintained by tax-exempt employers other than governmental employers.

[44] Sec. 414(i).

[45] The Setting Every Community Up for Retirement Enhancement Act of 2019 ("SECURE Act"), enacted as part of the Further Consolidated Appropriations Act, 2020, Pub. L. No. 116-94, Div. O, sec. 114, increased the age after which required minimum distribution must begin from 70½ to 72, effective for distributions required to be made after December 31, 2019, with respect to individuals who attain age 70½ after that date.

[46] Treas. Reg. sec. 1.401(a)(9)-5.

[47] Treas. Reg. sec. 1.401(a)(9)-9.

the couple is used (because the couple's remaining joint life expectancy is longer than the length provided in the Uniform Lifetime Table). There are special rules in the case of annuity payments from an insurance contract.

If an individual dies before the individual's entire interest is distributed, and the individual has a designated beneficiary, unless the designated beneficiary is an eligible designated beneficiary, the individual's entire account must be distributed within 10 years after the individual's death. This rule applies regardless of whether the individual dies before or after the individual's required beginning date.

In the case of an eligible designated beneficiary, the remaining required minimum distributions are distributed over the life of the beneficiary (or over a period not extending beyond the life expectancy of such beneficiary). Such distributions must begin no later than December 31 of the calendar year immediately following the calendar year in which the individual dies. An eligible designated beneficiary is a designated beneficiary who is (1) the surviving spouse of the individual; (2) a child of the individual who has not reached majority; (3) disabled; (4) chronically ill; or (5) not more than 10 years younger than the individual.[48] If the eligible designated beneficiary is the individual's spouse, commencement of distributions is permitted to be delayed until December 31 of the calendar year in which the deceased individual would have attained age 72. The required minimum distribution for each year is determined by dividing the account balance as of the end of the prior year by a distribution period, which is determined by reference to the beneficiary's life expectancy.[49] Special rules apply in the case of trusts for disabled or chronically ill beneficiaries.[50]

In the case of an individual who does not have a designated beneficiary, if an individual dies on or after the individual's required beginning date, the distribution period for the remaining required minimum distributions is equal to the remaining years of the deceased individual's single life expectancy, using the age of the deceased individual in the year of death.[51] If an individual dies before the required beginning date, the individual's entire account must be distributed no later than December 31 of the calendar year that includes the fifth anniversary of the individual's death.[52]

A special after-death rule applies for an IRA if the beneficiary of the IRA is the surviving spouse. The surviving spouse is permitted to choose to calculate required minimum distributions both while the surviving spouse is alive and after death as though the surviving spouse is the IRA owner, rather than a beneficiary.[53]

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[48] Sec. 401(a)(9)(E)(ii).

[49] Treas. Reg. sec. 1.401(a)(9)-5, A-5.

[50] Sec. 401(a)(9)(H)(iv).

[51] Treas. Reg. sec. 1.401(a)(9)-5, A-5(a).

[52] Treas. Reg. sec. 1.401(a)(9)-3, Q&As 1, 2.

[53] Treas. Reg. sec. 1.408-8, Q&A 5.

Roth IRAs are not subject to the minimum distribution rules during the IRA owner's lifetime. However, Roth IRAs are subject to the post-death minimum distribution rules that apply to traditional IRAs. For Roth IRAs, the IRA owner is treated as having died before the individual's required beginning date.

Failure to make a required minimum distribution triggers a 50-percent excise tax, payable by the individual or the individual's beneficiary. The tax is imposed during the taxable year that begins with or within the calendar year during which the distribution was required.[54] The tax may be waived if the failure to distribute is reasonable error and reasonable steps are taken to remedy the violation.[55]

Eligible rollover distributions

With certain exceptions, distributions from an employer-provided qualified retirement plan are eligible to be rolled over tax free into another employer-provided qualified retirement plan or an IRA. This can be achieved by contributing the amount of the distribution to the other plan or IRA within 60 days of the distribution, or by a direct payment by the plan to the other plan or IRA (referred to as a "direct rollover"). Distributions that are not eligible for rollover include (i) any distribution that is one of a series of periodic payments generally for a period of 10 years or more (or a shorter period for distributions made for certain life expectancies), and (ii) any distribution to the extent that the distribution is a required minimum distribution.[56]

For any distribution that is eligible for rollover, an employer-provided qualified retirement plan must offer the distributee the right to have the distribution made in a direct rollover.[57] Before making the distribution, the plan administrator must provide the distributee with a written explanation of the direct rollover right and related tax consequences.[58] Unless a distributee elects to have the distribution made in a direct rollover, the distribution is generally subject to mandatory 20-percent income tax withholding.[59]

Description of Proposal

The proposal changes the age on which the required beginning date for required minimum distributions is based, from the calendar year in which the employee or IRA owner attains age 72 to the calendar year in which the employee or IRA owner attains age 73, for individuals who attain age 72 after December 31, 2021, and who attain age 73 before January 1,

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[54] Sec. 4974(a).

[55] Sec. 4974(d).

[56] Sec. 402(c)(4). Distributions that are not eligible rollover distributions also include distributions made upon hardship of the employee.

[57] Sec. 401(a)(31).

[58] Sec. 402(f).

[59] Sec. 3405(c). This mandatory withholding does not apply to a distributee that is a beneficiary other than a surviving spouse of an employee.

2029. In addition, the proposal changes such age from 73 years to 74 years, for individuals who attain age 73 after December 31, 2028, and who attain age 74 before January 1, 2032. Such age is further increased to age 75 for individuals who attain age 74 after December 31, 2031.

Effective Date

The proposal is effective for distributions required to be made after December 31, 2021, for employees and IRA owners who attain age 72 after such date.

6. Indexing IRA catch-up limit

Present Law

There are two general types of individual retirement arrangements ("IRAs"): traditional IRAs and Roth IRAs.[60] The total amount that an individual may contribute to one or more IRAs for a year is generally limited to the lesser of: (1) a dollar amount ($6,000 for 2021); and (2) the amount of the individual's compensation that is includible in gross income for the year.[61] In the case of an individual who has attained age 50 by the end of the taxable year, the dollar amount is increased by $1,000 (referred to as a "catch-up contribution"). In the case of a married couple, contributions can be made up to the dollar limit for each spouse if the combined compensation of the spouses that is includible in gross income is at least equal to the contributed amount. An individual may make contributions to a traditional IRA (up to the contribution limit) without regard to his or her adjusted gross income.

An individual may deduct his or her contributions to a traditional IRA if neither the individual nor the individual's spouse is an active participant in an employer-sponsored retirement plan. If an individual or the individual's spouse is an active participant in an employer-sponsored retirement plan, the deduction is phased out for taxpayers with adjusted gross income over certain levels.[62]

Individuals with adjusted gross income below certain levels may make contributions to a Roth IRA (up to the contribution limit).[63] Contributions to a Roth IRA are not deductible.

Description of Proposal

Under the proposal, the $1,000 amount that may be contributed as a catch-up contribution by individuals who attain age 50 by the end of the taxable year is increased for cost-of-living adjustments for taxable years beginning in 2023 or later.

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[60] Secs. 408 and 408A.

[61] Sec. 219(b)(2) and (5), as referenced in secs. 408(a)(1) and (b)(2)(B) and 408A(c)(2). Under section 4973, IRA contributions in excess of the applicable limit are generally subject to an excise tax of six percent per year until withdrawn.

[62] Sec. 219(g).

[63] Sec. 408A(c)(3).

Effective Date

The proposal applies to taxable years beginning after December 31, 2022.

7. Higher catch-up limit to apply at age 62, 63, and 64

Present Law

Under certain types of employer-sponsored retirement plans, including section 401(k) plans, section 403(b) plans, SIMPLE IRAs,[64] and governmental section 457(b) plans, an employee may elect to have contributions (elective deferrals) made to the plan, rather than receive the same amount in cash. The maximum annual amount of elective deferrals that can be made by an employee for a year is $19,500 for 2021 ($13,500 in the case of a SIMPLE IRA or SIMPLE section 401(k) plan[65]) or, if less, the employee's compensation.[66] For individuals who will attain age 50 by the end of the taxable year, this limit is increased to allow additional "catch-up contributions."[67]

A section 401(k) plan, section 403(b) plan, and governmental section 457(b) plan may generally permit catch-up contributions up to $6,500 in 2021 (indexed for inflation). A SIMPLE IRA or SIMPLE section 401(k) plan may permit catch-up contributions up to $3,000 in 2021. If elective deferral and catch-up contributions are made to both a section 401(k) plan and a section 403(b) plan for the same employee, a single limit applies to the elective deferrals under both plans. Special contribution limits apply to certain employees under a section 403(b) plan maintained by a church. In addition, under a special catch-up rule, an increased elective deferral limit applies under a plan maintained by an educational organization, hospital, home health service agency, health and welfare service agency, church, or convention or association of churches in the case of employees who have completed 15 years of service. In this case, the limit is increased by the least of (1) $3,000, (2) $15,000, reduced by the employee's total elective deferrals in prior years, and (3) $5,000 times the employee's years of service, reduced by the employee's total elective deferrals in prior years.

The section 457(b) plan limits apply separately from the combined limit applicable to section 401(k) and section 403(b) plan contributions, so that an employee covered by a governmental section 457(b) plan and a section 401(k) or section 403(b) plan can contribute the full amount to each plan. In addition, under a special catch-up rule, for one or more of the participant's last three years before normal retirement age, the otherwise applicable limit is increased to the lesser of (1) two times the normal annual limit ($39,000 for 2021) or (2) the sum

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[64] Sec. 408(p).

[65] Sec. 401(k)(11).

[66] Secs. 402(g); 457(c). This limit applies to total elective deferrals under all of a participant's section 401(k) plans and section 403(b) plans but applies separately to any governmental section 457(b) plan. Sec. 414(v).

[67] Sec. 414(v).

of the otherwise applicable limit for the year plus the amount by which the limit applicable in preceding years of participation exceeded the deferrals for that year.

Catch-up contributions are not subject to any other contribution limits and are not taken into account in applying other contribution limits. In addition, such contributions are not subject to applicable nondiscrimination rules. However, a plan fails to meet the applicable nondiscrimination requirements under section 401(a)(4) with respect to benefits, rights, and features unless the plan allows all eligible individuals participating in the plan to make the same election with respect to catch-up contributions. For purposes of this rule, all plans of related employers are treated as a single plan. In addition, the special nondiscrimination rule for mergers and acquisitions applies for this purpose.[68]

An employer is permitted to make matching contributions with respect to catch-up contributions. Any such matching contributions are subject to the normally applicable rules.

Description of Proposal

Under the proposal, the limit on catch-up contributions is increased for individuals who have attained age 62, 63, or 64 (but who are not older than 64) by the end of the taxable year. A section 401(k) plan (other than a SIMPLE section 401(k) plan), section 403(b) plan, or governmental section 457(b) plan may increase the limit on catch-up contributions for such individuals to the lesser of (1) $10,000 or (2) the participant's compensation for the year reduced by any other elective deferrals of the participant for the year.[69] A SIMPLE section 401(k) plan or a SIMPLE IRA may increase the limit on catch-up contributions for such individuals to the lesser of (1) $5,000 or (2) the participant's compensation for the year reduced by any other elective deferrals of the participant for the year. Both the $10,000 amount and the $5,000 amount are indexed for inflation beginning in 2023.

Effective Date

The provision applies to taxable years beginning after December 31, 2022.

8. Multiple Employer 403(b) Plans

Present Law

Retirement savings under the Code and ERISA

The Code provides tax-favored treatment for various types of retirement plans, including employer-sponsored plans IRAs. Code provisions are generally within the jurisdiction of the Secretary of the Treasury (the "Secretary"), through his or her delegate, the IRS.

[68] Secs. 410(b)(6)(C); 414(v)(4)(B).

[69] This increase also applies to catch-up contributions under a simplified employee pension under section 408(k) that includes a salary reduction arrangement.

The most common type of tax-favored employer-sponsored retirement plan is a qualified retirement plan,[70] which may be a defined contribution plan or a defined benefit plan. Under a defined contribution plan, separate individual accounts are maintained for participants, to which accumulated contributions, earnings, and losses are allocated, and participants' benefits are based on the value of their accounts.[71] Defined contribution plans commonly allow participants to direct the investment of their accounts, usually by choosing among investment options offered under the plan. Under a defined benefit plan, benefits are determined under a plan formula and paid from general plan assets, rather than individual accounts.[72] Besides qualified retirement plans, certain tax-exempt employers and public schools may maintain tax-deferred annuity plans.[73]

An IRA is generally established by the individual for whom the IRA is maintained.[74] However, in some cases, an employer may establish IRAs on behalf of employees and provide retirement contributions to the IRAs.[75] In addition, IRA treatment may apply to accounts maintained for employees under a trust created by an employer (or an employee association) for the exclusive benefit of employees or their beneficiaries, provided that the trust complies with the relevant IRA requirements and separate accounting is maintained for the interest of each employee or beneficiary (referred to herein as an "IRA trust").[76] In that case, the assets of the trust may be held in a common fund for the account of all individuals who have an interest in the trust.

Tax-sheltered annuities ("section 403(b) plans")

Section 403(b) plans are a form of tax-favored employer-sponsored plan that provide tax benefits similar to qualified retirement plans. Section 403(b) plans may be maintained only by

[70] Sec. 401(a). A qualified annuity plan under section 403(a) is similar to and subject to requirements similar to those applicable to qualified retirement plans.

[71] Sec. 414(i). Defined contribution plans generally provide for contributions by employers and may include a qualified cash or deferred arrangement under a section 401(k) plan, under which employees may elect to contribute to the plan.

[72] Sec. 414(j).

[73] Sec. 403(b). Private and governmental employers that are exempt from tax under section 501(c)(3), including tax-exempt private schools, may maintain tax-deferred annuity plans. State and local governmental employers may maintain another type of tax-favored retirement plan, an eligible deferred compensation plan under section 457(b).

[74] Sections 219, 408 and 408A provide rules for IRAs. Under section 408(a)(2) and (n), only certain entities are permitted to be the trustee of an IRA. The trustee of an IRA generally must be a bank, an insured credit union, or a corporation subject to supervision and examination by the Commissioner of Banking or other officer in charge of the administration of the banking laws of the State in which it is incorporated. Alternatively, an IRA trustee may be another person who demonstrates to the satisfaction of the Secretary that the manner in which the person will administer the IRA will be consistent with the IRA requirements.

[75] Simplified employee pension ("SEP") plans under section 408(k) and SIMPLE IRA plans under section 408(p) are employer-sponsored retirement plans funded using IRAs for employees.

[76] Sec. 408(c).

(1) charitable tax-exempt organizations, and (2) educational institutions of State or local governments (that is, public schools, including colleges and universities).

Many of the rules that apply to section 403(b) plans are similar to the rules applicable to qualified retirement plans, including section 401(k) plans. Section 403(b) plans are generally subject to the minimum coverage and nondiscrimination rules that apply to qualified defined contribution plans. However, as in the case of a qualified retirement plan, a governmental section 403(b) plan is not subject to the nondiscrimination rules.

Contributions to section 403(b) plans

Employers may make nonelective or matching contributions to such plans on behalf of their employees, and the plan may provide for employees to make pre-tax elective deferrals, designated Roth contributions (held in designated Roth accounts)[77] or other after-tax contributions.

Annuity contracts

Generally, section 403(b) plans provide for contributions toward the purchase of annuity contracts for providing retirement benefits for their employees. The employee's rights under the annuity contract are nonforfeitable, except for a failure to pay future premiums.[78] Section 403(b) generally provides that amounts contributed by an employer for an annuity contract are excluded from the gross income of the employee for the taxable year if certain requirements are satisfied.

403(b) Custodial Accounts

Alternatively, such contributions may be held in custodial accounts established for each employee if those accounts satisfy certain requirements.

Contributions to a section 403(b) plan that are held in a custodial account are treated as contributions to an annuity contract[79] if the assets (1) are held by a bank[80] or another person who demonstrates, to the satisfaction of the Secretary, that the manner in which the assets will be held

[77] Sec. 402A.

[78] Sec. 403(b)(1)(C).

[79] Sec. 403(b)(7).

[80] A "bank" is defined as any bank as defined in section 581, an insured credit union within the meaning of section 101, paragraph (6) or (7) of the Federal Credit Union Act, and a corporation which, under the laws of the State of its incorporation, is subject to supervision and examination by the Commissioner of Banking or other officer of such State in charge of the administration of the banking laws of such State. Sec. 408(n).

is consistent with the requirements for a qualified retirement plan[81] and (2) are invested only in regulated investment company stock.[82]

Retirement Income Accounts

Assets of a section 403(b) plan generally must be invested in annuity contracts or mutual funds.[83] However, the restrictions on investments do not apply to a retirement income account, which is a type of 403(b) plan that is a defined contribution program established or maintained by a church, or a convention or association of churches, to provide benefits under the plan to employees of a religious, charitable or similar tax-exempt organization.[84]

Certain rules prohibiting discrimination in favor of highly compensated employees, which apply to section 403(b) plans generally, do not apply to a plan maintained by a church or qualified church-controlled organization.[85] For this purpose, church means a church, a convention or association of churches, or an elementary or secondary school that is controlled, operated, or principally supported by a church or by a convention or association of churches, and includes a qualified church-controlled organization. A qualified church-controlled organization is any church-controlled tax-exempt organization other than an organization that (1) offers goods, services, or facilities for sale, other than on an incidental basis, to the general public, other than goods, services, or facilities that are sold at a nominal charge substantially less than the cost of providing the goods, services, or facilities, and (2) normally receives more than 25 percent of its support from either governmental sources, or receipts from admissions, sales of merchandise, performance of services, or furnishing of facilities, in activities that are not unrelated trades or businesses, or from both. Church-controlled organizations that are not qualified church-controlled organizations are generally referred to as "nonqualified church-controlled organizations."

[81] Sec. 401(f)(2) and Treas. Reg. sec. 1.401(f)-1. A custodial account that satisfies the requirements of section 401(f)(2) is treated as an organization described in section 401(a) solely for purposes of subchapter F of chapter 1 of Subtitle A (secs. 501-530) and subtitle F (pertaining to procedure and administration) with respect to amounts received by the account and with respect to any income from the investment of those amounts.

[82] Sec. 403(b)(7) and Treas. Reg. sec. 1.403(b)-8(d)(2)(i).

[83] Sec. 403(b)(1)(A) and (7).

[84] Sec. 403(b)(9)(B), referring to organizations exempt from tax under section 501(c)(3). For this purpose, a church or a convention or association of churches includes an organization described in section 414(e)(3)(A), that is, an organization, the principal purpose or function of which is the administration or funding of a plan or program for the provision of retirement benefits or welfare benefits, or both, for the employees of a church or a convention or association of churches, provided that the organization is controlled by, or associated with, a church or a convention or association of churches.

[85] Sec. 403(b)(1)(D) and (12).

Church plans

A church plan is a plan established and maintained for employees (or their beneficiaries) by the church or by a convention or association of churches that is exempt from tax.[86] Church plans include plans maintained by an organization, whether a corporation or otherwise, that has as its principal purpose or function the administration or funding of a plan or program for providing retirement or welfare benefits for the employees of the church or convention or association of churches.[87]

ERISA

Retirement plans of private employers, including qualified retirement plans and tax-deferred annuity plans, are generally subject to requirements under the Employee Retirement Income Security Act of 1974 ("ERISA").[88] A plan covering only business owners (or business owners and their spouses)—that is, it covers no other employees—is exempt from ERISA.[89] Thus, a plan covering only self-employed individuals is exempt from ERISA. Tax-deferred annuity plans that provide solely for salary reduction contributions by employees may be exempt from ERISA.[90] IRAs are generally exempt from ERISA.

The provisions of Title I of ERISA are under the jurisdiction of the Secretary of Labor.[91] Many of the requirements under Title I of ERISA parallel Code requirements for qualified retirement plans. Under ERISA, in carrying out provisions relating to the same subject matter, the Secretary (of the Treasury) and the Secretary of Labor are required to consult with each other and develop rules, regulations, practices, and forms that, to the extent appropriate for efficient administration, are designed to reduce duplication of effort, duplication of reporting, conflicting or overlapping requirements, and the burden of compliance by plan administrators, employers, and participants and beneficiaries.[92] In addition, interpretive jurisdiction over parallel Code and

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[86] Sec. 414(e). The plan is exempt from tax under sec. 501.

[87] Sec. 414(e)(3)(A). With respect to certain provisions (*e.g.*, the exemption for church plans from nondiscrimination rules applicable for tax-sheltered annuities), the more limited definition of church under the employment-tax rules applies (secs. 3121(w)(3)(A) and (B)).

[88] ERISA applies to employee welfare benefit plans, such as health plans, of private employers, as well as to employer-sponsored retirement (or pension) plans. Employer-sponsored welfare and pension plans are both referred to under ERISA as employee benefit plans. Under ERISA sec. 4(b)(1) and (2), governmental plans and church plans are generally exempt from ERISA.

[89] 29 C.F.R. sec. 2510.3-3(b)-(c).

[90] 29 C.F.R. sec. 2510.3-2(f).

[91] The provisions of Title I of ERISA are codified at 29 U.S.C. 1001-734. Under Title IV of ERISA, defined benefit plans of private employers are generally covered by the Pension Benefit Guaranty Corporation's pension insurance program.

[92] ERISA sec. 3004.

ERISA provisions relating to retirement plans is divided between the two Secretaries by an Executive Order, referred to as the Reorganization Plan No. 4 of 1978.[93]

Certain church plans are exempt from the coverage, vesting, funding, and fiduciary requirements of ERISA ("non-electing" churches). Church plans may waive this exemption by election.[94] Electing plans become subject to all section 401(a) qualification requirements, title I of ERISA, and the excise tax on prohibited transactions.[95] Such plans participate in the termination insurance program administered by the Pension Benefit Guaranty Corporation ("PBGC").

Fiduciary and bonding requirements

Among other requirements, ERISA requires a plan to be established and maintained pursuant to a written instrument (that is, a plan document) that contains certain terms.[96] The terms of the plan must provide for one or more named fiduciaries that jointly or severally have authority to control and manage the operation and administration of the plan.[97] Among other required plan terms are a procedure for the allocation of responsibilities for the operation and administration of the plan and a procedure for amending the plan and for identifying the persons who have authority to amend the plan. Among other permitted terms, a plan may provide also that any person or group of persons may serve in more than one fiduciary capacity with respect to the plan (including service both as trustee and administrator) and that a person who is a named fiduciary with respect to the control or management of plan assets may appoint an investment manager or managers to manage plan assets.

In general, a plan fiduciary is responsible for the investment of plan assets. However, a special rule applies in the case of a defined contribution plan that permits participants to direct the investment of their individual accounts.[98] Under the special rule, if various requirements are met, a participant is not deemed to be a fiduciary by reason of directing the investment of the participant's account and no person who is otherwise a fiduciary is liable for any loss, or by reason of any breach, that results from the participant's investments. Defined contribution plans that provide for participant-directed investments commonly offer a set of investment options

[93] 43 Fed. Reg. 47713 (October 17, 1978).

[94] Section 4(b)(2) of ERISA excepts a church plan (as defined in section 3(3) of ERISA) with respect to which no election has been made under Code section 410(d) from the provisions of Title I of ERISA (including the fiduciary, participation and vesting, and funding rules).

[95] Sec. 4975.

[96] ERISA sec. 402.

[97] Fiduciary is defined in ERISA section 3(21), and named fiduciary is defined in ERISA section 402(a)(2).

[98] ERISA sec. 404(c). Under ERISA, a defined contribution plan is also referred to as an individual account plan.

among which participants may choose. The selection of investment options to be offered under a plan is subject to ERISA fiduciary requirements.

Under ERISA, any plan fiduciary or person that handles plan assets is required to be bonded, generally for an amount not to exceed $500,000.[99] In some cases, the maximum bond amount is $1 million, rather than $500,000.

Tax-sheltered annuity plans under ERISA

ERISA generally applies to section 403(b) plans maintained by tax-exempt organizations.

However, there is an exception from ERISA for certain tax-sheltered annuity programs established by tax-exempt entities which consist of a program for the purchase of an annuity contract or the establishment of a custodial account pursuant to salary reduction agreements or agreements to forego an increase in salary where the tax-exempt entity has very limited involvement. Under the program: (1) participation is completely voluntary for employees, (2) all rights under the annuity contract or custodial account are enforceable solely by the employee, and (3) the employer's sole involvement in the program is limited to the following, for example: (a) permitting annuity contractors to publicize their products to employees, (b) requesting information concerning proposed funding, media, products, or annuity contracts, (c) summarizing or otherwise compiling information provided, (d) collecting annuity or custodial account contributions, or (e) holding in the employer's name, one or more group annuity contracts covering the employees; and (4) for which the employer receives no direct or indirect consideration or compensation.[100]

Section 403(b) plans sponsored by governmental and public education employers are generally not subject to ERISA.

Similarly, non-electing church plans funded through section 403(b) annuities are generally not subject to ERISA.[101]

Multiple employer plans under the Code

In general

Qualified retirement plans, either defined contribution or defined benefit plans, are categorized as single employer plans or multiple employer plans ("MEPs"). A single employer plan is a plan maintained by one employer. For this purpose, businesses and organizations that

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[99] ERISA sec. 412.

[100] 29 C.F.R. sec. 2510.3-2(f).

[101] However, whether or not they are maintained by a church, plans that are funded through tax-deferred custodial accounts are subject to annual reporting requirements and to the duty to report distributions of $600 or more. This is because such an account constitutes a "funded plan of deferred compensation described in part I of subchapter D of chapter 1." Sec. 6058, 6041; Treas. Reg. sec. 301.6058-1(a)(2).

are members of a controlled group of corporations, a group under common control, or an affiliated service group are treated as one employer (referred to as "aggregation").[102]

A MEP generally is a single plan maintained by two or more unrelated employers (that is, employers that are not treated as a single employer under the aggregation rules).[103] MEPs are commonly maintained by employers in the same industry and are used also by professional employer organizations ("PEOs") to provide qualified retirement plan benefits to employees working for PEO clients.[104]

There is no specific provision in the Code that provides for section 403(b) plans maintained by more than one employer.[105]

Application of Code requirements to MEPs

Some requirements are applied to a MEP on a plan-wide basis.[106] For example, all employees covered by the plan are treated as employees of all employers participating in the plan for purposes of the exclusive benefit rule. Similarly, an employee's service with all participating employers is taken into account in applying the minimum participation and vesting requirements. In applying the limits on contributions and benefits, compensation, contributions, and benefits attributable to all employers are taken into account.[107] Other requirements are applied separately, including the minimum coverage requirements, nondiscrimination requirements (both the general requirements and the special tests for section 401(k) plans), and the top-heavy rules.[108]

"One bad apple" rule

The qualified status of the plan as a whole is determined with respect to all employers maintaining the plan, and the failure by one employer (or by the plan itself) to satisfy an

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[102] Sec. 414(b), (c), (m) and (o).

[103] Sec. 413(c). Multiple employer status does not apply if the plan is a multiemployer plan. Multiemployer plans are different from single employer plans and MEPs. A multiemployer plan is defined under section 414(f) as a plan maintained pursuant to one or more collective bargaining agreements with two or more unrelated employers and to which the employers are required to contribute under the collective bargaining agreement(s). Multiemployer plans are also known as Taft-Hartley plans.

[104] Rev. Proc. 2003-86, 2003-2 C.B. 1211, and Rev. Proc. 2002-21, 2002-1 C.B. 911, address the application of the MEP rules to qualified defined contribution plans maintained by PEOs.

[105] Section 413(c) provides rules governing MEPs subject to sections 401(a), 410(a) and 411, in other words tax-qualified retirement plans, but does not apply those rules to section 403(b) plans.

[106] Sec. 413(c).

[107] Treas. Reg. sec. 1.415(a)-1(e).

[108] Treas. Reg. secs. 1.413-2(a)(3)(ii)-(iii) and 1.416-1, G-2.

applicable qualification requirement may result in disqualification of the plan with respect to all employers (sometimes referred to as the "one bad apple" rule).[109]

The Setting Every Community Up for Retirement Enhancement (the "SECURE Act") provided relief from the "one bad apple" rule under the Code for certain MEPs.[110] MEPs that satisfy certain requirements (referred to herein as "covered MEP") may avoid the consequences of the "one bad apple rule." A "covered MEP" is a multiple employer qualified defined contribution plan[111] or a plan that consists of IRAs (referred to herein as an "IRA plan"), including under an IRA trust,[112] that either (1) is maintained by employers which have a common interest other than having adopted the plan, or (2) in the case of a plan not described in (1), has a pooled plan provider (referred to herein as a "pooled provider plan"),[113] and which meets certain other requirements as described below.

Relief from the "one bad apple" rule does not apply to a plan unless the terms of the plan provide that, in the case of any employer in the plan failing to take required actions (referred to herein as a "noncompliant employer"):

- plan assets attributable to employees of the noncompliant employer (or beneficiaries of such employees) will be transferred to a plan maintained only by that employer (or its successor), to a tax-favored retirement plan for each individual whose account is transferred,[114] or to any other arrangement that the Secretary determines is appropriate, unless the Secretary determines it is in the best interests of the employees of the noncompliant employer (and beneficiaries of such employees) to retain the assets in the plan, and
- the noncompliant employer (and not the plan with respect to which the failure occurred or any other employer in the plan) is, except to the extent provided by the Secretary, liable for any plan liabilities attributable to employees of the noncompliant employer (or beneficiaries of such employees).

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[109] Treas. Reg. sec. 1.413-2(a)(3)(iv).

[110] Sec. 101 of Div. O. of Pub. L. No. 116-94, the Further Consolidated Appropriations Act, 2020, December 20, 2019. With respect to plans described under section 413(e)(1)(A), other than providing relief from the "one bad apple" rule if certain requirements are met and adding certain reporting requirements, the provision generally did not change present law and related guidance applicable to such MEPs under the Code or ERISA.

[111] To which section 413(c) applies.

[112] In applying the exclusive benefit requirement under section 408(c) to an IRA plan with an IRA trust covering employees of unrelated employers, all employees covered by the plan are treated as employees of all employers participating in the plan.

[113] Sec. 413(e)(1).

[114] For this purpose, a tax-favored retirement plan means an eligible retirement plan as defined in section 402(c)(8)(B), that is, an IRA, a qualified retirement plan, a tax-deferred annuity plan under section 403(b), or an eligible deferred compensation plan of a State or local governmental employer under section 457(b).

In addition, in the case of a pooled provider plan, if the pooled plan provider does not perform substantially all the administrative duties required of the provider (as described below) for any plan year, the Secretary may provide that the determination as to whether the plan meets the Code requirements for tax-favored treatment will be made in the same manner as would be made without regard to the relief under the provision.

MEP status under ERISA

Like the Code, ERISA contains rules for multiple employer retirement plans.[115] However, a different concept of MEP applies under ERISA.

Under ERISA, an employee benefit plan (whether a pension plan or a welfare plan) must be sponsored by an employer, by an employee organization, or by both.[116] The definition of employer is any person acting directly as an employer, or indirectly in the interest of an employer, in relation to an employee benefit plan, and includes a group or association of employers acting for an employer in such capacity.[117]

Historically, these definitional provisions of ERISA have been interpreted as only permitting a MEP to be established or maintained by a cognizable, bona fide group or association of employers, acting in the interests of its employer members to provide benefits to their employees.[118] This approach is based on the premise that the person or group that maintains the plan is tied to the employers and employees that participate in the plan by some common economic or representational interest or genuine organizational relationship unrelated to the provision of benefits. Based on the facts and circumstances, the employers that participate in the benefit program must, either directly or indirectly, exercise control over that program, both in form and in substance, in order to act as a bona fide employer group or association with respect to the program, or the plan is sponsored by one or more employers as defined in section 3(5) of ERISA.[119] However, an employer association does not exist where several unrelated employers merely execute participation agreements or similar documents as a means to fund benefits, in the absence of any genuine organizational relationship between the employers. In that case, each participating employer establishes and maintains a separate employee benefit plan for the benefit of its own employees, rather than a MEP.

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[115] ERISA sec. 210(a).

[116] ERISA secs. 3(1) and (2).

[117] ERISA sec. 3(5).

[118] See, *e.g.*, Department of Labor Advisory Opinions 2012-04A, 2003-17A, 2001-04A, and 1994-07A, and other authorities cited therein.

[119] See, *e.g.*, Department of Labor Advisory Opinion 2017-02AC.

DOL MEP Regulations

On July 31, 2019, the Department of Labor ("DOL") issued final regulations[120] pursuant to Executive Order 13847[121] which had directed the DOL to consider within 180 days whether to issue a notice of proposed rulemaking, other guidance, or both, that would clarify when a group or association of employers or other appropriate business or organization could be an "employer" under ERISA.[122] The final regulation focuses its scope on MEPs sponsored by either a group or association of employers or by a PEO and is limited to defined contribution plans.[123] The final regulation does not deal with pooled employer plans.

The final regulation recognizes that a bona fide group or association of employers may establish a MEP if such group or association meets the following requirements: (1) the primary purpose of the group or association may be to provide MEP coverage to its employer members and their employees, but there must also be at least one substantial business purpose unrelated to offering and providing MEP coverage or other employee benefits to the employer members and their employees; (2) each employer member of the group or association is a person acting directly as an employer of at least one employee who is a participant covered under the plan; (3) the group or association has a formal organizational structure with a governing body and has by-laws or other similar indications of formality; (4) the functions and activities of the group or association are controlled by its employer members, and the group's or association's employer members that participate in the plan control (in form and in substance) the plan; (5) the employer members have a commonality of interest; (6) plan participation is only permitted to employees and former employees of employer members, and their beneficiaries; and (7) the group or association is not a bank or trust company, insurance issuer, broker-dealer or other similar financial services firm. Under the final regulation, a bona fide PEO may establish a MEP. Certain "working owners" may also establish a MEP.

403(b) Plans under ERISA

There is no specific provision in ERISA that provides for 403(b) plans maintained by more than one employer .[124]

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[120] 84 Fed. Reg. 37508, July 31, 2019. DOL noted in the preamble to the final regulations that these final regulations differ significantly from the legislative proposals introduced in Congress, including the SECURE Act which "makes comprehensive changes to ERISA and the Code to facilitate open MEPs." DOL indicates that the final rule is significantly more limited in scope because it relies solely on the Department's authority to promulgate regulations administering title I of ERISA and unlike Congress, DOL does not have the authority to make statutory changes to ERISA and other areas of law that govern retirement savings such as the Code.

[121] 83 Fed. Reg. 45321, September 6, 2018. The Executive Order was issued on August 31, 2018.

[122] Within the meaning of ERISA sec. 3(5).

[123] As defined in section 3(34) of ERISA.

[124] ERISA section 210 provides rules related to MEPs. Section 29 C.F.R. sec. 2530.210(c) defines the term "multiple employer plan" to mean a MEP within the meaning of sections 413(b) and (c) of the Code and the regulations thereafter, and as previously noted, those rules are applicable to plans subject to sections 401(a), 410(a) and 411.

“Pooled” MEPs under the Code and ERISA

As described above, the SECURE Act provided relief from the “one bad apple” rule under the Code for certain MEPs. The SECURE Act also introduced the concept of a “pooled” MEP for purposes of the Code and ERISA. Various requirements apply to a “pooled provider plan” under the Code, with similar, but not identical, requirements applying under ERISA.

Pooled provider plan

A “pooled provider plan” is a qualified defined contribution plan that is established or maintained for the purpose of providing benefits to the employees of a MEP administered by a “pooled plan provider.” A pooled provider plan does not include a plan maintained by employers that have a common interest other than having adopted the plan.

In the case of a pooled provider plan, if the pooled plan provider does not perform substantially all the administrative duties required of the provider (as described below) for any plan year, the Secretary may provide that the determination as to whether the plan meets the Code requirements for tax-favored treatment will be made in the same manner as would be made without regard to the relief under the provision.

Pooled plan provider

A “pooled plan provider” with respect to a plan means a person that:

- is designated by the terms of the plan as a named fiduciary under ERISA,[125] as the plan administrator, and as the person responsible to perform all administrative duties (including conducting proper testing with respect to the plan and the employees of each employer in the plan) that are reasonably necessary to ensure that the plan meets the Code requirements for tax-favored treatment and the requirements of ERISA and to ensure that each employer in the plan takes actions as the Secretary or the pooled plan provider determines necessary for the plan to meet Code and ERISA requirements, including providing to the pooled plan provider any disclosures or other information that the Secretary may require or that the pooled plan provider otherwise determines are necessary to administer the plan or to allow the plan to meet Code and ERISA requirements,
- registers with the Secretary as a pooled plan provider and provides any other information that the Secretary may require, before beginning operations as a pooled plan provider,
- acknowledges in writing its status as a named fiduciary under ERISA and as the plan administrator, and
- is responsible for ensuring that all persons who handle plan assets or are plan fiduciaries are bonded in accordance with ERISA requirements.

[125] Within the meaning of ERISA section 402(a)(2).

The Secretary may perform audits, examinations, and investigations of pooled plan providers as may be necessary to enforce and carry out the purposes of the statute.

In addition, in determining whether a person meets the requirements to be a pooled plan provider with respect to any plan, all persons who perform services for the plan and who are treated as a single employer[126] are treated as one person.

Plan sponsor

Except with respect to the administrative duties (as a named fiduciary, as the plan administrator, and as the person responsible for the performance of all administrative duties) for which the pooled plan provider is responsible as described above, each employer in a plan which has a pooled plan provider is treated as the plan sponsor with respect to the portion of the plan attributable to that employer's employees (or beneficiaries of such employees).

Guidance

The Secretary is directed to issue guidance (that the Secretary determines appropriate) (1) to identify the administrative duties and other actions required to be performed by a pooled plan provider, (2) that describes the procedures to be taken to terminate a plan that fails to meet the requirements to be a covered MEP, including the proper treatment of, and actions needed to be taken by, any employer in the plan and plan assets and liabilities attributable to employees of that employer (or beneficiaries of such employees), and (3) to identify appropriate cases in which corrective action will apply with respect to noncompliant employers. For purposes of (3), the Secretary is to take into account whether the failure of an employer or pooled plan provider to provide any disclosures or other information, or to take any other action, necessary to administer a plan or to allow a plan to meet the Code requirements for tax-favored treatment, has continued over a period of time that demonstrates a lack of commitment to compliance. An employer or pooled plan provider is not treated as failing to meet a requirement of guidance issued by the Secretary if, before the issuance of such guidance, the employer or pooled plan provider complies in good faith with a reasonable interpretation of the provisions to which the guidance relates.

The Secretary is directed to publish model plan language that meets the Code and ERISA requirements and that may be adopted in order for the plan to be treated as a pooled employer plan under ERISA.

The Secretary (or the Secretary's delegate) has the authority to provide for the proper treatment of a failure to meet any Code requirement with respect to any employer (and its employees) in a MEP.

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[126] Under subsection (b), (c), (m), or (o) of section 414.

Pooled employer plans under ERISA

In general

A pooled employer plan is treated for purposes of ERISA as a single plan that is a MEP. A "pooled employer plan" is a qualified defined contribution plan that is established or maintained for the purpose of providing benefits to the employees of two or more employers, that meets certain requirements in order to be treated for purposes of ERISA as a single plan that is a MEP. A pooled employer plan does not include a plan maintained by employers that have a common interest other than having adopted the plan.

In order for a plan to be a pooled employer plan, the plan terms must:

- designate a pooled plan provider and provide that the pooled plan provider is a named fiduciary of the plan;
- designate one or more trustees (other than an employer in the plan)[127] to be responsible for collecting contributions to, and holding the assets of, the plan, and require the trustees to implement written contribution collection procedures that are reasonable, diligent, and systematic;
- provide that each employer in the plan retains fiduciary responsibility for the selection and monitoring, in accordance with ERISA fiduciary requirements, of the person designated as the pooled plan provider and any other person who is also designated as a named fiduciary of the plan, and, to the extent not otherwise delegated to another fiduciary by the pooled plan provider (and subject to the ERISA rules relating to self-directed investments), the investment and management of the portion of the plan's assets attributable to the employees of that employer (or beneficiaries of such employees) in the plan;
- provide that employers in the plan, and participants and beneficiaries, are not subject to unreasonable restrictions, fees, or penalties with regard to ceasing participation, receipt of distributions, or otherwise transferring assets of the plan in accordance with applicable rules for plan mergers and transfers;
- require the pooled plan provider to provide to employers in the plan any disclosures or other information that the Secretary of Labor may require, including any disclosures or other information to facilitate the selection or any monitoring of the pooled plan provider by employers in the plan, and require each employer in the plan to take any actions that the Secretary of Labor or pooled plan provider determines are necessary to administer the plan or to allow for the plan to meet the ERISA and Code requirements applicable to the plan, including providing any disclosures or other information that the Secretary of Labor may require or that the pooled plan provider otherwise determines are necessary to administer the plan or to allow the plan to meet such ERISA and Code requirements; and

[127] Any trustee must meet the requirements under the Code to be an IRA trustee.

- provide that any disclosure or other information required to be provided as described above may be provided in electronic form and will be designed to ensure only reasonable costs are imposed on pooled plan providers and employers in the plan.

In the case of a fiduciary of a pooled employer plan or a person handling assets of a pooled employer plan, the maximum bond amount under ERISA is $1 million.

The term "pooled employer plan" does not include a multiemployer plan. Such term also does not include a plan established before the date of enactment of the SECURE Act unless the plan administrator elects to have the plan treated as a pooled employer plan and the plan meets the ERISA requirements applicable to a pooled employer plan established on or after such date.

Pooled plan provider

The definition of pooled plan provider for ERISA purposes is generally similar to the definition under the Code, described above.[128] The ERISA definition requires a person to register as a pooled plan provider with the Secretary of Labor and provide any other information that the Secretary of Labor may require before beginning operations as a pooled plan provider.

The Secretary of Labor may perform audits, examinations, and investigations of pooled plan providers as may be necessary to enforce and carry out the purposes of the statute.

Plan sponsor

Except with respect to the administrative duties (as a named fiduciary, as the plan administrator, and as the person responsible for the performance of all administrative duties) for which the pooled plan provider is responsible as described above, each employer in a pooled employer plan will be treated as the plan sponsor with respect to the portion of the plan attributable to that employer's employees (or beneficiaries of such employees).

Guidance

The Secretary of Labor is to issue guidance that he or she determines appropriate (1) to identify the administrative duties and other actions required to be performed by a pooled plan provider,[129] and (2) that requires, in appropriate cases of a noncompliant employer, plan assets attributable to employees of the noncompliant employer (or beneficiaries of such employees) to be transferred to a plan maintained only by that employer (or its successor), to a tax-favored retirement plan for each individual whose account is transferred, or to any other arrangement that

[128] In determining whether a person meets the requirements to be a pooled plan provider with respect to a plan, all persons who perform services for the plan and who are treated as a single employer under subsection (b), (c), (m), or (o) of section 414 are treated as one person.

[129] The DOL has issued guidance on registering as a pooled plan provider. See 85 Fed. Reg. 72934, November 16, 2020. (29 C.F.R. sec. 2510.3-44).

the Secretary of Labor determines in the guidance is appropriate,[130] and the noncompliant employer (and not the plan with respect to which the failure occurred or any other employer in the plan) to be liable for any plan liabilities attributable to employees of the noncompliant employer (or beneficiaries of such employees), except to the extent provided in the guidance. For purposes of (2), the Secretary of Labor is to take into account whether the failure of an employer or pooled plan provider to provide any disclosures or other information, or to take any other action, necessary to administer a plan or to allow a plan to meet the requirements of ERISA and the Code requirements for tax-favored treatment, has continued over a period of time that demonstrates a lack of commitment to compliance. An employer or pooled plan provider is not treated as failing to meet a requirement of guidance issued by the Secretary if, before the issuance of such guidance, the employer or pooled plan provider complies in good faith with a reasonable interpretation of the provisions to which the guidance relates.

Form 5500 reporting

Under the Code, an employer maintaining a qualified retirement plan generally is required to file an annual return containing information required under regulations with respect to the qualification, financial condition, and operation of the plan.[131] ERISA requires the plan administrator of certain pension and welfare benefit plans to file annual reports disclosing certain information to the DOL.[132] These filing requirements are met by filing a completed Form 5500, Annual Return/Report of Employee Benefit Plan. Forms 5500 are filed with DOL, and information from Forms 5500 is shared with the IRS.[133]

In the case of a MEP (including a pooled employer plan), the Form 5500 filing must include a list of participating employers in the plan; a good faith estimate of the percentage of total contributions made by the participating employers during the plan year; and the aggregate account balances attributable to each employer in the plan (determined as the sum of the account balances of the employees of each employer (and the beneficiaries of such employees)); and with respect to a pooled employer plan, the identifying information for the person designated under the terms of the plan as the pooled plan provider. The Secretary of Labor may prescribe

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[130] The Secretary of Labor may waive the requirement to transfer assets to another plan or arrangement in appropriate circumstances if the Secretary of Labor determines it is in the best interests of the employees of the noncompliant employer (and the beneficiaries of such employees) to retain the assets in the pooled employer plan.

[131] Sec. 6058. In addition, under section 6059, the plan administrator of a defined benefit plan subject to the minimum funding requirements is required to file an annual actuarial report. Under section 414(g) and ERISA section 3(16), plan administrator generally means the person specifically so designated by the terms of the plan document. In the absence of a designation, the plan administrator generally is (1) in the case of a plan maintained by a single employer, the employer, (2) in the case of a plan maintained by an employee organization, the employee organization, or (3) in the case of a plan maintained by two or more employers or jointly by one or more employers and one or more employee organizations, the association, committee, joint board of trustees, or other similar group of representatives of the parties that maintain the plan. Under ERISA, the party described in (1), (2), or (3) is referred to as the "plan sponsor."

[132] ERISA secs. 103 and 104. Under ERISA section 4065, the plan administrator of certain defined benefit plans must provide information to the PBGC.

[133] Information is shared also with the PBGC, as applicable. Form 5500 filings are also publicly released in accordance with section 6104(b) and Treas. Reg. sec. 301.6104(b)-1 and ERISA sections 104(a)(1) and 106(a).

simplified reporting for a MEP that covers fewer than 1,000 participants, but only if no single employer in the plan has 100 or more participants covered by the plan.

Description of Proposal

Section 403(b) MEPs under the Code

In general

The proposal clarifies that a section 403(b) plan may be established and maintained as a MEP. Specifically, it provides that, except in the case of a church plan, section 403(b) annuity contracts and 403(b) custodial accounts[134] do not fail to qualify as section 403(b) plans solely by reason of such contracts being purchased or accounts being established under a plan maintained by more than one employer.

For purposes of this proposal, a section 403(b) plan includes such a plan sponsored by (1) tax-exempt entities (described in section 501(c)(3) which is exempt from tax under section 501(a)) and (2) public schools (including state colleges and universities).

Relief from "one bad apple" rule

Under the proposal, as long as such a section 403(b) plan maintained by more than one employer satisfies rules similar to certain rules that apply to qualified retirement MEPs,[135] the section 403(b) plan will not fail to be treated as such merely because one or more employers of employees covered by the plan fail to meet the requirements of section 403(b). The rules applicable to qualified retirement MEPs require that where one or more employers of employees covered by the MEP fails to meet the applicable qualification requirements:

- the assets of the plan attributable to employees of such employer (or beneficiaries of such employees) will be transferred to a plan maintained only by such employer (or its successor), to an eligible retirement plan[136] for each individual whose account is transferred, or to any other arrangement that the Secretary determines is appropriate, unless the Secretary determines it is in the best interests of the employees of such employer (and the beneficiaries of such employees) to retain the assets in the plan, and
- such employer (and not the plan with respect to which the failure occurred or any other employer in such plan) will, except to the extent provided by the Secretary, be

[134] Sec. 403(b)(7) provides that amounts paid by a tax-exempt employer to a custodial account which satisfies the requirements of section 401(f)(2) shall be treated as amounts contributed by him for an annuity contract for his employee if the amounts are to be invested in regulated investment company stock to be held in that custodial account.

[135] Under section 413(e)(2).

[136] As defined in section 402(c)(8)(B).

liable for any liabilities with respect to such plan attributable to employees of such employer (or beneficiaries of such employees).

In addition, in the case of a section 403(b) plan maintained by tax-exempt entities, such plans must also meet either the commonality rule[137] or have a pooled plan provider. This requirement does not apply to plans maintained by governmental employers.

Section 403(b) MEPs under ERISA

The proposal:

- Amends the definition of pooled employer plan under ERISA[138] to include a section 403(b) MEP that meets the applicable requirements under the Code (as added by this proposal).[139]
- It also amends the requirements relating to plan terms for pooled employer plans to permit, in the case of section 403(b) plans, fiduciaries other than trustees to hold certain responsibilities relating to plan assets.[140]

Disclosure Rules

Special disclosure rules for tax-exempt employers joining a section 403(b) MEP

As noted above, there is an exception from ERISA for certain tax-sheltered annuity programs established by tax-exempt entities which consist of a program for the purchase of annuity contracts or the establishment of custodial accounts pursuant to salary reduction agreements or agreements to forego an increase in salary where the tax-exempt entity has very limited involvement in the program. However, if a tax-exempt employer who had participated in such a non-ERISA program decides to become a participating employer in a section 403(b) MEP, that employer will become subject to ERISA because of the fiduciary responsibilities imposed on each employer in a section 403(b) MEP.

To ensure that such tax-exempt employers are aware of their ERISA fiduciary duties, the proposal imposes additional disclosure to such employers. First, the proposal directs the Secretary (or the Secretary's delegate) to modify the model plan language applicable to qualified retirement MEPs[141] to include language which notifies participating tax-exempt employers that the plan is subject to ERISA and that each such employer is a plan sponsor with respect to its employees participating in the MEP, and, as such, has certain fiduciary duties with respect to the plan and the employees. Second, Treasury must undertake necessary education and outreach

[137] Sec. 413(e)(1)(A).

[138] ERISA sec. 3(43)(A).

[139] Under sec. 403(b)(15), as added by this proposal.

[140] ERISA sec. 3(43)(B)(ii).

[141] Sec. 413(e)(5).

efforts to increase awareness to tax-exempt employers that MEPs are subject to ERISA, that such employers are plan sponsors with respect to their employees participating in the MEP and, as such, have certain fiduciary duties with respect to the plan and to its employees.

Other disclosures

The proposal also provides that the Secretary also publish model plan language similar to the model plan language published for qualified plan MEPs[142] for section 403(b) MEPs sponsored by nongovernmental employers.

Reporting requirements for section 403(b) MEPs

In the case of any annuity contract described in section 403(b) that is a MEP, such plan shall be treated as a single plan for purposes of the reporting requirements under the Code relating to the annual registration statement and the annual return for certain plans[143] As a result, the plan can file a single Form 8955-SSA, Annual Registration Statement Identifying Separated Participants With Deferred Vested Benefits, and a single Form 5500, Annual Return/Report of Employee Benefit Plan, rather than having each participating employer in the section 403(b) MEP file their own form. These filing requirements only apply to tax-exempt employers because governmental employers are not subject to ERISA.

Regulations

The Secretary (or the Secretary's designee) must prescribe such regulations as may be necessary to clarify the treatment of a plan termination by an employer in the case of section 403(b) MEPs.[144]

No inference with respect to church plans

The proposal provides that regarding any application of section 403(b) to an annuity contract purchased under a church plan,[145] maintained by more than one employer, or to any application of rules similar to the rules that apply to qualified retirement MEPs[146] to such a plan, no inference is to be made from the rules applicable to section 403(b) MEPs not applying to such plans.

[142] Under section 413(e)(5).

[143] The reporting requirement relating to the annual registration statement is under section 6057, and the requirement relating to the annual return is under 6058. These requirements only apply in the case of a section 403(b) plan that is otherwise subject to such requirements.

[144] As described in section 403(b)(15).

[145] As defined in section 414(e).

[146] Sec. 413(e).

Effective Date

The proposal is generally effective for plan years beginning after December 31, 2021.

Nothing in the amendments made by the general rule is to be construed as limiting the authority of the Secretary or the Secretary's delegate (determined without regard to such amendment) to provide for the proper treatment of a failure to meet any requirement applicable under such Code with respect to one employer (and its employees) in the case of a section 403(b) MEP.[147]

9. Treatment of student loan payments as elective deferrals for purposes of matching contributions

Present Law

Section 401(k) plans

A section 401(k) plan is a type of profit-sharing or stock bonus plan that contains a qualified cash or deferred arrangement. Such arrangements are subject to the rules generally applicable to qualified defined contribution plans. In addition, special rules apply to such arrangements. Employees who participate in a section 401(k) plan may elect to have contributions made to the plan (referred to as "elective deferrals") rather than receive the same amount as current compensation.[148] The maximum annual amount of elective deferrals that can be made by an employee for a year is $19,500 (for 2021) or, if less, the employee's compensation.[149] For an employee who attains age 50 by the end of the year, the dollar limit on elective deferrals is increased by $6,500 (for 2021) (called "catch-up contributions").[150] An employee's elective deferrals must be fully vested. A section 401(k) plan may also provide for employer matching and nonelective contributions.

In order to constitute a qualified cash or deferred arrangement, no benefit under the arrangement may be conditioned, directly or indirectly, on the employee electing to have the employer make or not make contributions under the arrangement in lieu of receiving cash.[151] However, matching contributions are exempt from this rule.

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[147] As described in section 403(b)(15).

[148] Elective deferrals generally are made on a pre-tax basis and distributions attributable to elective deferrals are includible in income. However, a section 401(k) plan is permitted to include a "qualified Roth contribution program" that permits a participant to elect to have all or a portion of the participant's elective deferrals under the plan treated as after-tax Roth contributions. Certain distributions from a designated Roth account are excluded from income, even though they include earnings not previously taxed.

[149] Sec. 402(g).

[150] Sec. 414(v).

[151] Sec. 401(k)(4)(A).

Nondiscrimination test

Actual deferral percentage test

An annual nondiscrimination test, called the actual deferral percentage test (the "ADP" test) applies to elective deferrals under a section 401(k) plan.[152] The ADP test generally compares the average rate of deferral for highly compensated employees to the average rate of deferral for non-highly compensated employees and requires that the average deferral rate for highly compensated employees not exceed the average rate for non-highly compensated employees by more than certain specified amounts. If a plan fails to satisfy the ADP test for a plan year based on the deferral elections of highly compensated employees, the plan is permitted to distribute deferrals to highly compensated employees ("excess deferrals") in a sufficient amount to correct the failure. The distribution of the excess deferrals must be made by the close of the following plan year.[153]

The ADP test is deemed to be satisfied if a section 401(k) plan includes certain minimum matching or nonelective contributions under either of two plan designs ("401(k) safe harbor plan"), described below, as well as certain required rights and features and the plan satisfies a notice requirement.[154]

Section 401(k) safe harbor contributions

Under one type of 401(k) safe harbor plan ("basic 401(k) safe harbor plan"), the plan either (1) satisfies a matching contribution requirement ("matching contribution basic 401(k) safe harbor plan") or (2) provides for the employer to make a nonelective contribution to a defined contribution plan of at least three percent of an employee's compensation on behalf of each non-highly compensated employee who is eligible to participate in the plan ("nonelective basic 401(k) safe harbor plan"). The matching contribution requirement under the matching contribution basic 401(k) safe harbor requires a matching contribution equal to at least 100 percent of elective contributions of the employee for contributions not in excess of three percent of compensation, and 50 percent of elective contributions for contributions that exceed three percent of compensation but do not exceed five percent, for a total matching contribution of up to four percent of compensation. The required matching contributions and the three percent nonelective contribution under the basic 401(k) safe harbor must be immediately nonforfeitable (that is, 100 percent vested) when made.

Another safe harbor applies for a section 401(k) plan that includes automatic enrollment ("automatic enrollment 401(k) safe harbor"). Under an automatic enrollment 401(k) safe harbor, unless an employee elects otherwise, the employee is treated as electing to make elective deferrals equal to a percentage of compensation as stated in the plan, not in excess of 15 percent

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[152] Sec. 401(k)(3). Long-term part-time workers may be excluded from this and other nondiscrimination tests. Sec. 401(k)(2)(D).

[153] Sec. 401(k)(8).

[154] Sec. 401(k)(12) and (13). If certain additional requirements are met, matching contributions under 401(k) safe harbor plan may also satisfy a nondiscrimination test applicable under section 401(m).

and at least (1) three percent of compensation for the first year the deemed election applies to the participant, (2) four percent during the second year, (3) five percent during the third year, and (4) six percent during the fourth year and thereafter.[155] The matching contribution requirement under this safe harbor is 100 percent of elective contributions of the employee for contributions not in excess of one percent of compensation, and 50 percent of elective contributions for contributions that exceed one percent of compensation but do not exceed six percent, for a total matching contribution of up to 3.5 percent of compensation ("matching contribution automatic enrollment 401(k) safe harbor"). Alternatively, the plan can provide that the employer will make a nonelective contribution of three percent, as under the basic 401(k) safe harbor ("nonelective contribution automatic enrollment 401(k) safe harbor"). However, under the automatic enrollment 401(k) safe harbors, the matching and nonelective contributions are allowed to become 100 percent vested after two years of service (rather than being required to be immediately vested when made).

Matching contribution nondiscrimination test

Employer matching contributions are also subject to a special nondiscrimination test, the "ACP test," which compares the average actual contribution percentages ("ACPs") of matching contributions for the highly compensated employee group and the non-highly compensated employee group. The plan generally satisfies the ACP test if the ACP of the highly compensated employee group for the current plan year is either (1) not more than 125 percent of the ACP of the non-highly compensated employee group for the prior plan year, or (2) not more than 200 percent of the ACP of the non-highly compensated employee group for the prior plan year and not more than two percentage points greater than the ACP of the non-highly compensated employee group for the prior plan year.

A safe harbor section 401(k) plan that provides for matching contributions is deemed to satisfy the ACP test ("401(m) safe harbor") if, in addition to meeting the safe harbor contribution and notice requirements under section 401(k), (1) matching contributions are not provided with respect to elective deferrals in excess of six percent of compensation, (2) the rate of matching contribution does not increase as the rate of an employee's elective deferrals increases, and (3) the rate of matching contribution with respect to any rate of elective deferral of a highly compensated employee is no greater than the rate of matching contribution with respect to the same rate of deferral of a non-highly compensated employee.[156]

SIMPLE IRA plan

A small employer that employs no more than 100 employees who earned $5,000 or more during the prior calendar year can establish a simplified tax-favored retirement plan, which is called the SIMPLE IRA plan. A SIMPLE IRA plan is generally a plan under which

[155] These automatic increases in default contribution rates are required for plans using the safe harbor. Rev. Rul. 2009–30, 2009-39 I.R.B. 391, provides guidance for including automatic increases in other plans using automatic enrollment, including under a plan that includes an eligible automatic contribution arrangement.

[156] Sec. 401(m)(11); 401(m)(12).

contributions are made to an IRA for each employee (a "SIMPLE IRA").[157] A SIMPLE IRA plan allows employees to make elective deferrals to a SIMPLE IRA, subject to a limit of $13,500 (for 2021). An individual who has attained age 50 before the end of the taxable year may also make catch-up contributions under a SIMPLE IRA plan up to a limit of $3,000 (for 2021).

In the case of a SIMPLE IRA plan, the group of eligible employees generally must include any employee who has received at least $5,000 in compensation from the employer in any two preceding years and is reasonably expected to receive $5,000 in the current year. A SIMPLE IRA plan is not subject to the nondiscrimination rules generally applicable to qualified retirement plans.

Employer contributions to a SIMPLE IRA must satisfy one of two contribution formulas. Under the matching contribution formula, the employer generally is required to match employee elective contributions on a dollar-for-dollar basis up to three percent of the employee's compensation. The employer can elect a lower percentage matching contribution for all employees (but not less than one percent of each employee's compensation); however, a lower percentage cannot be elected for more than two years out of any five-year period. Alternatively, for any year, an employer is permitted to elect, in lieu of making matching contributions, to make a nonelective contribution of two percent of compensation on behalf of each eligible employee with at least $5,000 in compensation for such year, whether or not the employee makes an elective contribution.

The employer must provide each employee eligible to make elective deferrals under a SIMPLE IRA plan a 60-day election period before the beginning of the calendar year and a notice at the beginning of the 60-day period explaining the employee's choices under the plan.[158]

No contributions other than employee elective contributions, required employer matching contributions, or employer nonelective contributions can be made to a SIMPLE IRA plan, and the employer may not maintain any other qualified retirement plan.

Section 403(b) and governmental 457(b) plans

Tax-deferred annuity plans (referred to as section 403(b) plans) are generally similar to qualified defined contribution plans, but may be maintained only by (1) tax-exempt charitable organizations,[159] and (2) educational institutions of State or local governments (that is, public schools, including colleges and universities).[160] Section 403(b) plans may provide for employees to make elective deferrals (in pre-tax or designated Roth form), including catch-up contributions, or other after-tax employee contributions, and employers may make nonelective or matching contributions on behalf of employees. Contributions to a section 403(b) plan are generally

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[157] Sec. 408(p). Employer may also establish SIMPLE 401(k) plans. Sec. 401(k)(11).

[158] Notice 98-4, 1998-1 C.B. 269.

[159] These are organizations exempt from tax under section 501(c)(3). Section 403(b) plans of private, tax-exempt employers may be subject to ERISA as well as the requirements of section 403(b).

[160] Sec. 403(b).

subject to the same contribution limits applicable to qualified defined contribution plans, including the limits on elective deferrals.

Contributions to a section 403(b) plan must be fully vested. The minimum coverage and general nondiscrimination requirements applicable to a qualified retirement plan generally apply to a section 403(b) plan and to employer matching and nonelective contributions and after-tax employee contributions to the plan.[161] If a section 403(b) plan provides for elective deferrals, the plan is subject to a "universal availability" requirement under which all employees must be given the opportunity to make deferrals of more than $200.[162] In applying this requirement, nonresident aliens, students, and employees who normally work less than 20 hours per week may be excluded.[163]

An eligible deferred compensation plan of a governmental employer (referred to as a governmental section 457(b) plan) is generally similar to a qualified cash or deferred arrangement under a section 401(k) plan in that it consists of elective deferrals, that is, contributions (in pre-tax or designated Roth form) made at the election of an employee, including catch-up contributions. Deferrals under a governmental section 457(b) plan are generally subject to the same limits as elective deferrals under a section 401(k) plan or a section 403(b) plan.

Description of Proposal

The proposal modifies the definition of matching contribution[164] for purposes of defined contribution plans, including section 401(k) plans, to include employer contributions made to the plan on behalf of an employee on account of a qualified student loan payment. For this purpose, a qualified student loan payment is a payment made by an employee in repayment of a qualified education loan[165] and incurred by the employee to pay qualified higher education expenses, but only to the extent such payments in the aggregate for the year do not exceed the amount of elective deferrals that the employee would be permitted to contribute under the Code[166] (reduced by elective deferrals made by the employee for the year). Qualified higher education expenses

[161] These requirements do not apply to a governmental section 403(b) plan or a section 403(b) plan maintained by a church or a qualified church-controlled organization as defined in section 3121(w).

[162] Sec. 403(b)(12)(A)(ii).

[163] For this purpose, nonresident alien has the meaning in section 410(b)(3)(C), and student has the meaning in section 3121(b)(10). The universal availability requirement does not apply to a section 403(b) plan maintained by a church or a qualified church-controlled organization.

[164] Under section 401(m)(4)(A)(iii), as added by this proposal.

[165] As defined in section 221(d)(1), a qualified education loan is generally any indebtedness incurred by the taxpayer solely to pay qualified higher education expenses (1) which are incurred on behalf of the taxpayer, the taxpayer's spouse, or any dependent of the taxpayer as of the time the indebtedness was incurred; (2) which are paid or incurred within a reasonable period of time before or after the indebtedness is incurred; and (3) which are attributable to education furnished during a period during which the recipient was an eligible student.

[166] The limitation applicable under section 402(g) for the year ($19,500 for 2021), or, if less, the employee's compensation as defined in section 415(c)(3) for the year.

are defined as the cost of attendance at an eligible educational institution.[167] In addition, in order for the student loan payment to qualify, the employee must certify to the employer making the matching contribution that the loan payment has been made. The employer is permitted to rely on this certification.

In order for an employer contribution made on account of a qualified student loan payment to be treated as a matching contribution under the proposal, the plan must satisfy certain requirements. The plan must provide matching contributions on account of elective deferrals at the same rate as contributions on account of qualified student loan payments. The plan must provide matching contributions on account of qualified student loan payments only on behalf of employees otherwise eligible to receive matching contributions on account of elective deferrals (and, similarly, must provide matching contributions on account of elective deferrals only on behalf of employees eligible to receive matching contributions on account of qualified student loan payments). The plan must also provide that matching contributions on account of qualified student loan payments vest in the same manner as matching contributions on account of elective deferrals.

Under the proposal, for purposes of certain nondiscrimination rules and minimum coverage requirements,[168] matching contributions on account of qualified student loan payments do not fail to be treated as available to an employee solely because such employee does not have debt incurred under a qualified education loan. In addition, the proposal provides that a qualified student loan payment is generally not treated as a plan contribution. However, a plan may treat a qualified student loan payment as an elective deferral or an elective contribution (as applicable) for purposes of the matching contribution requirement under a basic safe harbor 401(k) plan or an automatic enrollment safe harbor 401(k) plan, as well as for purposes of the section 401(m) safe harbors.[169] A plan is also permitted to apply the ADP test separately to employees who receive matching contributions on account of qualified student loan payments.

The proposal also contains similar rules allowing matching contributions to be made on account of qualified student loan payments in the case of SIMPLE IRAs, section 403(b) plans, and section 457(b) plans. In the case of SIMPLE IRAs, the proposal provides that a SIMPLE IRA does not fail to meet the matching contribution requirement applicable to such arrangements solely because the arrangement treats qualified student loan payments as elective employer contributions to the extent such payments do not exceed the amount of elective employer

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[167] "Cost of attendance" for this purpose is defined in section 472 of the Higher Education Act of 1965, as in effect on the day before the enactment of the Taxpayer Relief Act of 1997. "Eligible educational institution" is defined in section 221(d)(2) of the Code.

[168] This rule applies for purposes of section 401(a)(4), section 410(b), and the rule under the proposal that all employees eligible to receive matching contributions on account of elective deferrals be eligible to receive matching contributions on account of qualified student loan payments.

[169] This rule applies for purposes of sections 401(k)(12)(B) and (13)(B), and sections 401(m)(11)(B) and (12). It also applies to SIMPLE section 401(k) plans under section 401(11)(B)(i)(II).

contributions the employee is permitted to contribute under the Code[170] (reduced by elective employer contributions contributed by the employee for the year). As under a section 401(k) plan, in order for the student loan payment to qualify, the employee must certify to the employer making the matching contribution that the loan payment has been made. In addition, matching contributions on account of qualified student loan payments must be provided only on behalf of employees otherwise eligible to make elective employer contributions, and all employees otherwise eligible to participate in the arrangement must be eligible to receive matching contributions on account of qualified student loan payments.

In the case of a section 403(b) plan, under the proposal, the fact that the employer offers matching contributions on account of qualified student loan payments[171] is not taken into account in determining whether the plan satisfies the universal availability requirement.[172] Similarly, in the case of a governmental 457(b) plan, the proposal provides that a plan is not treated as failing to meet the requirements applicable to such plans[173] solely because the plan, or another qualified plan[174] or section 403(b) plan maintained by the employer provides for matching contributions on account of qualified student loan payments.[175]

The proposal directs the Secretary to prescribe regulations for purposes of implementing the proposal, including regulations:

- Permitting a plan to make matching contributions for qualified student loan payments[176] at a different frequency than matching contributions are otherwise made under the plan, provided that the frequency is not less than annually;
- Permitting employers to establish reasonable procedures to claim matching contributions for such qualified student loan payments under the plan, including an annual deadline (not earlier than three months after the close of each plan year) by which a claim must be made; and
- Promulgating model amendments which plans may adopt to implement matching contributions on qualified student loan payments.[177]

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[170] The limitation applicable under section 408(p)(2)(E) for the year, including permitted catch-up contributions under section 414(v), or, if less, the employee's compensation as defined in section 415(c)(3) for the year.

[171] As described in section 401(m)(13), as added by this proposal.

[172] Sec. 403(b)(12)(A)(ii).

[173] Under section 457(b).

[174] Under section 401(a).

[175] As described in section 401(m)(13), as added by this proposal.

[176] As defined in sections 401(m)(4)(D) and 408(p)(2)(F), as added by this proposal.

[177] For purposes of sections 401(m), 408(p), 403(b), and 457(b).

Effective Date

The proposal is effective for contributions made for plan years beginning after December 31, 2021.

10. Application of credit for small employer pension plan start-up costs to employers which join an existing plan

Present Law

Present law provides a nonrefundable income tax credit equal to 50 percent of the qualified start-up costs paid or incurred during the taxable year by an eligible employer[178] that adopts a new eligible employer plan[179], provided that the plan covers at least one nonhighly compensated employee.[180] Qualified start-up costs are expenses connected with the establishment or administration of the plan and retirement-related education of employees with respect to the plan. The amount of the credit for any taxable year is limited to the greater of (1) $500 or (2) the lesser of (a) $250 multiplied by the number of nonhighly compensated employees of the eligible employer who are eligible to participate in the plan or (b) $5,000. The credit applies for up to three consecutive taxable years beginning with the taxable year the plan is first effective, or, at the election of the employer, with the year preceding the first plan year.

An eligible employer is an employer that, for the preceding year, had no more than 100 employees, each with compensation of $5,000 or more.[181] In addition, the employer must not have had a qualified employer plan covering substantially the same employees as the new plan with respect to which contributions were made or benefits were accrued during the three years preceding the first year for which the credit would apply. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[182] All eligible employer plans of an employer are treated as a single plan.

No deduction is allowed for the portion of qualified start-up costs paid or incurred for the taxable year equal to the amount of the credit.

[178] An eligible employer has the meaning given such term by section 408(p)(2)(C)(i).

[179] An eligible employer plan means a qualified employer plan within the meaning of section 4972(d) and includes a section 401(a) qualified retirement plan, a section 403 annuity, any simplified employee pension ("SEP") within the meaning of section 408(k), and any simple retirement account ("SIMPLE") within the meaning of section 408(p). An eligible employer plan does not include a plan maintained by a tax-exempt employer or a governmental plan, as defined in section 414(d).

[180] A nonhighly compensated employee is an employee who is not a highly compensated employee as defined under section 414(q).

[181] As defined in section 408(p)(2)(C).

[182] Sec. 52(a) or (b) and 414(m) or (o).

Description of Proposal

The proposal clarifies that the first credit year is the taxable year which includes the date that the eligible employer plan to which such costs relate becomes effective with respect to the eligible employer.

Effective Date

The proposal applies to eligible employer plans which become effective with respect to the eligible employer after the date of enactment.

11. Military spouse retirement plan eligibility credit for small employers

Present Law

Currently, there are no special credits for small employers that provide retirement benefits to military spouses.

Description of Proposal

The proposal allows eligible small employers to take a new nonrefundable income tax credit with respect to each individual who is married to a member of the uniformed services and self-certifies as such (referred to as a military spouse), who is an employee of the employer, who is eligible to participate in an eligible defined contribution plan of the employer, and who is a nonhighly compensated employee.[183] The credit is determined to be the sum of $250 for each such employee plus the amount of the contributions made to all eligible defined contribution plans by the employer with respect to the employee up to a maximum of $250 for each such employee. The credit applies for up to three consecutive years beginning with the first taxable year in which the individual begins participating in the plan.

An eligible small employer is an employer that, for the preceding year, had no more than 100 employees, each with compensation of $5,000 or more. In addition, the employer must not have had a plan covering substantially the same employees as the new plan during the three years preceding the first year for which the credit would apply. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[184]

An eligible defined contribution plan is a plan in which military spouses are eligible to participate within two months of beginning employment, and in which military spouses who are eligible to participate, 1) are immediately eligible to receive employer contributions in amounts not less than that received by similarly situated nonmilitary spouses with two years of service, and 2) have an immediate, nonforfeitable right to accrued benefits derived from employer contributions under the plan.

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[183] A nonhighly compensated employee is an employee who is not a highly compensated employee as defined under section 414(q).

[184] Sec. 52(a) or (b) and 414(m) or (o).

Effective Date

The proposal applies to taxable years beginning after the date of enactment.

12. Small immediate financial incentives for contributing to a plan

Present Law

Section 401(k) plans

A section 401(k) plan is a type of profit-sharing or stock bonus plan that contains a qualified cash or deferred arrangement. Such arrangements are subject to the rules generally applicable to qualified defined contribution plans. In addition, special rules apply to such arrangements. Employees who participate in a section 401(k) plan may elect to have contributions made to the plan (elective deferrals) rather than receive the same amount as current compensation.[185] The maximum annual amount of elective deferrals that can be made by an employee for a year is $19,500 (for 2021) or, if less, the employee's compensation.[186] For an employee who attains age 50 by the end of the year, the dollar limit on elective deferrals is increased by $6,500 (for 2021) (called "catch-up contributions").[187] An employee's elective deferrals must be fully vested. A section 401(k) plan may also provide for employer matching and nonelective contributions.

In order to constitute a qualified cash or deferred arrangement, no benefit under the arrangement may be conditioned, directly or indirectly, on the employee electing to have the employer make or not make contributions under the arrangement in lieu of receiving cash.[188] However, matching contributions are exempt from this rule.

Tax-sheltered annuities (section 403(b) plans)

Section 403(b) plans are a form of tax-favored employer-sponsored plan that provide tax benefits similar to qualified retirement plans. Section 403(b) plans may be maintained only by (1) charitable tax-exempt organizations, and (2) educational institutions of State or local governments (that is, public schools, including colleges and universities). Many of the rules that apply to section 403(b) plans are similar to the rules applicable to qualified retirement plans, including section 401(k) plans. Employers may make nonelective or matching contributions to such plans on behalf of their employees, and the plan may provide for employees to make pre-

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[185] Elective deferrals generally are made on a pre-tax basis and distributions attributable to elective deferrals are includible in income. However, a section 401(k) plan is permitted to include a "qualified Roth contribution program" that permits a participant to elect to have all or a portion of the participant's elective deferrals under the plan treated as after-tax Roth contributions. Certain distributions from a designated Roth account are excluded from income, even though they include earnings not previously taxed.

[186] Sec. 402(g).

[187] Sec. 414(v).

[188] Sec. 401(k)(4)(A).

tax elective deferrals, designated Roth contributions (held in designated Roth accounts)[189] or other after-tax contributions. Generally, section 403(b) plans provide for contributions toward the purchase of annuity contracts or provide for contributions to be held in custodial accounts for each employee. In the case of contributions to custodial accounts under a section 403(b) plan, the amounts must be invested only in regulated investment company stock.[190]

Contributions to a section 403(b) plan must be fully vested. The minimum coverage and general nondiscrimination requirements applicable to a qualified retirement plan generally apply to a section 403(b) plan and to employer matching and nonelective contributions and after-tax employee contributions to the plan.[191] If a section 403(b) plan provides for elective deferrals, the plan is subject to a "universal availability" requirement under which all employees must be given the opportunity to make deferrals of more than $200. In applying this requirement, nonresident aliens, students, and employees who normally work less than 20 hours per week may be excluded.[192]

Prohibited transactions

In general

The Code and ERISA prohibit certain transactions ("prohibited transaction") between a qualified retirement plan and a disqualified person (referred to as a "party in interest" under ERISA).[193] The prohibited transaction rules under the Code apply also to IRAs, Archer MSAs, HSAs, and Coverdell ESAs.[194]

Disqualified persons include a fiduciary of the plan; a person providing services to the plan; an employer with employees covered by the plan; an employee organization any of whose members are covered by the plan; certain owners, officers, directors, highly compensated

[189] Sec. 402A.

[190] Sec. 403(b)(7).

[191] These requirements do not apply to a governmental section 403(b) plan or a section 403(b) plan maintained by a church or a qualified church-controlled organization as defined in section 3121(w).

[192] For this purpose, nonresident has the meaning in section 410(b)(3)(C), and student has the meaning in section 3121(b)(10). The universal availability requirement does not apply to a section 403(b) plan maintained by a church or a qualified church-controlled organization.

[193] Sec. 4975; ERISA sec. 406. The prohibited transaction rules of the Code and ERISA are very similar; however, some differences exist between the two sets of rules. As mentioned above, ERISA generally does not apply to governmental plans or church plans. The prohibited transaction rules under the Code also generally do not apply to governmental plans or church plans. However, under section 503, the trust holding assets of a governmental or church plan may lose its tax-exempt status in the case of a prohibited transaction listed in section 503(b). Before the enactment of ERISA in 1974, section 503 applied to qualified retirement plans generally. In connection with the enactment of section 4975 by ERISA, section 503 was amended to apply only to governmental and church plans.

[194] These are included in the definition of "plan" under section 4975(e)(1).

employees, family members, and related entities.[195] A fiduciary includes any person who (1) exercises any discretionary authority or discretionary control respecting management of the plan or exercises any authority or control respecting management or disposition of the plan's assets, (2) renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of the plan, or has any authority or responsibility to do so, or (3) has any discretionary authority or discretionary responsibility in the administration of the plan.[196]

Prohibited transactions include the following transactions, whether direct or indirect, between a plan and a disqualified person:

1. The sale or exchange or leasing of property,

2. The lending of money or other extension of credit,

3. The furnishing of goods, services, or facilities,

4. The transfer to, or use by or for the benefit of, the income or assets of the plan,

5. In the case of a fiduciary, an act dealing with the plan's income or assets in the fiduciary's own interest or for the fiduciary's own account, and

6. The receipt by a fiduciary of any consideration for the fiduciary's own personal account from any party dealing with the plan in connection with a transaction involving the income or assets of the plan.[197]

Exemptions from prohibited transaction treatment

Certain transactions are statutorily exempt from prohibited transaction treatment, for example, certain loans to plan participants and arrangements with a disqualified person for legal,

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[195] Sec. 4975(e)(2). Party in interest is defined similarly under ERISA section 3(14) with respect to an employee benefit plan. Under ERISA, employee benefit plans, defined in ERISA section 3(3), consist of two types: pension plans (that is, retirement plans), defined in ERISA section 3(2), and welfare plans, defined in ERISA section 3(1).

[196] Sec. 4975(d)(3); ERISA sec. 3(21)(A). Under ERISA, fiduciary also includes any person designated under ERISA section 405(c)(1)(B) by a named fiduciary (that is, a fiduciary named in the plan document) to carry out fiduciary responsibilities.

[197] Sec. 4975(c)(1)(A)-(F) and ERISA sec. 406(a)(1)(A)-(D) and (b)(1) and (3). Under ERISA section 406(a)(1), a plan fiduciary is prohibited from causing the plan to engage in a transaction described in paragraphs (A)-(D). ERISA section 406(b)(2) also prohibits a plan fiduciary, in the fiduciary's individual capacity or any other capacity, from acting in any transaction involving the plan on behalf of a party (or represent a party) whose interests are adverse to the interests of the plan or the interests of plan participants or beneficiaries. ERISA section 406(a)(1)(E) and (a)(2) relate to limitations under ERISA section 407 on a plan's acquisition or holding of employer securities and real property.

accounting or other services necessary for the establishment or operation of a plan if no more than reasonable compensation is paid for the services.[198]

Sanctions for violations

Under the Code, if a prohibited transaction occurs, the disqualified person who participated in the transaction is generally subject to a two-tiered excise tax. The first tier tax is 15 percent of the amount involved in the transaction. The second tier tax, imposed if the prohibited transaction is not corrected within a certain period, is 100 percent of the amount involved. In the case of an IRA, HSA, Archer MSA or Coverdell ESA, the sanction for some prohibited transactions is the loss of tax favored status, rather than an excise tax. A private right of action is not available for a Code violation.

Under ERISA, DOL may assess a civil penalty against a person who engages in a prohibited transaction, other than a transaction with a plan covered by the prohibited transaction rules of the Code.[199] The penalty may not exceed five percent of the amount involved in the transaction for each year or part of a year that the prohibited transaction continues. If the prohibited transaction is not corrected within 90 days after notice from DOL, the penalty can be up to 100 percent of the amount involved in the transaction. A prohibited transaction by a fiduciary may also be the basis for an action for a breach of fiduciary responsibility by DOL, a plan participant or beneficiary, or another plan fiduciary (as discussed above).

Description of Proposal

The proposal modifies the rule applicable to section 401(k) plans that prohibits the conditioning of benefits (other than matching contributions) on an employee's election to defer. As modified, the rule exempts de minimis financial incentives in addition to matching contributions. Thus, a section 401(k) plan will not fail to include a qualified cash or deferred arrangement merely because it conditions a de minimis financial incentive on an employee's election to defer.

Similarly, in the case of a section 403(b) plan, the proposal provides that a plan does not fail to satisfy the universal availability requirement[200] solely by reason of offering a de minimis financial incentive to employees to elect to have the employer make contributions pursuant to a salary reduction agreement.

[198] Sec. 4975(d) and ERISA sec. 408. The Code and ERISA also provide for the grant of administrative exemptions, on either an individual or class basis, subject to a finding that the exemption is administratively feasible, in the interests of the plan and of its participants and beneficiaries, and protective of the rights of participants and beneficiaries of the plan.

[199] ERISA sec. 502(i).

[200] Sec. 403(b)(12)(A)(ii).

In addition, under the proposal, the provision of such de minimis financial incentives under a section 401(k) plan or a section 403(b) plan is not treated as a prohibited transaction under the Code or ERISA.[201]

Effective Date

The proposal applies to plan years beginning after the date of enactment.

13. Safe harbor for correction of employee elective deferral failures

Present Law

Background on automatic enrollment features in retirement plans may be found in section A.1. of this document.

Employee Plans Compliance Resolution System

A retirement plan that is intended to be a tax-qualified plan provides retirement benefits on a tax-favored basis if the plan satisfies all of the qualification requirements under the Code.[202] Similarly, an annuity that is intended to be a tax-sheltered annuity provides retirement benefits on a tax-favored basis if the program satisfies all of the requirements under the Code applicable to section 403(b) plans. Failure to satisfy all of the applicable requirements may disqualify a plan or annuity for the intended tax-favored treatment.

The IRS has established the Employee Plans Compliance Resolution System ("EPCRS"), which is a comprehensive system of correction programs for sponsors of retirement plans and annuities that are intended, but have failed, to satisfy the applicable requirements under the Code.[203] EPCRS permits employers to correct compliance failures and continue to provide their employees with retirement benefits on a tax-favored basis.

The IRS designed EPCRS to (1) encourage operational and formal compliance, (2) promote voluntary and timely correction of compliance failures, (3) provide sanctions for compliance failures identified on audit that are reasonable in light of the nature, extent, and severity of the violation, (4) provide consistent and uniform administration of the correction programs, and (5) permit employers to rely on the availability of EPCRS in taking corrective actions to maintain the tax-favored status of their retirement plans and annuities.

The basic elements of the programs that comprise EPCRS are self-correction, voluntary correction with IRS approval, and correction on audit. The Self-Correction Program ("SCP") generally permits a plan sponsor that has established practices and procedures (formal or informal) reasonably designed to promote and facilitate overall compliance in form and

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[201] Under section 4975 and section 408 of ERISA.

[202] Sec. 401(a).

[203] The requirements under sections 401(a), 403(a), or 403(b), as applicable. Rev. Proc. 2019-19, 2019-19 I.R.B. 1086.

operation with applicable Code requirements to correct certain insignificant failures at any time (including during an audit), and certain significant failures within a two-year period, without payment of any fee or sanction. The Voluntary Correction Program ("VCP") permits an employer, at any time before an audit, to pay a limited fee and receive IRS approval of a correction. For a failure that is discovered on audit and corrected, the Audit Closing Agreement Program ("Audit CAP") provides for a sanction that bears a reasonable relationship to the nature, extent, and severity of the failure and that takes into account the extent to which correction occurred before audit.

SCP, VCP and Audit CAP are not available to correct failures relating to the diversion or misuses of plan assets.[204] With respect to the SCP program, in the event that the plan or the plan sponsor has been a party to an abusive tax avoidance transaction, SCP is not available to correct any operational failure that is directly or indirectly related to the abusive tax avoidance transaction.[205]

SEP and SIMPLE Plans

SCP and VCP[206] under EPCRS are available to a SEP or SIMPLE plan.[207] SCP is only available to such a plan to correct insignificant operational failures,[208] and only if the SEP or SIMPLE plan is established and maintained on a document approved by the IRS.

Section 457(b) plans

EPCRS does not apply to section 457(b) plans. However, the IRS will accept submissions relating to section 457(b) plans on a provisional basis outside of EPCRS through standards that are similar to those that apply to VCP filings.[209]

Special safe harbor correction method for failures related to automatic contribution features in a section 401(k) or 403(b) plan

Employee Elective Deferral Failures

A safe harbor correction method is available for certain employee elective deferral failures associated with missed elective deferrals for eligible employees who ae subject to an automatic contribution feature in a section 401(k) or 403(b) plan (including employees who

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[204] Sec. 4.11 of Rev. Proc. 2019-19.

[205] Sec. 4.12 of Rev. Proc. 2019-19.

[206] Sec. 6.11 of Rev. Proc. 2019-9.

[207] Secs. 1.01 and 1.02 of Rev. Proc. 2019-19. A SEP is a plan intended to satisfy the requirements of Code section 408(k); a SIMPLE plan is a plan intended to satisfy the requirements of Code section 408(p). Secs. 5.06 and 5.07 of Rev. Proc. 2019-19.

[208] Sec. 4.01(c) of Rev. Proc. 2019-19.

[209] Sec. 4.09 of Rev. Proc. 2019-19.

made affirmative elections in lieu of automatic contributions but whose elections were not implemented correctly).[210]

An "employee elective deferral failure"[211] is a failure to implement elective deferrals correctly in a section 401(k) plan or 403(b) plan, including elective deferrals pursuant to an affirmative election or pursuant to an automatic contribution feature under such a plan, and a failure to afford an employee the opportunity to make an affirmative election because the employee was improperly excluded from the plan. Automatic contribution features include automatic enrollment and automatic escalation features that are affirmatively elected.[212]

If the failure to implement an automatic contribution feature for an affected eligible employee or the failure to implement an affirmative election of an eligible employee who is otherwise subject to an automatic contribution feature does not extend beyond the end of the nine and one-half month period after the end of the plan year of the failure (which is generally the filing deadline of the Form 5500 series return, including automatic extensions), no qualified nonelective contribution ("QNEC")[213] for the missed elective deferrals is required, provided that the following conditions are satisfied:

1. Correct deferrals begin no later than the earlier of the first payment of compensation made on or after the last day of the nine and one-half month period after the end of the plan year in which the failure first occurred for the affected eligible employee or, if the plan sponsor was notified of the failure by the affected eligible employee, the first payment of compensation made on or after the end of the month after the month of notification;

2. Notice of the failure, that satisfies the content requirements described below, is given to the affected eligible employee not later than 45 days after the date on which correct deferrals begin; and

3. If the eligible employee would have been entitled to additional matching contributions had the missed deferrals been made, the plan sponsor makes a corrective allocation (adjusted for earnings) on behalf of the employee equal to the matching contributions that would have been required under the terms of the plan as if the missed deferrals had been contributed to the plan in accordance with the timing requirements under SCP for significant operational failures. This correction method provides an

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[210] Sec. 05(8) of Appendix A of Rev. Proc. 2019-19.

[211] Sec. 05(10) of Appendix A of Rev. Proc. 2019-19.

[212] Sec. 05(10) of Appendix A of Rev. Proc. 2019-19.

[213] A QNEC, as defined in Treas. Reg. sec. 1.401(k)-6 means "employer contributions, other than elective contributions or matching contributions, that, except as provided otherwise in § 1.401(k)–1(c) and (d), satisfy the requirements of § 1.401(k)–1(c) and (d) as though the contributions were elective contributions, without regard to whether the contributions are actually taken into account under the ADP test under § 1.401(k)–2(a)(6) or the ACP test under § 1.401(m)–2(a)(6). Thus, the nonelective contributions must satisfy the nonforfeitability requirements of § 1.401(k)-1(c) and be subject to the distribution limitations of § 1.401(k)-1(d) when they are allocated to participants' accounts."

alternative safe harbor method for calculating earnings for Employee Elective Deferral Failures under section 401(k) plans or 403(b) plans.[214]

Content of notice requirement

The required notice must include the following information:

1. General information relating to the failure, such as the percentage of eligible compensation that should have been deferred, and the approximate date that the compensation should have begun to be deferred. The general information need not include a statement of the dollar amounts that should have been deferred;

2. A statement that appropriate amounts have begun to be deducted from compensation and contributed to the plan (or that appropriate deductions and contributions will begin shortly);

3. A statement that corrective allocations relating to missed matching contributions have been made (or that corrective allocations will be made). Information relating to the date and the amount of corrective allocations need not be provided;

4. An explanation that the affected participant may increase his or her deferral percentage in order to make up for the missed deferral opportunity, subject to applicable limits for elective deferrals;[215] and

5. The name of the plan and plan contact information (including name, street address, email address, and telephone number of a plan contact).

Sunset of safe harbor correction method

The safe harbor correction method is available for plans only with respect to failures that begin on or before December 31, 2020.

Description of Proposal

Under the proposal, a plan will not fail to be treated as a qualified plan, a section 403(b) tax sheltered annuity, an IRA, or a section 457(b) plan solely by reason of a "corrected error."

For purposes of this proposal, a "corrected error" means a reasonable administrative error in implementing an automatic enrollment or automatic escalation feature in accordance with the terms of an eligible automatic contribution arrangement,[216] provided that such implementation error:

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[214] The plan may also use the earnings adjustment methods set forth in section 3 of Appendix B of Rev. Proc. 2019-19.

[215] Under sec. 402(g).

[216] As defined in section 414(w)(3).

1. Is corrected by the date that is nine and one-half months after the end of the plan year during which the failure occurred;

2. Is corrected in a manner that is favorable to the participant; and

3. Is of a type which is so corrected for all similarly situated participants in a nondiscriminatory manner.

The correction may occur before or after the participant has terminated employment and may occur without regard to whether the error is identified by the Secretary.

The Secretary must issue regulations or other guidance of general applicability specifying the methods that are "in a manner favorable to the participant or beneficiary."

Effective Date

The proposal applies to any errors with respect to which the date that is nine and one-half months after the end of the plan year during which the error occurred is after the date of enactment.

14. One-year reduction in period of service requirement for long-term, part-time workers

Present Law

Background on section 401(k) plans may be found in section A.9. of this document.

General participation requirements

A qualified retirement plan generally can delay participation in the plan based on attainment of age or completion of years of service but not beyond the later of completion of one year of service (that is, a 12-month period with at least 1,000 hours of service) or attainment of age 21.[217] A plan also cannot exclude an employee from participation (on the basis of age) when that employee has attained a specified age.[218] Employees can be excluded from plan participation on other bases, such as job classification, as long as the other basis is not an indirect age or service requirement. A plan can provide that an employee is not entitled to an allocation of employer nonelective or matching contributions for a plan year unless the employee completes either 1,000 hours of service during the plan year or is employed on the last day of the year even if the employee previously completed 1,000 hours of service in a prior year.

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[217] Secs. 401(a)(3) and 410(a)(1). Parallel requirements generally apply to plans of private employers under section 202 of the Employee Retirement Income Security Act of 1974 ("ERISA"). Governmental plans under section 414(d) and church plans under section 414(e) are generally exempt from these Code requirements and from ERISA.

[218] Sec. 410(a)(2).

Long-term part-time workers

Section 401(k) plans generally must permit an employee to make elective deferrals if the employee has worked at least 500 hours per year with the employer for at least three consecutive years and has met the minimum age requirement (age 21) by the end of the three-consecutive-year period (for this proposal, an employee is referred to as a "long-term part-time employee" after having completed this period of service).[219] Thus, a long-term part-time employee may not be excluded from the plan merely because the employee has not completed a year of service. Once a long-term part-time employee meets the age and service requirements, such employee must be able to commence participation no later than the earlier of (1) the first day of the first plan year beginning after the date on which the employee satisfied the age and service requirements or (2) the date six months after the date on which the individual satisfied those requirements.

The plan is not required to provide that a long-term part-time employee is otherwise eligible to participate in the plan. Thus, the plan can continue to treat a long-term part-time employee as ineligible under the plan for employer nonelective and matching contributions based on not having completed a year of service. However, for a plan that does provide employer contributions for long-term part-time employees, the plan must credit, for each year in which such an employee worked at least 500 hours, a year of service for purposes of vesting in any employer contributions. If a long-term part-time employee under such a plan becomes a full-time employee, the plan must continue to credit the employee with any years of service earned under the special rule for long-term part-time employees.

Employers are permitted to exclude long-term part-time employees from nondiscrimination testing,[220] including top-heavy vesting and top-heavy benefit requirements. However, the relief from the nondiscrimination rules ceases to apply to any employee who becomes a full-time employee (as of the first plan year beginning after the plan year in which the employee completes a 12-month period with at least 1,000 hours of service).

The long-term part-time employee rules are effective for plan years beginning after December 31, 2020, except that for determining whether the three-consecutive-year period has been met, 12-month periods beginning before January 1, 2021 are not taken into account.

Description of Proposal

The proposal modifies the rules that apply to long-time part-time employees under a section 401(k) plan to reduce the service requirement for such employees from three years to two years. Thus, under the proposal, a section 401(k) plan generally must permit an employee to make elective deferrals if the employee has worked at least 500 hours per year with the employer

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[219] Sec. 401(k)(2)(D). This rule does not apply to collectively bargained plans.

[220] Nondiscrimination testing relief applies to sections 401(a)(4), 401(k)(3), 401(k)(12), 401(k)(13), 401(m)(2), and 410(b).

for at least two consecutive years and has met the minimum age requirement (age 21) by the end of the two-consecutive-year period.

In addition, the proposal clarifies the effective date of the long-term part-time employee rules. Under the proposal, 12-month periods beginning before January 1, 2021 are also not taken into account in determining a year of service for purposes of the rules applicable to the vesting of employer contributions.

Effective Date

The proposal is effective as if included in the enactment of section 112 of the Setting Every Community Up for Retirement Enhancement Act of 2019.[221]

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[221] Pub. L. No. 116-94, Division O.

B. Preservation of Income

1. Remove required minimum distribution barriers for life annuities

Present Law

Required minimum distributions

Background on required minimum distributions under qualified retirement plans may be found in section A.5. of this document.

Annuities

A plan will not fail to satisfy the minimum required distribution rules merely because distributions are made from an annuity contract which is purchased with the employee's benefit by the plan from an insurance company.[222] Prior to the date that an annuity contract under an individual account plan commences benefits under the contract, the interest of the employee or beneficiary under that contract is treated as an individual account for purposes of the required minimum distribution requirements.[223] Once distributions are required to begin (on the required beginning date), payments under the annuity contract will satisfy the required minimum distribution rules if distributions of the employee's entire interest are paid in the form of periodic annuity payments for the employee's life (or the joint lives of the employee and beneficiary) or over a period certain as defined in the regulations.[224]

All annuity payments (whether paid over an employee's life, joint lives, or a period certain) must be nonincreasing, or only increase in accordance with certain exceptions.[225]

There are additional increases permitted for annuity payments under annuity contracts purchased from insurance companies. If the total future payments expected to be made under the annuity contract ("future expected payments") exceed the "total value being annuitized," the payments under the annuity contract will not fail to satisfy the nonincreasing payment requirement merely because the payments (1) are increased by a constant percentage, applied not less frequently than annually; (2) provide for a final payment upon the death of the employee that does not exceed the excess of the total value being annuitized over the total of payments before the death of the employee; (3) are increased as a result of dividend payments or other payments that result from actuarial gains but only if actuarial gain is measured no less frequently than annually and the resulting payments are either paid no later than the year following the year for

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[222] Treas. Reg. sec. 1.401(a)(9)-6, A-4.

[223] Treas. Reg. sec. 1.401(a)(9)-6, A-12(a).

[224] Treas. Reg. sec. 1.401(a)(9)-6, A-1, -3 and -4. If the annuity contract is purchased after the required beginning date, the first payment must begin on or before the purchase date and the payment required must be made no later than the end of that required period.

[225] Treas. Reg. sec. 1.401(a)(9)-6, A-14(a). The exceptions include eligible cost of living increases, increased benefits resulting from a plan amendment, and lump sum distributions made to a beneficiary upon the death of the employee.

which the actuarial experience is measured or paid in the same form as the payment of the annuity over the remaining period of the annuity; and (4) are increased for certain accelerations of payment.[226] However, in operation, this actuarial test does not permit certain guarantees in life annuities such as certain guaranteed annual increases, return of premium death benefits and period certain guarantees for participating annuities.

Description of Proposal

The proposal amends the minimum required distribution rules to permit commercial annuities[227] that are issued in connection with any eligible retirement plan[228] to provide one or more of the following types of payments on or after the annuity starting date:

- Annuity payments that increase by a constant percentage, applied not less frequently than annually, at a rate that is less than five percent per year;
- A lump sum payment that results in a shortening of the payment period with respect to an annuity, or a full or partial commutation of the future annuity payments, provided that such a lump sum is determined using reasonable actuarial methods and assumptions, determined in good faith by the issuer of the contract;
- A lump sum payment that accelerates the receipt of annuity payments that are scheduled to be received within the ensuing 12 months, regardless of whether such acceleration shortens the payment period with respect to the annuity, reduces the dollar amount of benefits to be paid under the contract, or results in a suspension of annuity payments during the period being accelerated;
- Dividends or similar distributions determined in an actuarially reasonable manner; and
- Lump sum return of premium death benefits.

The proposal also directs the Secretary, within one year after the date of enactment, to conform the regulations to the foregoing statutory amendments and thereby exempt the listed annuity benefits from the actuarial test in the regulations. The Secretary is also directed to provide that any commercial annuity that provides an initial payment that is at least equal to the initial payment that is required from an individual account is deemed to satisfy the actuarial test in the regulations. The Secretary is also directed to amend the actuarial test in the regulations to provide that the calculations under the test are made using the reasonable tables or other actuarial assumptions that the issuer of the contract actually uses in pricing the premiums and benefits

[226] Treas. Reg. sec. 1.401(a)(9)-6, A-14(c).

[227] Within the meaning of section 3405(e)(6).

[228] Within the meaning of section 402(c)(8)(B), other than a defined benefit plan.

under the contract, provided that such tables or other actuarial assumptions are reasonable, rather than using the life expectancy tables in the regulations.

The proposal also directs the Secretary as of the date of enactment to administer and enforce the law in accordance with the provisions of this proposal.

Effective Date

The proposal is effective as of the date of enactment.

2. Qualifying longevity annuity contracts

Present Law

Required minimum distributions

Background on required minimum distributions under qualified retirement plans may be found in section A.5. of this document.

Annuity distributions

The regulations provide rules for the amount of annuity distributions from a defined benefit plan, or from an annuity purchased by the plan from an insurance company (including annuity contracts under a defined contribution plan), that are paid over life or life expectancy. Annuity distributions are generally required to be nonincreasing with certain exceptions, which include, for example, (i) increases to the extent of certain specified cost-of-living indices, (ii) a constant percentage increase (for a qualified defined benefit plan, the constant percentage cannot exceed five percent per year), (iii) certain accelerations of payments, and (iv) increases to reflect when an annuity is converted to a single life annuity after the death of the beneficiary under a joint and survivor annuity or after termination of the survivor annuity under a qualified domestic relations order.[229] If distributions are in the form of a joint and survivor annuity and the survivor annuitant both is not the surviving spouse and is younger than the employee (or IRA owner), the survivor annuity benefit is limited to a percentage of the life annuity benefit for the employee (or IRA owner). The survivor benefit as a percentage of the benefit of the primary annuitant is required to be smaller (but not required to be less than 52 percent) as the difference in the ages of the primary annuitant and the survivor annuitant become greater.

If an annuity contract held under a defined contribution plan has not yet been annuitized, the interest of an employee or beneficiary under that contract is treated as an individual account for purposes of the minimum required distribution rules. Thus, the value of that contract is included in the account balance used to determine required minimum distributions from the employee's individual account.[230]

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[229] Treas. Reg. sec. 1.401(a)(9)-6, A-14.

[230] Treas. Reg. sec. 1.401(a)(9)-6, A-12.

Plan amendment and anti-cut-back requirements

Present law provides a remedial amendment period during which, under certain circumstances, a qualified retirement plan may be amended retroactively in order to comply with the qualification requirements.[231] In general, plan amendments to reflect changes in the law generally must be made by the time prescribed by law for filing the income tax return of the employer for the employer's taxable year in which the change in law occurs.[232] The Secretary may extend the time by which plan amendments need to be made.

The Code and ERISA generally prohibit plan amendments that reduce accrued benefits, including amendments that eliminate or reduce optional forms of benefit with respect to benefits already accrued except to the extent prescribed in regulations.[233] This prohibition on the reduction of accrued benefits is commonly referred to as the "anti-cut-back rule."

Qualifying longevity annuity contracts

A "qualifying longevity annuity contract" ("QLAC") is a deferred annuity contract that is purchased from an insurance company for an employee that is generally scheduled to commence payments at an advanced age (but no later than age 85)[234] and which satisfies each of the following requirements:[235]

1. Premiums for the QLAC do not exceed the lesser of a dollar or percentage limitation. The dollar limitation is (1) $125,000 (as adjusted) ($135,000 for 2020 and 2021) over (2) the sum of (a) the premiums previously paid with respect to the contract and (b) the premiums previously paid with respect to any other QLAC that is purchased for the employee under the plan, or any other plan of the employer.[236] The percentage limitation is 25 percent of the employer's account balance under the plan (including the value of any QLAC held under the plan for the employee) over the previously paid

[231] Sec. 401(b).

[232] In addition, if an employer adopts a qualified retirement plan after the close of a taxable year but before the time prescribed by law for filing the return of tax of the employer for the taxable year (including extensions thereof), the employer may elect to treat the plan as having been adopted as of the last day of the taxable year. See 401(b)(2), as enacted under section 201 of the Setting Every Community up for Retirement Enhancement (the "SECURE Act"). See also the description of the proposal in section C.19. of this document, Amendments to increase benefit accruals under plan for previous plan year allowed until employer tax return due date.

[233] Sec. 411(d)(6) and ERISA sec. 204(g).

[234] Because under section 401(a)(9), minimum required distributions must generally begin no later than the April 1 of the year following the year in which the individual attains age 72, without these special rules, QLACs would violate the requirements of section 401(a)(9). See the description of the proposal in section A.5. of this document, which proposes an increase in the age for the required beginning date for mandatory distributions.

[235] Treas. Reg. sec. 401(a)(9)-6, A-17.

[236] Including any other plan, annuity, or account described in sections 401(a), 403(a), 403(b), or 408, or an eligible governmental plan under section 457(b).

premiums with respect to the contract or with respect to any other QLAC that is purchased for the employee under the plan, or any other plan of the employer.

2. The QLAC provides that distributions under the contract must commence not later than the first day of the month following the individual's attainment of age 85.

3. The QLAC provides that once distributions begin under the contract, the distributions satisfy the minimum required distribution rules, except for the rule that annuity payments commence on or before the required beginning date.

4. The contract does not make available any commutation benefit, cash surrender right, or other similar feature.

5. No benefits are provided under the contract after the death of the employee other than those provided for in the regulations.

6. When the contract is issued, the contract (or a rider or endorsement) states that it is intended to be a QLAC.

7. The contract is not a variable contract, an indexed contract, or a similar contract, except as provided in guidance.

Description of Proposal

Under the proposal, no later than one year after the date of enactment, the Secretary (or the Secretary's delegate) is directed to amend the minimum required distribution regulation which applies to QLACs:

- To eliminate the requirement that premiums for QLACs be limited to 25 percent (or any other percentage) of an individual's account balance;
- To provide that in the case of a QLAC purchased with joint and survivor annuity benefits for the individual and his or her spouse that were permissible under the regulations at the time the contract was originally purchased, a divorce occurring after the original purchase and before the annuity payments commence under the contract, does not affect the permissibility of the joint and survivor annuity benefits or other benefits under the contract, or require any adjustment to the amount or duration of benefits payable under the contract provided that any qualified domestic relations order[237] or any divorce or separation instrument (1) provides that the former spouse is entitled to the survivor benefits under the contract, (2) does not modify the treatment of the former spouse as beneficiary under the contract who is entitled to the survivor benefits, or (3) does not modify the treatment of the former spouse as the measuring life for the survivor benefits under the contract. For purposes of this proposal, the term "divorce or separation instrument" means (1) a decree of divorce or separate maintenance or a written instrument incident to such a decree, (2) a written separation

[237] Within the meaning of section 414(p).

agreement, or (3) a decree (not described in (1)) requiring a spouse to make payments for the support or maintenance of the other spouse; and

- To ensure that the regulation does not preclude a contract from including a provision under which an employee may rescind the purchase of the contract within a period not exceeding 90 days from the date of purchase (the "short free look period.")

Effective Date

The proposal is generally effective with respect to contracts purchased or received in an exchange on or after the date of enactment. The changes with respect to joint and survivor annuities and the short free look period are effective with respect to contracts purchased or received in an exchange on or after July 2, 2014.

Prior to the date the Secretary issues final regulations, the Secretary shall administer and enforce the law in accordance with the effective dates above, and taxpayers may rely upon their reasonable good faith interpretations of the law prior to this proposal becoming effective.

3. Insurance-dedicated exchange-traded funds

Present Law

Income exclusion and deferred tax treatment for life insurance and annuity contracts

An exclusion from gross income is provided for amounts received under a life insurance contract paid by reason of the death of the insured.[238] Further, no Federal income tax generally is imposed on a policyholder with respect to the earnings under a life insurance contract (''inside buildup''). Distributions from a life insurance contract (other than a modified endowment contract[239]) that are made prior to the death of the insured generally are includible in income only to the extent that the amounts distributed exceed the taxpayer's investment in the contract. Such distributions generally are treated first as a tax-free recovery of the investment in the contract, and then as income.[240] Present law provides a definition of life insurance designed to limit the investment orientation of the contract.[241]

No Federal income tax is generally imposed on a deferred annuity contract holder who is a natural person with respect to the earnings on the contract (inside buildup) in the absence of a distribution under the contract. Annuity distributions generally are treated as partially excludable return of basis and partially ordinary income under an ''exclusion ratio'' (the ratio of

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[238] Sec. 101(a).

[239] Sec. 7702A. A modified endowment contract is generally a life insurance contract funded more rapidly than in seven level annual premiums. Distributions (including loans) from a modified endowment contract are generally treated as income first, then as a tax-free return of basis. Sec. 72(e)(10).

[240] Sec. 72(e).

[241] Sec. 7702.

the investment in the contract to the expected return under the contract as of that date).[242] Other distributions (which for this purpose include loans) are treated as income first, then as a tax-free return of basis.[243] An additional 10-percent tax is imposed on the income portion of distributions made before age 59–1/2, and in certain other circumstances.[244] An annuity contract must provide for certain required distributions if the holder dies before the entire interest in the contract has been distributed.[245] No dollar limit is imposed on the amount that may be paid into an annuity contract (that is not a pension plan contract) for Federal income tax purposes.

Variable contracts

A variable contract is generally an annuity or life insurance contract whose death benefit, payout, or premium amounts are based on the return on and market value of underlying assets. For tax purposes, a variable contract is defined by statute.[246] Under the statutory criteria, all or part of the amounts received for the contract (premiums) must be allocated to a segregated asset account of the insurer. The contract must provide for the payment of annuities, must be a life insurance contract,[247] or must fund insurance on retired lives.[248] The contract must reflect the investment return and the market value of the segregated asset account, or in the case of a life insurance contract, the amount of the death benefit or period of coverage must be adjusted on the basis of the investment return and the market value of the segregated asset account. The segregated asset accounts for variable contracts generally are invested in a variety of investment funds.

Diversification requirements

The investment assets held in the segregated asset account for a variable contract must be adequately diversified.[249] If the assets are not adequately diversified, the variable contract is not treated as an annuity or life insurance contract.[250] As a result, otherwise tax-deferred or excluded

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[242] Sec. 72(b).

[243] Sec. 72(e).

[244] Sec. 72(q).

[245] Sec. 72(s).

[246] Sec. 817(d).

[247] As defined for Federal tax purposes in section 7702.

[248] As described in section 807(c)(6) (governing life insurer reserve deductions).

[249] Sec. 817(h).

[250] The investor control doctrine can also apply in some fact situations. This two-pronged doctrine generally treats a contract as not a life insurance contract or not an annuity contract if the contract holder has significant incidents of ownership with respect to the investments in the insurer segregated asset account, or if the segregated asset account assets are publicly available for purchase (*i.e*, not exclusively through the contract). See Rev. Rul. 81-225, 1981-2 C.B. 12, as modified by Rev. Proc. 99-44 and as clarified and amplified by Rev. Rul. 2007-7; *Christofferson v. U.S.*, 749 F.2d 513 (8th Cir. 1984); *Webber v. Commissioner*, 144 T.C. 324 (2015).

income on the contract is treated as ordinary income received or accrued by the contract holder during the taxable year.[251]

When the diversification requirement for variable contracts was added in 1984, the Conference Report stated, "[i]n authorizing Treasury to prescribe diversification standards, the conferees intend that standards be designed to deny annuity or life insurance treatment for investments that are publicly available to investors and investments that are made, in effect, at the direction of the investor."[252]

The regulatory diversification requirements impose investment concentration limits based on percentages of the total value of the assets in the segregated asset account.[253] A safe harbor is provided for a segregated asset account holding a regulated investment company ("RIC" or mutual fund) that is at least as diversified as is required under the RIC rules of section 851(b)(4) and no more than 55 percent of the value of whose assets is in cash, cash items, government securities, and securities of other RICs.[254]

The diversification requirements provide a lookthrough rule for assets held through a RIC, real estate investment trust (REIT), partnership, or certain trusts such as a grantor trust. This lookthrough rule provides that the RIC, REIT, partnership or trust is not treated as a single investment of the segregated asset account, but rather, a pro rata portion of each of its assets is treated as an asset of the account.[255]

However, the lookthrough rule imposes requirements.[256] All the beneficial interests in the RIC, REIT, partnership, or trust generally must be held by a segregated asset account. Public access to the RIC, REIT, partnership, or trust must generally be available exclusively through the purchase of a variable contract. For example, if an investment fund's interests are held by a market maker or by a financial institution that, as a participant in a clearing agency, is permitted to purchase and redeem shares directly from the fund and sell them to third parties, then the fund does not satisfy this requirement of the lookthrough rule.

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[251] Secs. 72 and 7702, and Treas. Reg. sec. 1.817-5(a).

[252] H.R. Conf. Rep. No. 861, 98th Cong., 2d Sess. (1984), page 1055. Similarly, the Blue Book for the 1984 Act states that the diversification requirements were enacted "to discourage the use of tax-preferred variable annuities and variable life insurance primarily as investment vehicles. The Congress believed that a limitation on a customer's ability to select specific investments underlying a variable contract will help ensure that a customer's primary motivation in purchasing the contract is more likely to be the traditional economic protections provided by annuities and life insurance." Joint Committee on Taxation, *General Explanation of the Revenue Provisions of the Deficit Reduction Act of 1984*, Pub. L. No. 98-369, JCS-41-84, December 31, 1984, page 607.

[253] Treas. Reg. sec. 1.817-5(b).

[254] Treas. Reg. sec. 1.817-5(b)(2).

[255] Treas. Reg. sec. 1.817(f)(1).

[256] Treas. Reg. sec. 1.817(f)(2) and (3).

Explanation of Provision

Diversification requirements

The provision directs the Secretary of the Treasury to revise the regulations setting forth diversification requirements with respect to variable contracts under section 817(h) to facilitate the use of exchange-traded funds ("ETFs") under variable contracts. The provision directs that the lookthrough rule requirements in the regulations be amended so that satisfaction of those requirements with respect to an ETF is not prevented by reason of beneficial interests in an investment fund being held by one or more authorized participants or market makers.

Under the provision, an ETF means a RIC, partnership, or trust that is registered with the SEC as an open-end investment company or unit investment trust, and the shares of which can be purchased or redeemed directly from the fund only by an authorized participant, and the shares of which are traded throughout the day on a national stock exchange at market prices that may or may not be the same as the net asset value of the shares. An authorized participant means a financial institution that is a member or participant in a clearing agency registered under section 17A(b) of the Securities Exchange Act of 1934 that contracts with an ETF to permit the financial institution to purchase or redeem shares of the ETF and to sell the shares to third parties, provided that the financial institution is precluded from purchasing the shares for its own investment purposes and from selling the shares to persons that are not market makers. A market maker means a financial institution that is a registered broker or dealer under section 15(b) of the Securities Exchange Act of 1934 and that maintains liquidity for an ETF on a national stock exchange by always being ready to buy and sell shares, provided that the financial institution is precluded from buying or selling shares to or from persons who are not authorized participants or who are persons not permitted to buy or sell shares under the lookthrough rule in the regulations.

Effective Date

The provision relating to the amendments to the regulatory diversification requirements is effective for segregated asset account investments made on or after the date that is seven years after the date of enactment.

C. Simplification and Clarification of Retirement Plan Rules

1. Recovery of retirement plan overpayments

Present Law

Employee Plans Compliance Resolution System

A general description of the Employee Plans Compliance Resolution System that this provision modifies may be found in section A.13 of this document.

Recoupment of overpayments

An overpayment is defined as a qualification failure due to a payment being made to a participant or beneficiary that exceeds the amount payable to such individual under the terms of the plan or that exceeds a limitation provided in the Code or regulations.[257] Overpayments include both payments from a defined benefit plan and from a defined contribution plan (either not made from the individual's account under the plan or not permitted to be paid under the Code, the regulations, or the terms of the plan).

An overpayment from a defined benefit plan generally is corrected either by having the plan sponsor take reasonable steps to have the overpayment (with appropriate interest) returned by the recipient to the plan and then reducing future benefit payments (if any) due to the employee or any other appropriate correction method.[258] Depending on the nature of the overpayment, an appropriate correction method may include having the employer or another person contribute the amount of the overpayment (with appropriate interest) to the plan instead of seeking recoupment from a plan participant or beneficiary. Another appropriate correction method may include a plan sponsor adopting a retroactive amendment to conform the plan document to the plan's operations.

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[257] Sec. 5.01(3)(c) of Rev. Proc. 2019-19.

[258] Sec. 6.06(3) of Rev. Proc. 2019-19. Prior to 2015, the correction method for overpayments was solely for the employer to take reasonable steps to have the overpayment returned to the plan by the participant or beneficiary. The IRS was informed that some plans had demanded recoupment of large amounts from plan participants and beneficiaries on account of plan administration errors made over lengthy periods of time, and that those individuals, particularly older individuals, might have financial difficulty meeting those corrective actions including the return of overpayments with substantial accumulated interest. As a result, IRS and Treasury issued Revenue Procedure 2015-27, 2015-16 I.R.B. 914 providing more flexibility to plans, stating that depending on the facts and circumstances, correcting an overpayment under EPCRS may not need to include requesting that an overpayment be returned to the plan by plan participants and beneficiaries but could include such options as having the employer or another person contribute the amount of the overpayment (with appropriate interest) to the plan in lieu of seeking recoupment from plan participants and beneficiaries or having a plan sponsor adopt a retroactive amendment to conform the plan document to the plan's operations. Treasury and IRS requested comments on a number of issues, including whether, and under what circumstances, correction should require employer make-whole contributions rather than recouping overpayments from participants and beneficiaries and whether additional guidance was needed related to unusual circumstances in which full corrective payments to a plan should not be required. Treasury and IRS are continuing to review these comments and have indicated that they are in the process of developing further changes.

An overpayment from a defined contribution plan or section 403(b) plan is generally corrected by having the employer take reasonable steps to have the overpayment repaid to the plan, adjusted for earnings at the plan's earnings rate from the date of the distribution to the date of the correction of the overpayment.[259] To the extent such a repayment is not made by the participant or beneficiary, the employer or another person must contribute the difference to the plan ("make-whole contribution method"). The make-whole contribution method does not apply when the failure arises solely because a payment was made from the plan to a participant or beneficiary in the absence of a distributable event (but was otherwise determined in accordance with the terms of the plan (for example, an impermissible in-service distribution).

The employer must generally notify the employee that the overpayment is not eligible for favorable tax treatment accorded to distributions from an eligible retirement plan (and specifically, is not eligible for tax-free rollover).

However, if the total amount of an overpayment to a participant or beneficiary is $100 or less, the plan sponsor is not required to seek the return of the overpayment from the participant or beneficiary and the plan sponsor is not required to notify the participant or beneficiary that the overpayment is not eligible for favorable tax treatment accorded to distributions from the plan (and specifically, is not eligible for tax-free rollover).

PBGC overpayment recoupment policy

Private defined benefit plans are covered by the Pension Benefit Guaranty Corporation ("PBGC") insurance program, under which the PBGC guarantees the payment of certain plan benefits, and plans are required to pay annual premiums to the PBGC.[260] Single-employer and multiple-employer plans, including CSEC plans, are subject to the same PBGC premium requirements, consisting of flat-rate, per participant premiums and variable rate premiums, based on the unfunded vested benefits under the plan. For 2021, flat-rate premiums are $86 per participant, and variable rate premiums are $46 for each $1,000 of unfunded vested benefits, subject to a limit of $582 multiplied by the number of plan participants.[261] For this purpose, unfunded vested benefits under a plan for a plan year is the excess (if any) of (1) the plan's funding target for the plan year, determined by taking into account only vested benefits and using specified interest rates, over (2) the fair market value of plan assets.

If at any time, the PBGC determines that net benefits paid to a participant in a PBGC-trusteed plan exceed the total amount to which the participant or beneficiary is entitled up to that time under Title IV of ERISA, and the participant or beneficiary is, as of the plan termination date, entitled to receive future benefits, the PBGC will recoup the net overpayment by calculating a monthly account balance for each month ending after the termination date. The PBGC will subtract from the account balance the amount of overpayments made in that month. Only overpayments made on or after the latest of the proposed termination date, the termination

[259] Sec. 6.06(4) of Rev. Proc. 2019-19.

[260] Title IV of ERISA.

[261] These premium rates have been increased several times by legislation since 2005 and are subject to automatic increases to reflect inflation (referred to as "indexing").

date, or, if no notice of intent to terminate was issued, the date on which proceedings to terminate the plan are instituted by the PBGC.

The PBGC will recoup net overpayments of benefits by reducing the amount of each future benefit payment to which the participant or beneficiary is entitled by a fraction which is determined by dividing the amount of the net overpayment by the present value of the benefit payable with respect to the participant or beneficiary under Title IV of ERISA. The PBGC will reduce benefits to a participant or beneficiary by no more than the greater of (1) 10 percent per month; or (2) the amount of benefit per month in excess of the maximum guaranteed benefit payable under ERISA, determined without adjustment for age and benefit form. Before affecting a benefit reduction, PBGC will notify the participant or beneficiary in writing of the amount of the net overpayment and of the amount of the reduced benefit. The PBGC may, in its discretion, decide not to recoup net overpayments that it determines to be de minimis.

Description of Proposal

Overpayments under the Code

Under the proposal, a plan will not fail to be treated as a qualified plan, section 403(a) annuity, section 403(b) tax sheltered annuity or a governmental plan[262] (and will not fail to be treated as satisfying the requirements of section 401 or 403) merely because (1) the plan fails to obtain payment from any participant, beneficiary, employer, plan sponsor, fiduciary, or other party on account of any inadvertent benefit overpayment made by the plan, or (2) the plan sponsor amends the plan to increase past or future benefit payments to affected participants and beneficiaries in order to adjust for prior inadvertent benefit overpayments. Notwithstanding the foregoing, the plan may instead reduce future benefit payments to the correct amount provided for under the terms of the plan or seek recovery from the person or persons responsible for the overpayment. If an employer decides not to recover an overpayment, nothing in this proposal relieves that employer of any obligation imposed upon it to make contributions to a plan to satisfy the minimum funding requirements[263] or to prevent or restore an impermissible forfeiture.[264] In addition, the plan must observe any salary, compensation or benefit limitations imposed upon it,[265] and may enforce such limitations using any method approved by the Secretary for recouping benefits previously paid or allocations previously made in excess of such limitations.

The Secretary may issue regulations or other guidance of general applicability specifying how benefit overpayments and their recoupment or non-recoupment from a participant or beneficiary are to be taken into account for purposes of satisfying any requirement applicable to such a plan.

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[262] Under section 219(g)(5)(A)(i), (ii), (iii) or (iv).

[263] Under sections 412 and 430.

[264] In accordance with section 411.

[265] Secs. 401(a)(17) and 415.

Rollovers

In the case of an inadvertent benefit overpayment from a plan which is transferred to an eligible retirement plan by or on behalf of a participant or beneficiary, (1) the portion of the overpayment with respect to which recoupment is not sought on behalf of the plan will be treated as having been paid in an eligible rollover distribution if the payment would have been an eligible rollover distribution but for being an overpayment, and (2) the portion of such overpayment with respect to which recoupment is sought on behalf of the plan will be permitted to be returned to the plan, and in such case, will be treated as an eligible rollover distribution transferred to such plan by the participant or beneficiary who received the overpayment (and the plans making and receiving such transfer will be treated as permitting such transfer).

In any case in which recoupment is sought on behalf of the plan, but is disputed by the participant or beneficiary who received the overpayment, where the recoupment has been transferred to another eligible retirement plan, the dispute will be subject to the claims and appeals procedures of the plan that made the overpayment, that plan will notify the plan receiving the rollover of the dispute, and the plan receiving the rollover will retain the overpayment on behalf of the participant or beneficiary (and will be entitled to treat the overpayment as plan assets) pending the outcome of the procedures.

Overpayments under ERISA

Fiduciary duties

Under the proposal, in the case of an inadvertent benefit overpayment by any pension plan, the responsible plan fiduciary will not be considered to have failed to comply with its fiduciary responsibilities merely because such fiduciary determines, in the exercise of its fiduciary discretion, not to seek recovery of all or pay of such overpayment from:

1. Any participant or beneficiary;

2. Any plan sponsor of, or contributing employer to, (a) an individual account plan, provided that the amount needed to prevent or restore any impermissible forfeiture from any participant's or beneficiary's account arising in connection with the overpayment is, separately from and independently of the overpayment, allocated to such account pursuant to the nonforfeitability requirements of ERISA[266] (for example, out of the plan's forfeiture account, additional employer contributions, or recoveries from those responsible for the overpayment), or (b) a defined benefit pension plan subject to the funding rules of ERISA,[267] unless the responsible plan fiduciary determines, in the exercise of its fiduciary discretion, that failure to recover all or a part of the overpayment faster than required under such funding rules would

[266] Sec. 203.

[267] In part 3 of subtitle B of ERISA.

materially affect the plan's ability to pay benefits due to other participants and beneficiaries; or

3. Any fiduciary of the plan, other than a fiduciary (including a plan sponsor or contributing employer acting in a fiduciary capacity) whose breach of its fiduciary duties resulted in such overpayment, provided that if the plan has established prudent procedures to prevent and minimize overpayment of benefits and the relevant plan fiduciaries have followed such procedures, an inadvertent benefit overpayment will not give rise to a breach of fiduciary duty. Notwithstanding the foregoing, the responsible plan fiduciary may instead reduce future benefit payments to the correct amount provided for under the terms of the plan or seek recovery from the person or persons responsible for the overpayment.

If an employer decides not to recover an overpayment, nothing in this proposal relieves that employer of any obligation imposed upon it to make contributions to a plan to satisfy the minimum funding requirements[268] or to prevent or restore an impermissible forfeiture.[269]

Conditions imposed upon recoupment

If the responsible plan fiduciary, in the exercise of its fiduciary discretion, decides to seek recoupment from a participant or beneficiary of all or part of an inadvertent benefit overpayment made by the plan to such participant or beneficiary, it may do so, subject to the following conditions:

1. No interest or other additional amounts (such as collection costs or fees) are sought on overpaid accounts;

2. If the plan seeks to recoup past overpayments of a non-decreasing periodic benefit by reducing future benefit payments:

    - The reduction ceases after the plan has recovered the full dollar amount of the overpayment;
    - The amount recouped each calendar year does not exceed 10 percent of the full dollar amount of the overpayment; and
    - Future benefit payments are not reduced to below 90 percent of the periodic amount otherwise payable under the terms of the plan.

3. Alternatively, if the plan seeks to recoup past overpayments of a non-decreasing periodic benefit through one or more installment payments, the sum of such installment payments in any calendar year does not exceed the sum of the reductions that would be permitted in such year under the preceding sentence;

[268] Under part 3 of Subtitle B of Title I of ERISA.

[269] In accordance with section 203 of ERISA.

4. If the plan seeks to recoup past overpayments of a benefit other than a non-decreasing periodic benefit, the plan satisfies requirements developed by the Secretary;

5. Efforts to recoup overpayments are not made through a collection agency or similar third party and such efforts are not accompanied by threats of litigation, unless the responsible plan fiduciary reasonably believes it could prevail in a civil action brought in Federal or State court to recoup the overpayments;

6. Recoupment of past overpayments to a participant is not sought from any beneficiary of the participant, including a spouse, surviving spouse, former spouse or other beneficiary;

7. Recoupment may not be sought if the first overpayment occurred more than three years before the participant or beneficiary is first notified in writing of the error;

8. A participant or beneficiary from whom recoupment is sought is entitled to contest all or part of the recoupment pursuant to the plan's claims and appeals procedures; and

9. In determining the amount of recoupment to seek, the responsible plan fiduciary may take into account the hardship that recoupment likely would impose on the participant or beneficiary.

Conditions (1) through (6) shall not apply to protect a participant or beneficiary who is culpable. For purposes of this rule, a participant or beneficiary is culpable if the individual bears responsibility for the overpayment (such as through misrepresentations or omissions that led to the overpayment), or if the individual knew, or had good reason to know under the circumstances, that the benefit payment or payments were materially in excess of the correct amount. Notwithstanding the preceding sentence, an individual is not culpable merely because the individual believed the benefit payment or payments were or might be in excess of the correct amount, if the individual raised that question with an authorized plan representative and was told the payment or payments were not in excess of the correct amount. With respect to a culpable participant or beneficiary, efforts to recoup overpayments shall not be made through threats of litigation, unless a lawyer for the plan could make the representations required under Rule 11 of the Federal Rules of Civil Procedure if the litigation were brought in Federal court.

Effective Date

The proposal applies on the date of enactment.

Plans, fiduciaries, employers, and plan sponsors are entitled to rely on (1) a good faith interpretation of then existing administrative guidance for inadvertent benefit overpayment recoupments and recoveries that commenced before the date of enactment and (2) determinations made before the date of enactment by the responsible plan fiduciary, in the exercise of its fiduciary discretion, not to seek recoupment or recovery of all or part of an inadvertent benefit overpayment.

In the case of a benefit overpayment that occurred prior to the date of enactment, any installment payments by the participant or beneficiary to the plan or any reduction in periodic

benefit payments to the participant or beneficiary, which were made in recoupment of such overpayment and which commenced prior to such date, may continue after such date. Nothing in this subsection shall relieve a fiduciary from responsibility for an overpayment that resulted from a breach of its fiduciary duties.

2. Reduction in excise tax on certain accumulations in qualified retirement plans

Present Law

Background on required minimum distributions under qualified retirement plans may be found in section A.5. of this document.

The Code imposes an excise tax on an individual if the amount distributed to an individual during a taxable year is less than the required minimum distribution under the plan for that year.[270] The excise tax is equal to 50 percent of the shortfall (that is, 50 percent of the amount by which the required minimum distribution exceeds the actual distribution). However, the Secretary may waive the tax if the individual establishes that the shortfall was due to reasonable error and reasonable steps are being taken to remedy the error.

Description of Proposal

The proposal reduces the excise tax that generally applies to the failure to take required minimum distributions from 50 percent of the shortfall to 25 percent.

In addition, the proposal further reduces the excise tax to 10 percent in the case of an individual who, during the correction window, corrects the shortfall and submits a return reflecting the excise tax. The correction window is defined as the time period beginning on the date the excise tax is imposed on the shortfall and ending on the earlier of (1) the date the Secretary initiates an audit with respect to the shortfall or otherwise demands payment, and (2) the last day of the second taxable year that begins after the end of the taxable year in which the excise tax is imposed.

Effective Date

The proposal applies to taxable years beginning after December 31, 2021.

3. Performance benchmarks for asset allocation funds

Present Law

Fiduciary rules under ERISA

ERISA contains general fiduciary duty standards that apply to all fiduciary actions, including investment decisions. ERISA requires that a plan fiduciary generally discharge its duties solely in the interests of participants and beneficiaries and with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like

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[270] Sec. 4974.

capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. With respect to plan assets, ERISA requires a fiduciary to diversify the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so.

Special rule for participant control of assets

ERISA provides a special rule in the case of a defined contribution plan that permits participants to exercise control over the assets in their individual accounts. Under the special rule, if a participant exercises control over the assets in his or her account (as determined under regulations), the participant is not deemed to be a fiduciary by reason of such exercise, and no person who is otherwise a fiduciary is liable for any loss, or by reason of any breach, that results from the participant's exercise of control.

Regulations issued by the Department of Labor describe the requirements that must be met in order for a participant to be treated as exercising control over the assets in his or her account. With respect to investment options, the regulations provide in part:

- The plan must provide at least three different investment options, each of which is diversified and has materially different risk and return characteristics;
- The plan must allow participants to give investment instructions with respect to each investment option under the plan with a frequency that is appropriate in light of the reasonably expected market volatility of the investment option (the general volatility rule);
- At a minimum, participants must be allowed to give investment instructions at least every three months with respect to at least three of the investment options, and those investment options must constitute a broad range of options (the three-month minimum rule);
- Participants must be provided with detailed information about the investment options, information regarding fees, investment instructions and limitations, and copies of financial data and prospectuses; and
- Specific requirements must be satisfied with respect to investments in employer stock to ensure that employees' buying, selling, and voting decisions are confidential and free from employer influence.

Under the regulations,[271] the plan administrator (or person designated by the plan administrator to act on its behalf), based on the latest information available, must furnish to each participant or beneficiary on or before the date on which he or she can first direct his or her investments and at least annually thereafter, the following information (as well as certain other information), with respect to each designated investment alternative offered under the plan:

[271] 29 C.F.R. sec. 2550.404a-5(d).

- *Identifying information* including the name of each designated investment alternative and the type or category of the investment (*e.g.*, money market fund, balanced fund (stocks and bonds), large-cap stock fund, employer securities);
- *Performance data* including:
    - For designated investment alternatives with respect to which the return is not fixed, the average annual total return of the investment for 1-, 5-, and 10-calendar year periods (or for the life of the alternative, if shorter) ending on the date of the most recently completed calendar year; as well as a statement indicating that an investment's past performance is not necessarily an indication of how the investment will perform in the future; and
    - For designated investment alternatives with respect to which the return is fixed or stated for the term of the investment, both the fixed or stated annual rate of return and the term of the investment. If, with respect to such a designated investment alternative, the issuer reserves the right to adjust the fixed or stated rate of return prospectively during the term of the contract or agreement, the current rate of return, the minimum rate guaranteed under the contract, if any, and a statement advising participants and beneficiaries that the issuer may adjust the rate of return prospectively and how to obtain (*e.g.*, telephone or website) the most recent rate of return required under this section.
- *Benchmarks.* For designated investment alternatives with respect to which the return is not fixed, the name and returns of an appropriate broad-based securities market index over the 1-, 5-, and 10-calendar year periods (or for the life of the alternative, if shorter) comparable to the performance data periods provided for designated investment alternatives with respect to which the return is not fixed, and which is not administered by an affiliate of the investment issuer, its investment adviser, or a principal underwriter, unless the index is widely recognized and used.

If these and the other requirements under the regulations are met, a plan fiduciary may be liable for the investment options made available under the plan, but not for the specific investment decisions made by participants. However, the regulations currently do not provide guidance as to a designated investment alternative which contains a mix of asset classes.

<u>Description of Proposal</u>

Not later than six months after the date of enactment, the proposal requires that the Secretary of Labor (or the Secretary's delegate) modify the regulations on fiduciary duties[272] to provide that, in the case of a designated investment alternative which contains a mix of asset classes, a plan administrator may, but is not required to, use a benchmark which is a blend of different broad-based securities market indices if:

[272] Under section 404 of ERISA.

1. The blend is reasonably representative of the asset class holdings of the designated investment alternative;

2. For purposes of determining the blend's returns for 1-, 5-, and 10-calendar-year periods (or for the life of the alternative, if shorter), the blend is modified at least once per year to reflect changes in the asset class holdings of the designated investment alternative;

3. The blend is furnished to participants and beneficiaries in a manner that is reasonably designed to be understandable and helpful; and

4. Each securities market index which is used for an associated asset class would separately satisfy the requirements of such regulations for such asset class.

Not later than December 31, 2022, the Secretary of Labor (or the Secretary's delegate) must deliver a report to the Committees on Ways and Means and Education and Labor of the House of Representatives and the Committees on Finance and Health, Education, Labor, and Pensions of the U.S. Senate regarding the effectiveness of the benchmarking requirements under Department of Labor regulations.[273]

Effective Date

The proposal is effective on the date of enactment.

4. Review and report to the Congress relating to reporting and disclosure requirements

Present Law

Under the Code and ERISA, plans must satisfy requirements relating to reporting and disclosure of plan information. These requirements include information required to be reported to the IRS, the Department of Labor ("DOL"), and the Pension Benefit Guaranty Corporation ("PBGC"), as well as to participants and beneficiaries.[274]

For example, plan administrators generally must file an annual return with the IRS, an annual report with the DOL, and certain information annually with the PBGC. Form 5500, which consists of a primary form and various schedules, includes the information required to be filed with all three agencies. The plan administrator satisfies the reporting requirement with respect to each agency by filing the Form 5500 with DOL. Other information required to be reported to the IRS includes plan distributions, excise taxes imposed on the plan, and separated participants with deferred vested benefits.[275] Defined benefit plans must report certain

[273] 29 C.F.R. sec. 2550.404a-5.

[274] In certain cases, plan information also must be provided to other interested parties such as unions (in the case of multiemployer plans).

[275] This information is reported on the Form 1099-R (plan distributions), Form 5330 (excise tax), and Form 8955-SSA (separated participants with deferred vested benefits).

information to PBGC, including information relating funding, terminations, and reportable events.

With respect to participants and beneficiaries, the reporting and disclosure requirements include the provision of a summary plan description, which describes the plan's eligibility requirements for participation and benefits, vesting provisions, procedures for claiming benefits under the plan, and other information.[276] Plans must also furnish participants and beneficiaries with periodic benefit statements that indicate the total benefits accrued and the nonforfeitable benefits (or the earliest date on which benefits become nonforfeitable).[277] Certain information is required to be provided upon certain events, such as termination of employment,[278] plan termination,[279] reduction in future benefit accruals,[280] or a plan distribution that is eligible for rollover treatment.[281] Certain requirements also apply depending on the type of plan. For example, section 401(k) plans and section 403(b) plans must advise employees of opportunities to make or change elective deferrals under the plan,[282] and section 401(k) safe harbor plans and plans with automatic enrollment features have special notice requirements.[283] Certain notices must be provided to participants and beneficiaries in individual account plans who are permitted to exercise control over account assets.[284] In the case of defined benefit plans, notices relating to plan funding, such as an annual funding notice, must be furnished to participants and beneficiaries.[285]

Description of Proposal

The proposal requires the Secretary, the Secretary of Labor, and PBGC to review the reporting and disclosure requirements that apply to pension plans[286] under Title I of ERISA and

[276] ERISA sec. 102; 29 C.F.R. sec. 2520.102-2 and -3. Plans must also provide summaries of material modifications to the plan. ERISA sec. 102.

[277] ERISA sec. 105.

[278] ERISA sec. 209.

[279] 29 C.F.R. sec. 2550.404a-3 (relating to termination of individual account plans); ERISA sec. 4041(a)(2) (relating to termination of single-employer defined benefits plans). Single employer defined benefit plans also must report plan termination to the PBGC.

[280] Sec. 4980F; ERISA sec. 204(h).

[281] Sec. 402(f).

[282] Treas. Reg. sec. 1.401(k)-1(e)(2)(ii); Treas. Reg. sec. 1.403(b)-5(b)(2). This requirement also applies to SIMPLE plans. Sec. 408(p)(5)(C).

[283] Sec. 401(k)(12)(D); sec. 401(k)(13)(E); sec. 414(w)(4).

[284] ERISA sec. 404(c).

[285] ERISA sec. 101. Certain notices related to plan funding also must be provided to PBGC.

[286] ERISA sec. 3(2).

that apply to qualified retirement plans[287] under the Code. Such review must take place as soon as practicable after the date of enactment, and, no later than 18 months after such date, the agencies must report on the effectiveness of the reporting and disclosure requirements and make certain recommendations, as described below, to the appropriate committees of the Congress. The agencies must conduct appropriate surveys and data collection to obtain any needed information.

The report must include the following:

- Recommendations as may be appropriate to consolidate, simplify, standardize, and improve such requirements so as to simplify reporting for such plans and ensure that plans can simply furnish and participants and beneficiaries timely receive and better understand the information they need to monitor their plans, plan for retirement, and obtain the benefits they have earned;
- An assessment of the extent to which retirement plans are retaining disclosures, work records, and plan documents that are needed to ensure accurate calculation of future benefits; and
- To assess the effectiveness of the applicable reporting and disclosure requirements, an analysis, based on plan data, of how participants and beneficiaries are providing preferred contact information, the methods by which plan sponsors and plans are furnishing disclosures, and the rate at which participants and beneficiaries (grouped by key demographics) are receiving, accessing, and retaining disclosures.

Effective Date

The proposal is effective on date of enactment.

5. Eliminating unnecessary plan requirements related to unenrolled participants

Present Law

Background on the reporting and disclosure requirements that apply to plans under the Code and ERISA may be found in section C.4. of this document.

Description of Proposal

The proposal generally exempts defined contribution plans from requirements under the Code and ERISA to provide disclosures, notices, and other plan documents to unenrolled participants, provided that the unenrolled participant receives: (1) an annual reminder notice of the participant's eligibility to participate in the plan and any applicable election deadlines, and (2) any document the participant requests that the participant would be entitled to if not for this proposal.

[287] For this purpose, qualified retirement plans include plans qualified under section 401(a), annuity plans described in section 403(a), and section 403(b) plans. Sec. 4974(c)(1), (2), and (3).

Under the proposal, the annual reminder notice must be furnished in connection with the plan's annual open season election period (or, if there is no such period, within a reasonable period prior to the beginning of each plan year), and must notify the participant of (1) the participant's eligibility to participate in the plan, and (2) the key benefits under the plan and key rights and features under the plan affecting such benefits. The annual reminder notice must be provided in accordance with the Department of Labor regulations relating to disclosure[288] and may be provided in paper or, if the participant consents, electronically. The notice must provide the required information in a prominent manner calculated to be understood by the average participant.

The proposal defines "unenrolled participant" as an employee who (1) is eligible to participate in a defined contribution plan; (2) has received all required notices, disclosures, and other plan documents, including the summary plan description, required to be furnished under the Code or ERISA in connection with the participant's initial eligibility to participate in the plan; (3) is not participating the plan; and (4) does not have a balance in the plan. For this purpose, any eligibility to participate in the plan following any period of ineligibility is treated as initial eligibility.

Effective Date

The proposal is effective for plan years beginning after December 31, 2021.

6. Retirement savings lost and found

Present Law

Pension Benefit Guaranty Corporation Missing Participants Program

When a defined benefit pension plan (maintained by a single employer and subject to the plan termination insurance program under Title IV of ERISA) terminates under a standard termination, the plan administrator generally must purchase annuity contracts from a private insurer to provide the benefits to which participants are entitled and distribute the annuity contracts to the participants.

If the plan administrator of a terminating single employer plan cannot locate a participant after a diligent search (has a "missing participant"), the plan administrator may satisfy the distribution requirement only by purchasing an annuity from an insurer or transferring the participant's designated benefit to the Pension Benefit Guaranty Corporation ("PBGC"). The PBGC holds the benefit of the missing participant as trustee until the PBGC locates the missing participant and distributes the benefit.[289]

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[288] 29 C.F.R. sec. 2520.104(b)-1 (or any successor regulation).

[289] Sec. 4041(b)(3)(A); sec. 4050 of ERISA.

Pursuant to the Pension Protection Act of 2006,[290] the PBGC prescribed rules for terminating multiemployer plans similar to the missing participant rules applicable to terminating single employer plans subject to Title IV of ERISA. In addition, plan administrators of certain types of plans not otherwise subject to the PBGC termination insurance program are permitted, but not required, to elect to transfer missing participants' benefits to the PBGC upon plan termination. Specifically, the provision extends the missing participants program (in accordance with regulations) to defined contribution plans[291], defined benefit pension plans that have no more than 25 active participants and are maintained by professional service employers, and the portion of defined benefit pension plans that provide benefits based upon the separate accounts of participants and therefore are treated as defined contribution plans under ERISA.

On December 22, 2017, PBGC established the PBGC Defined Contribution Missing Participants Program ("Missing Participants Program") to hold retirement benefits for missing participants and beneficiaries in most terminated defined contribution plans and to help those participants and beneficiaries find and receive those benefits.[292]

<u>Department of Labor</u>

A fiduciary safe harbor[293] may apply with respect to distributions from terminated individual account plans[294] and abandoned plans[295] on behalf of participants and beneficiaries who fail to make an election regarding a form of benefit distribution, including "missing participants." The safe harbor generally requires that distributions be rolled over to an individual retirement account or annuity (IRA), although in limited circumstances fiduciaries may make distributions to certain bank accounts or to a state unclaimed property fund. If the conditions of the safe harbor are met, a fiduciary (including a Qualified Termination Administrator ("QTA") in the case of an abandoned plan) is deemed to have satisfied the requirements of section 404(a) of ERISA with respect to distributing benefits, selecting a transferee entity, and investing funds in connection with the distribution.

The Department of Labor ("DOL") consulted with the PBGC during the PBGC's development of its Missing Participants Program. As noted in the preamble to the final rule adopting the Missing Participants Program, the DOL may revise its fiduciary safe harbor

[290] Pub. L. No. 109-280, August 17, 2006.

[291] The Missing Participants program for Defined Contribution plans covers common types of defined contribution pension plans; specifically section 401(k) plans, profit sharing plans, money purchase plans, target benefit plans, employee stock ownership plans, stock bonus plans, and section 403(b)(7) plans subject to Title I of ERISA. Some examples of plans not covered are governmental plans, church plans, and plans that cannot pay benefits to PBGC in cash. See 29 C.F.R. sec. 4050.201.

[292] 29 C.F.R. sec. 4050.201-207.1.

[293] 29 C.F.R. sec. 2550.404a–3.

[294] Sec. 3(34) of ERISA.

[295] As described in 29 C.F.R. sec. 2578.1

regulation so that transfers to the PBGC by terminating individual account plans would be eligible for relief under the safe harbor.

On January 12, 2021, the DOL issued Field Assistance Bulletin 2021-01[296] in which it announced that pending further guidance, the Department of Labor will not pursue fiduciary violations against either responsible plan fiduciaries of terminating defined contribution plans or QTAs of abandoned plans[297] in connection with the transfer of a missing or non-responsive participant's or beneficiary's account balance to the PBGC in accordance with the PBGC's missing participant regulations (rather than to an IRA, certain bank accounts, or to a state unclaimed property fund),[298] if the plan fiduciary or QTA complies with the guidance in the Bulletin and has acted in accordance with a good faith, reasonable interpretation of the fiduciary rules under ERISA[299] with respect to matters not specifically addressed in the memorandum.

Mandatory rollovers

If a qualified retirement plan participant ceases to be employed by the employer that maintains the plan, the plan may distribute the participant's nonforfeitable accrued benefit without the consent of the participant and, if applicable, the participant's spouse, if the present value of the benefit does not exceed $5,000. If such an involuntary distribution occurs and the participant subsequently returns to employment covered by the plan, then service taken into account in computing benefits payable under the plan after the return need not include service with respect to which a benefit was involuntarily distributed unless the employee repays the benefit.

Generally, a participant may roll over an involuntary distribution from a qualified plan to an IRA or to another qualified plan. Before making a distribution that is eligible for rollover, a plan administrator must provide the participant with a written explanation of the ability to have the distribution rolled over directly to an IRA or another qualified plan and the related tax consequences.

A direct rollover is the default option for involuntary distributions that exceed $1,000 and that are eligible rollover distributions from qualified retirement plans. The distribution must be rolled over automatically to a designated IRA, unless the participant affirmatively elects to have the distribution transferred to a different IRA or a qualified plan or to receive it directly. The written explanation provided by the plan administrator is required to explain that an automatic direct rollover will be made unless the participant elects otherwise. The plan administrator is also required to notify the participant in writing (as part of the general written explanation or separately) that the distribution may be transferred without cost to another IRA.

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[296] Field Assistance Bulletin 2021-01 can be found at: https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2021-01.

[297] As described in 29 C.F.R. sec. 2578.1.

[298] As specified in 29 C.F.R. sec. 2550.404a-3.

[299] Sec. 404 of ERISA.

Under the fiduciary rules of ERISA, in the case of an automatic direct rollover, the participant is treated as exercising control over the assets in the IRA upon the earlier of: (1) the rollover of any portion of the assets to another IRA, or (2) one year after the automatic rollover.

Lost and Found

Under present law, there is not a "Lost and Found" database to collect information on benefits owed to missing, lost or non-responsive participants and beneficiaries in tax-qualified retirement plans (other than terminated plans) and to assist such plan participants and beneficiaries in locating those benefits.

Description of Proposal

Establishment of the Lost and Found

Under the proposal, not later than three years after the date of enactment, the Secretary of Labor, the Secretary of the Treasury, and the Secretary of Commerce, in cooperation, will establish an online searchable database to be managed by the PBGC,[300] to be known as the Retirement Savings Lost and Found (the "Lost and Found"), containing information on plans, subject to the vesting standards under ERISA,[301] as well as certain additional information related to the location of certain unclaimed vested benefits of missing, lost and non-responsive participants and beneficiaries in such plans.[302] The Lost and Found database will contain information: (1) provided by plan administrators that are required to periodically report to the Office of the Lost or Found each plan year;[303] (2) provided by plan administrators that transfer certain small benefits of non-responsive participants and beneficiaries to the Lost and Found; and (3) other relevant information obtained by PBGC.

The collection of this information in the Lost and Found would allow the PBGC to assist participants and beneficiaries by providing contact information[304] on record for the plan administrator of any plan in which the participant or beneficiary may have an unclaimed benefit sufficient to allow that participant or beneficiary to locate the individual's plan in order to recover any benefit owing to that individual under the plan. With respect to those plans which have transferred such benefits to the PBGC, the PBGC would also be able to pay those benefits to such participants and beneficiaries. Because the PBGC would be provided additional and updated information from plan administrators through reporting requirements, the PBGC would

[300] The Office of the Retirement Savings Lost and Found will be established within the PBGC to maintain the Retirement Savings Lost and Found.

[301] Sec. 203 of ERISA.

[302] Tax-qualified defined benefit and defined contribution plans (as set forth in 29 C.F.R. sec. 4050.201) that are subject to the vesting standards contained in section 203 of ERISA.

[303] In accordance with section 4051 of ERISA, as added to this proposal. See also, discussion of *Annual Reporting Requirements* below.

[304] Such individuals will be provided only with the ability to view contact information for the plan administrator of any plan with respect to which the individual is or was a participant or beneficiary.

be able to make any necessary changes to the database reflecting updates to contact information on record for the plan administrator based on any changes to such plans including those arising from mergers or consolidations of the plan with any other plan, division of the plan into two or more plans, bankruptcy, termination, change in name of the plan, change in name or address of the plan administrator, transfers of such accounts to IRAs, purchase of annuities, or other causes.

Safeguarding Participant Privacy and Security

In establishing the Lost and Found, the PBGC, in consultation with the Secretary of Labor, the Secretary of Treasury, and the Secretary of Commerce must take all necessary and proper precautions to ensure that individuals' plan information maintained by the Lost and Found is protected and that persons other than the individual cannot fraudulently claim the benefits to which any individual is entitled, and to allow any individual to opt out of inclusion in the Lost and Found at the election of the individual.

Establishment and responsibilities of the Office of the Retirement Savings Lost and Found

Not later than two years after the date of the enactment of this Act, the Secretary of Labor, the Secretary of Treasury, and the Secretary of Commerce must establish, within the PBGC, an Office of the Retirement Savings Lost and Found ("Office of the Lost and Found").

The "Office of the Lost and Found" will (1) maintain the Lost and Found database; (2) facilitate the transfer of small benefits of non-responsive participants and beneficiaries[305] to the Office of the Lost and Found by (a) collecting information, applicable fees, and benefits related to such individuals from the applicable plan; (b) investing such benefits; (3) searching for and paying out benefits to those participants and beneficiaries for whom benefits have been transferred to the Office of the Lost and Found; and (4) performing an annual audit of plan information contained in the Lost and Found and ensuring that such information is current and accurate.

[305] In defined benefit and defined contribution plans subject to the vesting requirements of section 203 of ERISA.

Required transfer of small benefits of certain non-responsive participants by plans to the Office of the Lost and Found

Under the proposal, the administrator of a plan that is not terminated[306] must transfer a non-responsive participant's[307] benefit to the Office of the Lost and Found[308] if the nonforfeitable accrued benefit[309] is no greater than $1,000.

Upon making a transfer to the Office of the Lost and Found of small benefits of non-responsive participants, the plan administrator must provide such information and certifications as the Office of the Lost and Found specifies including with respect to the transferred amount of the benefit and the identification of the non-responsive participant. In the event that, after such a transfer, the relevant non-responsive participant contacts the plan administrator or the plan administrator discovers information that may assist the Office of the Lost and Found in locating the non-responsive participant, the plan administrator must notify and provide such information to the Office of the Lost and Found as such Office specifies.

A transfer of such benefits to the Office of the Lost and Found under this proposal will be treated as a transfer to an individual retirement plan. Such benefits will be held in a new ninth fund[310] established for the payment of such benefits[311] which fund will also be credited with earnings on investments in the fund or on assets credited to the fund. Whenever the PBGC determines that the moneys of any fund are in excess of current needs, it may request the investment of such amounts as it determines advisable by the Secretary in obligations issued or guaranteed by the United States.

Following a transfer of such benefits to the Office of the Lost and Found, the Office of the Lost and Found shall periodically, and upon receiving information from the plan administrator as described above, conduct a search for the non-responsive participant for whom the Office of the Lost and Found has received a transfer. Upon location of such a non-responsive participant who claims benefits, the Office of the Lost and Found shall pay the non-responsive participant the amount transferred to it in a single sum (plus an amount reflecting the return on the investment attributable to such amount). The PBGC has the regulatory authority to prescribe regulations as are necessary to carry out the transfer of small benefits including rules relating to the amount payable to the Office of the Lost and Found by the plan administrator and the amount to be paid

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[306] And to which section 401(a)(31)(B) of the Code applies.

[307] For this proposal, a non-responsive participant means a participant or beneficiary of a plan who is entitled to a benefit subject to a mandatory transfer under section 401(a)(31)(B)(iii) and for whom the plan has satisfied the conditions in section 401(a)(31)(B)(iv).

[308] Under sec. 401(a)(31)(B) and section 4051(b) of ERISA.

[309] Under sec. 401(a)(31)(B) and section 4051(b) of ERISA.

[310] For amounts transferred to the Lost and Found under section 4051(b)(1)(A).

[311] Pursuant to sec. 4005(j) as set forth in this proposal.

to the non-responsive participant or beneficiary by the Office of the Lost and Found when that individual is located.

Annual reporting requirements

Under the proposal, within such period after the end of each plan year beginning after the second December 31 occurring after the date of enactment, as the Office of the Lost and Found may prescribe, the plan administrator of a plan to which the vesting standards of ERISA apply[312] will submit the following information, and such other information as the Office of the Lost and Found may require:[313]

- The name of the plan;
- The name and address of the plan administrator;
- Any change in the name of the plan;
- Any change in the name or address of the plan administrator;
- The name and taxpayer identifying number of each participant or former participant in the plan:
    - Who, during the current plan year or any previous plan year, was reported to IRS[314] as a separated participant with a deferred vested benefit that had not been paid as of the end of the previous plan year, and with respect to whom such benefit was fully paid during the plan year;
    - With respect to whom any amount was distributed as a mandatory distribution during the plan year; or
    - With respect to whom a deferred annuity contract was distributed during the plan year;
- The termination of the plan
- The merger or consolidation of the plan with any other plan or its division into two or more plans;
- In the case of a participant or former participant whose benefit was distributed as a mandatory distribution during the plan year, the name and address of the designated trustee or issuer and the account number of the individual retirement plan to which the amount was distributed; and

[312] Sec. 203 of ERISA.

[313] Because this reporting begins approximately two years after the date of enactment, unless the Office of the Lost and Found prescribes otherwise, this information will only be provided to the Office of the Lost and Found prospectively.

[314] Under sec. 6057.

- In the case of a participant or former participant to whom a deferred annuity contract was distributed during the plan year, the name and address of the issuer of such annuity contract and the contract or certificate number.

Guidance

The Office of the Lost and Found shall prescribe such regulations as are necessary to carry out the purposes of this proposal, including rules relating to the amount payable to the Office of the Lost and Found and the amount to be paid by the Office of the Lost and Founds.

Option to contract

Not later than two years after the date of enactment, the PBGC must conduct an analysis of the cost effectiveness of contracting with a third party to carry out the responsibilities of the Office of the Lost and Found. If the PBGC determines that it would be more cost effective to do so than to carry out such responsibilities within the Office of the Lost and Found, the PBGC may enter into such contracts as merited by the analysis. The PBGC must report on the results of its analysis to the Committees on Finance and Health, Education, Labor, and Pensions of the Senate and the Committees on Ways and Means and Education and Labor of the House of Representatives.

Authorization of Appropriations

There are authorized to be appropriated such sums as may be necessary to carry out the purposes of the Lost and Found.

Mandatory Transfers of Rollover Distributions and Coordination with Distribution Requirements

Investment options

The proposal amends ERISA[315] to provide that in the case of a pension plan which makes a transfer to an IRA under the mandatory distribution rules under the Code,[316] that the Secretary of Labor may provide, in guidance or regulations issued after the enactment of this proposal, that such transfer may be made to:

- A target date or life cycle fund held under such account;
- An investment product held under such account designed to preserve principal and provide a reasonable rate of return;[317]

[315] Sec. 404(c)(3) of ERISA.

[316] Sec. 401(a)(31)(B).

[317] As described in 29 C.F.R. sec. 2550.404a-2.

- The Office of the Lost and Found in accordance with the mandatory distribution rules in the Code[318] rules in this proposal for the transfer of certain benefits to the Office of the Lost and Found; or
- Such other option as the Secretary of Labor may so provide.

Not later than 270 days after the date of enactment, the Secretary of Labor must promulgate regulations identifying the target date or life cycle funds, or specifying the characteristics of such a fund, that will be deemed to meet the applicable requirements of ERISA.[319]

Expansion of cap

The proposal increases the cap on mandatory distributions from $5,000 to $6,000.[320]

Distribution of larger amounts only to IRAs, not to the Office of the Lost and Found

Under the proposal, the Office of the Lost and Found is not treated as a trustee eligible to receive mandatory distributions[321] that are in excess of $1,000 but not in excess of $6,000. In other words, PBGC may only accept transfers of nonforfeitable accrued benefits of $1,000 or less.

Mandatory distributions of lesser amounts for non-responsive individuals to the Office of the Lost and Found

Under the proposal, in the case of a plan that provides for mandatory distributions of amounts of $6,000 or less, the trust of such plan will not be considered a qualified trust under the Code unless the plan provides that, if a participant in the plan separates from the service covered by the plan and the participant's nonforfeitable accrued benefit is not in excess of $1,000, the plan administrator must (either separately or as part of the written notice to recipients of distributions eligible for rollover treatment) either (1) notify the participant that the participant is entitled to such benefit, or (2) attempt to pay the benefit directly to the participant.

If, after a plan administrator either notifies the participant of the entitlement to the benefit or attempts to pay the benefit directly to the participant, the participant does not:

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[318] Sec. 401(a)(31(B)(iv).

[319] Sec. 404(c)(3)(B) of ERISA.

[320] Under section 401(a)(31)(B)(ii)(I) and section 203(e)(1) of ERISA.

[321] Sec. 401(a)(31(B).

- Within 6 months of the notification either make an election to have the distribution paid directly to a specified eligible retirement plan[322] or elect to receive a distribution of the benefit directly, or
- Accept any direct payment made within 6 months of the attempted payment (in other words, does not cash the check),
- then the plan administrator must transfer the amount of such benefit to the Office of the Lost and Found.[323]

A transfer of such a distribution to the Office of the Lost and Found is treated as a transfer to an individual retirement plan, and the distribution of such amounts by the Office of the Lost and Found to a non-responsive participant who is subsequently located will be treated as a distribution from an individual retirement account.

Reporting for mandatory transfers

The proposal modifies the reporting requirements by plan administrators with respect to plans that are subject to the vesting standards of section 203 of ERISA which include section tax qualified defined benefit and defined contribution plans as follows:

- By providing that plan administrators must report[324] the name and taxpayer identification number of each participant in the plan who, during the plan year immediately preceding such plan year separated from the service covered by the plan.
- By requiring that the following information must also be included in the registration statement:
  - The name and taxpayer identifying number of each participant or former participant in the plan:
    - Who, during the current plan year or any previous plan year, was reported to IRS[325] as a separated participant with a deferred vested benefit that had not been paid as of the end of the previous plan year, and with respect to whom such benefit was fully paid during the plan year;
    - With respect to whom any amount was distributed as a mandatory distribution during the plan year; or
    - With respect to whom a deferred annuity contract was distributed during the plan year;
- In the case of a participant or former participant whose benefit was distributed as a mandatory distribution during the plan year, the name and address of the designated

[322] Sec. 402(c)(8)(B), except that a qualified trust is considered an eligible retirement plan only if it is a defined contribution plan that accepts rollovers.

[323] In accordance with section 4051(b) of ERISA.

[324] Pursuant to sec. 6057.

[325] Under sec. 6057.

trustee or issuer and the account number of the individual retirement plan to which the amount was distributed; and

- In the case of a participant or former participant to whom a deferred annuity contract was distributed during the plan year, the name and address of the issuer of such annuity contract and the contract or certificate number.

Rules relating to direct trustee-to trustee transfers

Under the proposal, additional reporting is required with respect to direct trustee-to-trustee transfers as follows:

- Notification of the Trustee: In the case of a mandatory distribution under the Code,[326] the plan administrator must notify the designated trustee of the account or issuer, or the plan administrator will be subject to a penalty equal to $100 for each such failure, up to a maximum for all such failures during any calendar year not to exceed $50,000, unless it is shown that the failure was due to reasonable cause and not to willful neglect.[327]
- The reports required to be made to the Secretary by the trustee of an IRA or the issuer of an endowment contract[328] are modified to require, in the case of an IRA account, endowment contract or IRA annuity to which a mandatory transfer[329] is made (including a transfer from the individual retirement plan to which the original transfer was made to another individual retirement plan), for the year of the transfer and any year in which the information previously reported changes that such report:

    1. Identify the transfer as a required mandatory distribution;
    2. Include the name, address, and taxpayer identifying number of the trustee or issuer of the individual retirement plan to which the amount is transferred; and
    3. Be filed with the PBGC as well as with the Secretary.

There is also a similar rule for Savings Incentive Match Plan for Employees ("SIMPLE") plans where the benefit is transferred from a SIMPLE plan to another individual retirement plan; the report required for the year of the transfer and any year in which the information previously reported is changed with the same information required.

[326] Pursuant to section 401(a)(31)(B).

[327] Sec. 6652(i) of the Code.

[328] Sec. 408(i).

[329] Under section 401(a)(31)(B.

Notification of participant upon separation of service

- The individual registration statement that needs to be provided to each separated participant[330] by the plan administrator must include a notice of availability of, and the contact information for, the Lost and Found.

Requirement of electronic filing

Under the proposal, reports required with respect to separated participants from retirement plans,[331] information required with respect to certain plans of deferred compensation,[332] and periodic reports of actuaries,[333] as well as certain reports with respect to IRAs, (including endowment contracts),[334] information returns at source,[335] and information reports relating to certain trust and annuity plans,[336] (to the extent each such return or report relates to the tax treatment of a distribution from a plan, account, contract, or annuity), the report must be filed on magnetic media, but only with respect to persons who are required to file at least 50 returns during the calendar year which includes the first day of the plan year to which such returns or reports relate.

Fiduciary Duties under the Code and ERISA

Under the proposal, not later than one year after the date of enactment, the Secretary of Labor, in consultation with the Secretary of the Treasury, shall issue a request for information (with a final rule to be issued not later than three years after such date).with respect to the following:

1. The steps a plan sponsor must take to locate a deferred vested participant in order to meet its fiduciary duty under ERISA with respect to locating that participant; and

2. The ongoing practices and procedures a plan sponsor must institute in order to meet such fiduciary duty with respect to maintaining up-to-date contact information on deferred vested participants.

Effective Date

The effective date of the proposal is generally on the date of enactment.

[330] Pursuant to section 6057(e).

[331] Sec. 6057.

[332] Sec. 6058.

[333] Sec. 6059.

[334] Pursuant to sec. 408(i).

[335] Sec. 6047.

[336] Sec. 6041.

The proposals related to the transfer of small benefits to the Office of the Lost and Found for certain non-responsive participants and the submission of information by plan administrators to the Office of the Lost and Found are effective with respect to plan years beginning after the second December 31 occurring after the date of the enactment.

The proposal related to changes to the mandatory distribution rules is applicable to vested benefits with respect to participants who separate from service connected to the plan in plan years beginning after the second December 31 occurring after the date of enactment.

The proposals related to modified reporting requirements under the Code and to filing certain reports electronically are applicable to returns and reports relating to years beginning after the second December 31 occurring after the date of enactment.

7. Expansion of Employee Plans Compliance Resolution System

Present Law

Employee Plans Compliance Resolution System[337]

General description of the Employee Plans Compliance Resolution System that this provision modifies may be found in section A.13 of this document.

The current EPCRS program does not provide corrections for individual IRAs although it does provide for certain corrections for SIMPLE plans and SEPs. SCP and VCP[338] are available to a SEP or SIMPLE plan.[339] SCP is only available to such a plan to correct insignificant operational failures,[340] and only if the SEP or SIMPLE plan is established and maintained on a document approved by the IRS.

Loans

EPCRS is available for plan loans that do not comply with one or more Code requirements (for example, the amount of the loan must not exceed the lesser of 50 percent of the participant's account balance or $50,000[341] (generally taking into account outstanding balances

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[337] See sec. 72(p)(2).

[338] Sec. 6.11 of Rev. Proc. 2019-9.

[339] Secs. 1.01 and 1.02 of Rev. Proc. 2019-19. A SEP is a plan intended to satisfy the requirements of Code section 408(k); a SIMPLE plan is a plan intended to satisfy the requirements of Code section 408(p). Secs. 5.06 and 5.07 of Rev. Proc. 2019-19.

[340] Sec. 4.01(c) of Rev. Proc. 2019-19.

[341] There are certain exceptions to these rules for loans, for example, individuals eligible to receive a coronavirus-related distribution under section 2202 of the Coronavirus Aid, Relief, and Economic Security Act, Pub. L. No. 116-136, March 27, 2020, may take a loan during a specified period of time equal to the lesser of the present value of the nonforfeitable accrued benefit of the employee under the plan or $100,000 and certain other rules apply to such loans. Special rules for loans also apply for certain individuals impacted by specified disasters, see, e.g., section 302 of Div. EE of the Consolidated Appropriations Act, 2021, Pub. L. No. 116-260, December 27, 2020.

of previous loans); the terms of the loan must provide for a repayment period of not more than five years[342] and provide for level amortization of loan payments (with payments not less frequently than quarterly); and the terms of the loan must be legally enforceable) and such errors are corrected through VCP or Audit CAP.

Unless correction is made, a deemed distribution[343] in connection with a failure relating to a loan to a participant made from a plan must be reported[344] with respect to the affected participant and any applicable income tax withholding amount that was required to be paid in connection with the failure must be paid by the employer. As part of VCP and Audit CAP, the deemed distribution may be reported with respect to the affected participant for the year of correction (instead of the year of the failure) if the plan sponsor requests such reporting relief. Where certain requirements in EPCRS are met, no reporting may be required but this relief applies only if the plan sponsor requests the relief and provides an explanation supporting the request.

Voluntary Fiduciary Correction Program

The Department of Labor also has a correction program entitled the Voluntary Fiduciary Correction Program ("VFCP")[345] under the Employee Retirement Income Security Act ("ERISA")[346] designed to encourage the voluntary correction of fiduciary violations under Title I of ERISA. VFCP also provides for the correction of certain participant loan failures including situations where participant loans exceed the Code section 72(p) limitations on amount or duration.

Description of Proposal

In general

The proposal provides that, except as otherwise provided in the Code or regulations prescribed by the Secretary (or the Secretary's delegate), any eligible inadvertent failure to comply with the rules applicable to certain tax-qualified retirement plans[347] may be self-corrected under EPCRS,[348] except to the extent that such failure was identified by the Secretary prior to any actions which demonstrate a commitment to implement a self-correction. As of the date of the enactment of this Act, EPCRS is deemed amended to provide that the correction

[342] Loans specifically for home purchases may be repaid over a longer period.

[343] Under sec. 72(p)(1).

[344] On IRS Form 1099-R.

[345] 71 Fed. Reg. 20261, April 19, 2006.

[346] Pub. L. No. 93-406, Sept. 2, 1974.

[347] Under sections 401(a), 403(a), 403(b), 408(p), or 408(k).

[348] For purposes of this proposal, references to corrections under EPCRS refers those described under Rev. Proc. 2019-19 or any successor guidance.

period[349] for an eligible inadvertent failure, except as otherwise provided under the Code or in regulations prescribed by the Secretary, is indefinite and has no last day, other than with respect to failures identified by the Secretary prior to any self-correction.

Loan errors

Under this proposal, in the case of an eligible inadvertent plan loan error:

- Such failure may be self-corrected according to the rules of EPCRS[350], including the provisions related to whether a deemed distribution must be reported on Form 1099-R, (rather than being corrected in VCP or Audit CAP); and
- the Secretary of Labor must treat such correction as meeting the requirements of VFCP if, with respect to the violation of the fiduciary standards of ERISA, there is a similar loan error eligible for correction under EPCRS and the loan error is corrected in such manner.

IRAs

The proposal also directs the Secretary to expand EPCRS to allow custodians of IRAs[351] to address eligible inadvertent failures with respect to an IRA, including, but not limited to:

1. waivers of the excise tax[352] that would otherwise apply to certain accumulations in an IRA where the amount distributed during a taxable year of a participant or beneficiary is less than the minimum required distribution for such taxable year;

2. under the self-correction component of EPCRS, waivers of the 60-day deadline for a rollover where the deadline is missed for reasons beyond the reasonable control of the account owner; and

3. rules permitting a nonspouse beneficiary to return distributions to an inherited individual IRA[353] where, due to an inadvertent error by a service provider, the beneficiary had reason to believe that the distribution could be rolled over without inclusion in income of any part of the distributed amount.

Additional safe harbors

The Secretary is directed to expand EPCRS to provide additional safe harbor means of correcting eligible inadvertent failures including safe harbor means of calculating the earnings

[349] Under sec. 9.02 of Rev. Proc. 2019-19 or any successor guidance.

[350] According to the rules of section 6.07 of Rev. Proc. 2019-19 (or any successor guidance).

[351] As defined in section 7701(a)(37).

[352] Sec. 4974.

[353] As described in section 408(d)(3)(C).

which must be restored to a plan in cases where plan assets have been depleted by reason of an eligible inadvertent failure.

Definition of eligible inadvertent failure

An eligible inadvertent failure means a failure that occurs despite the existence of practices and procedures which either (1) satisfy the standards set forth in EPCRS;[354] or (2) satisfy similar standards in the case of an individual retirement plan. However, an eligible inadvertent failure does not include any failure which is egregious, relates to the diversion or misuse of plan assets, or is directly or indirectly related to an abusive tax avoidance transaction.

This proposal does not apply to any such failure unless the correction is made in conformity with the general principles that apply to corrections of such failures under the Code, including regulations, or other guidance issued thereunder and including those principles and corrections set forth in EPCRS.

Effective Date

The proposal is effective on the date of enactment.

8. Eliminate the "first day of the month" requirement for governmental section 457(b) Plans

Present Law

Section 457(b) plans

Among the various types of tax-favored retirement plans under present law are eligible deferred compensation plans under section 457(b). A section 457(b) plan is a plan maintained by a State or local government or a tax-exempt organization that meets certain requirements. Generally, the maximum amount that can be deferred under a section 457(b) plan by an individual during any taxable year is limited to the lesser of 100 percent of the participant's includible compensation or the applicable dollar amount for the taxable year. The applicable dollar amount for 2021 is $19,500 and is indexed for future taxable years. For an employee who attains age 50 by the end of the year, the dollar limit on deferrals is increased by $6,500 (for 2021)[355] (called catch-up contributions).[356] A participant's includible compensation means the compensation of the participant from the eligible employer for the taxable year.

One of the requirements to be an eligible deferred compensation plan under section 457(b) is that a participant's compensation is deferred for any calendar month only if an

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[354] Sec. 4.04 of Rev. Proc. 2019-19 (or any successor guidance). Section 4.04 provides that the plan sponsor or plan administrator has established practices and procedures in place which are reasonably designed to promote and facilitate overall compliance in form and operation with applicable Code provisions and such practices and procedures have been in place and are routinely followed.

[355] For 2020 and 2021, this amount is $6,500.

[356] Sec. 414(v).

agreement providing for such deferral has been entered into before the beginning of such month.[357]

Description of Proposal

The proposal provides that compensation is deferred under a governmental section 457(b) plan only if an agreement providing for such deferral has been entered into before the compensation is currently available to the individual, consistent with the rule for section 401(k) and 403(b) plans. In the case of a section 457(b) plan maintained by a tax-exempt organization, the proposal provides that compensation is deferred under the plan for a calendar month only if an agreement providing for such deferral has been entered into before the beginning of such month.

Effective Date

The proposal applies to taxable years beginning after the date of enactment.

9. One-time election for qualified charitable distribution to split-interest entity; increase in qualified charitable distribution limitation

Present Law

In general

If an amount withdrawn from a traditional individual retirement arrangement ("IRA") or a Roth IRA is donated to a charitable organization, the rules relating to the tax treatment of withdrawals from IRAs apply to the amount withdrawn and the charitable contribution is subject to the normally applicable limitations on deductibility of such contributions. An exception applies in the case of a qualified charitable distribution.

Charitable contributions

In computing taxable income, an individual taxpayer who itemizes deductions generally is allowed to deduct the amount of cash and up to the fair market value of property contributed to the following entities: (1) a charity described in section 170(c)(2); (2) certain veterans' organizations, fraternal societies, and cemetery companies;[358] and (3) a Federal, State, or local governmental entity, but only if the contribution is made for exclusively public purposes.[359] The deduction also is allowed for purposes of calculating alternative minimum taxable income.

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[357] Sec. 457(b)(4).

[358] Secs. 170(c)(3)-(5).

[359] Sec. 170(c)(1).

The amount of the deduction allowable for a taxable year with respect to a charitable contribution of property may be reduced depending on the type of property contributed, the type of charitable organization to which the property is contributed, and the income of the taxpayer.[360]

A taxpayer who takes the standard deduction (*i.e.*, who does not itemize deductions) generally may not take a separate deduction for charitable contributions.[361] Under a temporary provision in effect for contributions made in any taxable year beginning in 2021, however, a taxpayer who does not itemize deductions is permitted to take a deduction for contributions of cash to a public charity (other than a donor advised fund or a supporting organization) not to exceed $300 ($600 in the case of a joint return).[362]

A payment to a charity (regardless of whether it is termed a "contribution") in exchange for which the donor receives an economic benefit is not deductible, except to the extent that the donor can demonstrate, among other things, that the payment exceeds the fair market value of the benefit received from the charity. To facilitate distinguishing charitable contributions from purchases of goods or services from charities, present law provides that no charitable contribution deduction is allowed for a separate contribution of $250 or more unless the donor obtains a contemporaneous written acknowledgement of the contribution from the charity indicating whether the charity provided any good or service (and an estimate of the value of any such good or service provided) to the taxpayer in consideration for the contribution.[363] In addition, present law requires that any charity that receives a contribution exceeding $75 made partly as a gift and partly as consideration for goods or services furnished by the charity (a "quid pro quo" contribution) is required to inform the contributor in writing of an estimate of the value of the goods or services furnished by the charity and that only the portion exceeding the value of the goods or services may be deductible as a charitable contribution.[364]

Under present law, total deductible contributions of an individual taxpayer to public charities, private operating foundations, and certain types of private nonoperating foundations generally may not exceed 50 percent of the taxpayer's contribution base, which is the taxpayer's adjusted gross income for a taxable year (disregarding any net operating loss carryback). To the extent a taxpayer has not exceeded the 50-percent limitation, (1) contributions of capital gain property to public charities generally may be deducted up to 30 percent of the taxpayer's contribution base, (2) contributions of cash to most private nonoperating foundations and certain other charitable organizations generally may be deducted up to 30 percent of the taxpayer's contribution base, and (3) contributions of capital gain property to private foundations and certain other charitable organizations generally may be deducted up to 20 percent of the

[360] Secs. 170(b) and (e).

[361] Sec. 170(a).

[362] Secs. 63(b)(4) and 170(p).

[363] Sec. 170(f)(8). For any contribution of a cash, check, or other monetary gift, no deduction is allowed unless the donor maintains as a record of such contribution a bank record or written communication from the donee charity showing the name of the donee organization, the date of the contribution, and the amount of the contribution. Sec. 170(f)(17).

[364] Sec. 6115.

taxpayer's contribution base. For taxable years beginning after December 31, 2017, and before January 1, 2026, the 50-percent limit is increased to 60 percent for contributions of cash.[365]

Contributions by individuals in excess of the applicable limits generally may be carried over and deducted over the next five taxable years, subject to the relevant percentage limitations on the deduction in each of those years.

In general, a charitable deduction is not allowed for income, estate, or gift tax purposes if the donor transfers an interest in property to a charity (*e.g.*, a remainder) while also either retaining an interest in that property (*e.g.*, an income interest) or transferring an interest in that property to a noncharity for less than full and adequate consideration.[366] Exceptions to this general rule are provided for, among other interests, remainder interests in charitable remainder trusts (discussed below), pooled income funds, and present interests in the form of a guaranteed annuity or a fixed percentage of the annual value of the property.[367] For such interests, a charitable deduction is allowed to the extent of the present value of the interest designated for a charitable organization.

Charitable remainder trusts and charitable gift annuities

Both charitable remainder trusts and charitable gift annuities are arrangements under which a taxpayer contributes assets to charity (directly or through a trust) but retains an interest. As part of these arrangements, a stream of payments is guaranteed to one or more noncharitable beneficiaries (possibly including the taxpayer) over a period of time, with the remaining interest passing to charity. The taxpayer claims a charitable deduction for the portion of the transfer attributable to the charitable interest.

Charitable remainder trusts

A charitable remainder annuity trust is a trust that is required to pay, at least annually, a fixed dollar amount of at least five percent of the initial value of the trust to a noncharity for the life of an individual or for a period of 20 years or less, with the remainder passing to charity. A charitable remainder unitrust is a trust that generally is required to pay, at least annually, a fixed percentage of at least five percent of the fair market value of the trust's assets determined at least annually to a noncharity for the life of an individual or for a period of 20 years or less, with the remainder passing to charity.[368]

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[365] Sec. 170(b)(1)(G).

[366] Secs. 170(f), 2055(e)(2), and 2522(c)(2).

[367] Sec. 170(f)(2).

[368] Sec. 664(d). Charitable remainder annuity trusts and charitable remainder unitrusts are exempt from Federal income tax for a tax year unless the trust has any unrelated business taxable income for the year (including certain debt financed income). A charitable remainder trust that loses its exemption from income tax for a taxable year is taxed as a complex trust. As such, the trust is allowed a deduction in computing taxable income for amounts required to be distributed in a taxable year, not to exceed the amount of the trust's distributable net income for the year. Taxes imposed on the trust are required to be allocated to corpus. Treas. Reg. sec. 1.664-1(d)(2).

A trust does not qualify as a charitable remainder annuity trust if the annuity for a year is greater than 50 percent of the initial fair market value of the trust's assets. A trust does not qualify as a charitable remainder unitrust if the percentage of assets that are required to be distributed at least annually is less than five percent or greater than 50 percent. A trust does not qualify as a charitable remainder annuity trust or a charitable remainder unitrust unless the value of the remainder interest in the trust is at least 10 percent of the value of the assets contributed to the trust.

Distributions from a charitable remainder annuity trust or charitable remainder unitrust are treated in the following order as: (1) ordinary income to the extent of the trust's current and previously undistributed ordinary income for the trust's year in which the distribution occurred, (2) capital gains to the extent of the trust's current capital gain and previously undistributed capital gain for the trust's year in which the distribution occurred, (3) other income (*e.g.*, tax-exempt income) to the extent of the trust's current and previously undistributed other income for the trust's year in which the distribution occurred, and (4) corpus.[369]

In general, distributions to the extent they are characterized as income are includible in the income of the beneficiary for the year that the annuity or unitrust amount is required to be distributed even though the annuity or unitrust amount is not distributed until after the close of the trust's taxable year.[370]

Charitable gift annuities

A charitable gift annuity is similar in concept to a charitable remainder annuity trust, except that, under a contract between the taxpayer and a charity, the assets are transferred to the charity (not to a separate trust) in exchange for the charity's promise to make fixed annuity payments for life to the donor or to the donor and one other person.

Charitable gift annuities are not treated as commercial-type insurance for purposes of section 501(m), under which an organization is not described in section 501(c)(3) if a substantial part of its activities consists of providing commercial-type insurance.[371]

IRA rules

Within limits, individuals may make deductible and nondeductible contributions to a traditional IRA. Amounts in a traditional IRA are includible in income when withdrawn (except to the extent the withdrawal represents a return of nondeductible contributions). Certain individuals also may make nondeductible contributions to a Roth IRA (deductible contributions cannot be made to Roth IRAs). Qualified withdrawals from a Roth IRA are excludable from gross income. Withdrawals from a Roth IRA that are not qualified withdrawals are includible in gross income to the extent attributable to earnings. Includible amounts withdrawn from a traditional IRA or a Roth IRA before attainment of age 59½ are subject to an additional 10-

[369] Sec. 664(b).

[370] Treas. Reg. sec. 1.664-1(d)(4).

[371] Sec. 501(m)(3)(E) and (5).

percent early withdrawal tax unless an exception applies. Under present law, minimum distributions are required to be made from tax-favored retirement arrangements, including IRAs. Minimum required distributions from a traditional IRA must generally begin by April 1 of the calendar year following the year in which the IRA owner attains age 72.[372]

If an individual has made nondeductible contributions to a traditional IRA, a portion of each distribution from an IRA is nontaxable until the total amount of nondeductible contributions has been received. In general, the amount of a distribution that is nontaxable is determined by multiplying the amount of the distribution by the ratio of the remaining nondeductible contributions to the account balance. In making the calculation, all traditional IRAs of an individual are treated as a single IRA, all distributions during any taxable year are treated as a single distribution, and the value of the contract, income on the contract, and investment in the contract are computed as of the close of the calendar year.

In the case of a distribution from a Roth IRA that is not a qualified distribution, in determining the portion of the distribution attributable to earnings, contributions and distributions are deemed to be distributed in the following order: (1) regular Roth IRA contributions; (2) taxable conversion contributions;[373] (3) nontaxable conversion contributions; and (4) earnings. In determining the amount of taxable distributions from a Roth IRA, all Roth IRA distributions in the same taxable year are treated as a single distribution, all regular Roth IRA contributions for a year are treated as a single contribution, and all conversion contributions during the year are treated as a single contribution.

Distributions from an IRA (other than a Roth IRA) are generally subject to withholding unless the individual elects not to have withholding apply.[374] Elections not to have withholding apply are to be made in the time and manner prescribed by the Secretary.

Qualified charitable distributions

Otherwise taxable IRA distributions from a traditional or Roth IRA are excluded from gross income to the extent they are qualified charitable distributions.[375] The exclusion may not exceed $100,000 per taxpayer per taxable year.

An individual who receives a deduction for a contribution to a traditional IRA for years ending on or after age 70½ is not eligible to exclude such amount from income as a qualified charitable distribution. Thus, the amount of qualified charitable distributions otherwise excludable from an individual's gross income for a taxable year is reduced (but not below zero) by the excess of (i) the aggregate amount of deductions allowed to the taxpayer for contributions

[372] Minimum distribution rules also apply in the case of distributions after the death of a traditional or Roth IRA owner.

[373] Conversion contributions refer to conversions of amounts in a traditional IRA to a Roth IRA.

[374] Sec. 3405.

[375] Sec. 408(d)(8). The exclusion does not apply to distributions from employer-sponsored retirement plans, including SIMPLE IRAs and simplified employee pensions ("SEPs").

to a traditional IRA for taxable years ending on or after the individual attains age 70½, over (ii) the aggregate amount of reductions for all taxable years preceding the current year.

Special rules apply in determining the amount of an IRA distribution that is otherwise taxable. The otherwise applicable rules regarding taxation of IRA distributions and the deduction of charitable contributions continue to apply to distributions from an IRA that are not qualified charitable distributions. A qualified charitable distribution is taken into account for purposes of the minimum distribution rules applicable to traditional IRAs to the same extent the distribution would have been taken into account under such rules had the distribution not been directly distributed under the qualified charitable distribution provision. An IRA does not fail to qualify as an IRA as a result of qualified charitable distributions being made from the IRA.

A qualified charitable distribution is any distribution from an IRA directly by the IRA trustee to an organization described in section 170(b)(1)(A) (generally, public charities) other than a supporting organization (as described in section 509(a)(3)) or a donor advised fund (as defined in section 4966(d)(2)). Distributions are eligible for the exclusion only if made on or after the date the IRA owner attains age 70½ and only to the extent the distribution would be includible in gross income (without regard to this provision).

The exclusion applies only if a charitable contribution deduction for the entire distribution otherwise would be allowable (under present law), determined without regard to the generally applicable percentage limitations. Thus, for example, if the deductible amount is reduced because of a benefit received in exchange, or if a deduction is not allowable because the donor did not obtain sufficient substantiation, the exclusion is not available with respect to any part of the IRA distribution.

If the IRA owner has any IRA that includes nondeductible contributions, a special rule applies in determining the portion of a distribution that is includible in gross income (but for the qualified charitable distribution provision) and thus is eligible for qualified charitable distribution treatment. Under the special rule, the distribution is treated as consisting of income first, up to the aggregate amount that would be includible in gross income (but for the qualified charitable distribution provision) if the aggregate balance of all IRAs having the same owner were distributed during the same year. In determining the amount of subsequent IRA distributions includible in income, proper adjustments are to be made to reflect the amount treated as a qualified charitable distribution under the special rule.

Distributions that are excluded from gross income by reason of the qualified charitable distribution provision are not taken into account in determining the deduction for charitable contributions under section 170.

Description of Proposal

First, the proposal indexes the annual $100,000 exclusion limit for inflation for taxable years beginning after 2021.

Second, the proposal allows a taxpayer to elect for a taxable year to treat certain distributions from an IRA to a split-interest entity as if the contributions were made directly to a qualifying charity for purposes of the exclusion from gross income for qualified charitable

distributions. Such an election may not have been in effect for a preceding taxable year; thus, the election may be made for only one taxable year during the taxpayer's lifetime. The aggregate amount of distributions of the taxpayer with respect to the election may not exceed $50,000 (indexed for inflation for taxable years beginning after 2021).

A split-interest entity means: (1) a charitable remainder annuity trust (as defined in section 664(d)(1)); (2) a charitable remainder unitrust (as defined in section 664(d)(2)); or (3) a charitable gift annuity (as defined in section 501(m)). In each case, the trust or arrangement must be funded exclusively by qualified charitable distributions. In the case of a charitable gift annuity, fixed payments of 5 percent or greater must commence not later than one year from the date of funding.

In the case of a distribution from an IRA to a charitable remainder annuity trust or charitable remainder unitrust, the distribution qualifies for the one-time election only if a charitable deduction for the entire value of the charitable remainder interest would be allowable under section 170 (determined without regard to this provision or the charitable deduction percentage limits under section 170(b)). In the case of a distribution to a charitable gift annuity, the distribution qualifies for the one-time election only if a charitable deduction in an amount equal to the amount of the distribution reduced by the value of the annuity[376] would be allowable under section 170 (determined without regard to this provision or the charitable deduction percentage limits under section 170(b)).

In addition, a distribution from an IRA to a split-interest entity qualifies for the one-time election only if: (1) no person holds an income interest in the split-interest entity other than the individual for whose benefit such account is maintained, the spouse of such individual, or both; and (2) the income interest in the split-interest entity is nonassignable.

In the case of a charitable remainder annuity trust or a charitable remainder unitrust that is funded by qualified charitable distributions, distributions are treated as ordinary income in the hands of a beneficiary to whom an annuity or unitrust payment is made. A qualified charitable distribution made to fund a charitable gift annuity is not treated as an investment in the contract for purposes of section 72(c).

[376] The annuity must be described in section 501(m)(5)(B), which provides that the annuity is described in section 514(c)(5), determined as if the amount paid in cash for the issuance of the annuity were property. Section 514(c)(5), in turn, describes when an obligation to pay an annuity is not treated as "acquisition indebtedness" for purposes of the section 514 debt-financed income rules. Under that section, the obligation to pay the annuity: (1) generally must be the sole consideration issued in exchange for property if, at the time of the exchange, the value of the annuity is less than 90 percent of the value of the property received in exchange; (2) is payable over the life of one individual or the lives of two individuals in being at such time; and (3) does not guarantee a minimum amount of payments or specify a maximum amount of payments and does not provide for any adjustment of the amount of the annuity payments by reference to the income received from the transferred property or any other property. Sec. 514(c)(5).

Effective Date

The proposal is effective for distributions made in taxable years ending after the date of enactment.

10. Distributions to firefighters

Present Law

Distributions from tax-favored retirement plans

A distribution from a qualified retirement plan,[377] a tax-sheltered annuity plan (a "section 403(b) plan"), an eligible deferred compensation plan of a State or local government employer (a "governmental section 457(b) plan"), or an IRA generally is included in income for the year distributed.[378] These plans are referred to collectively as "eligible retirement plans." In addition, unless an exception applies, a distribution from a qualified retirement plan, a section 403(b) plan, or an IRA received before age 59½ is subject to a 10-percent additional tax (referred to as the "early withdrawal tax") on the amount includible in income.[379]

Qualified public safety employees in governmental plans

An exception to the early withdrawal tax applies if a distribution is made to an employee after separation from service after attainment of age 55.[380] Under a special rule for distributions to qualified public safety employees in a governmental plan,[381] this exception applies to distributions made after separation from service after attainment of age 50 ("age 50 exception").[382] For this purpose, a qualified public safety employee means (1) any employee of a State or a political subdivision of a State who provides police protection, firefighting services, or emergency medical services for any area within the State or political subdivision's jurisdiction; or (2) any Federal law enforcement officer,[383] any Federal customs and border

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[377] Qualified under section 401(a).

[378] Secs. 401(a), 403(a), 403(b), 457(b), and 408. Under section 3405, distributions from these plans are generally subject to income tax withholding unless the recipient elects otherwise. In addition, certain distributions from a qualified retirement plan, a section 403(b) plan, or a governmental section 457(b) plan are subject to mandatory income tax withholding at a 20-percent rate unless the distribution is rolled over.

[379] Sec. 72(t). Under present law, the 10-percent early withdrawal tax does not apply to distributions from a governmental section 457(b) plan.

[380] Sec. 72(t)(2)(A)(v).

[381] As defined in section 414(d).

[382] Sec. 72(t)(10).

[383] As defined in 5 U.S.C. secs. 8331(20) or 8401(17).

protection officer,[384] any Federal firefighter,[385] any Federal employee who is an air traffic controller[386] or nuclear materials courier,[387] any member of the United States Capitol Police, any member of the Supreme Court Police, or any diplomatic security special agent of the Department of State.

Description of Proposal

The proposal amends the age 50 exception for qualified public safety employees in governmental plans so that the exception also apples to distributions from a qualified retirement plan or section 403(b) plan[388] to an employee who provides firefighting services. Thus, the proposal expands the age 50 exception to also apply to private-sector firefighters receiving distributions from a qualified retirement plan or section 403(b) plan.

Effective Date

The proposal is effective for distributions made after December 31, 2021.

11. Exclusion of certain disability-related first responder retirement payments

Present Law

Qualified retirement plans (and other tax-favored employer-sponsored retirement plans) are accorded special tax treatment and fall into two categories: defined benefit plans and defined contribution plans. A defined contribution plan is a type of qualified retirement plan whereby contributions, earnings, and losses are allocated to a separate account for each participant. Defined contribution plans may provide for nonelective contributions and matching contributions by employers and pre-tax (that is, contributions are either excluded from income or deductible) or after-tax contributions by employees.

Disability-related payments

Amounts received under worker's compensation acts as compensation for personal injuries or sickness ("disability payments") generally are excluded from the gross income of the recipients.[389] The exclusion from gross income includes compensation for personal injuries or sickness received under a statute in the nature of a worker's compensation act, and also extends such exclusion to survivors of the affected worker. However, these exclusions generally do not

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[384] As defined in 5 U.S.C. secs. 8331(31) or 8401(36).

[385] As defined in 5 U.S.C. secs. 8331(21) or 8401(14).

[386] As defined in 5 U.S.C. secs. 8331(30) or 8401(35).

[387] As defined in 5 U.S.C. secs. 8331(27) or 8401(33).

[388] The proposal applies to a distribution from a qualified retirement plan, an annuity plan described in section 403(a), or an annuity contract described in section 403(b). Sec. 402(c)(8)(B)(iii), (iv), and (vi).

[389] Sec. 104(a)(1).

apply to amounts received as a retirement pension or annuity (including retirement disability payments) to the extent that the amounts are determined by reference to the employee's age, length of service, or prior contributions. Such retirement payments, which may be distributed from a section 401(a) qualified retirement plan, a section 403(a) or (b) tax-sheltered annuity plan, or an eligible deferred compensation plan of a State or local government employer under section 457(b) ("retirement distributions"), generally are included in income for the year distributed.

Description of Proposal

The proposal adds Section 139C to the Code to address the tax treatment of certain disability-related retirement distributions to qualified first responders. An individual's gross income does not include qualified first responder retirement payments for any taxable year to the extent such payments do not exceed an annualized excludable disability amount. A qualified first responder retirement payment that is excluded from gross income is a pension or annuity that would otherwise be includible in gross income, is received in connection with the individual's qualified first responder service, and is paid from a qualified trust, annuity plan, governmental deferred compensation plan under section 457(b), or a section 403(b) plan.[390] Also, for this purpose, qualified first responder service means services performed as a law enforcement officer, firefighter, paramedic, or emergency medical technician. The proposal does not limit the exclusion from gross income to individuals who provide such services in a public capacity or to individuals who address only emergency situations.

The portion of the retirement distributions which is exempted from gross income is the "annualized excludable disability amount." This is based on the determination of the excludable amount of disability payments ("service-connected excludable disability amount") that the individual received during the 12-month period before the individual attained retirement age. A service-connected excludable disability amount means periodic payments which are not includible in the individual's gross income because they are amounts received under workmen's compensation acts as compensation for personal injuries or sickness,[391] are received in connection with the individual's qualified first responder service, and terminate when the individual attains retirement age.

The proposal also provides that for an individual who only receives service-connected excludable disability amounts for a portion of the year, the annualized excludable disability amount is determined by multiplying the service-connected excludable disability amounts by the ratio of 365 to the number of days in such period to which amounts were properly attributable.

Unlike worker's compensation payments, the exclusion under the proposal that is applicable to eligible first responders does not extend to surviving spouses or other survivors once the eligible individual is deceased.

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[390] These plans are described in clauses (iii), (iv), (v), and (vi) of section 402(c)(8)(B), respectively.

[391] Sec. 104(a)(1).

Effective Date

The proposal is effective for amounts received with respect to taxable years beginning after December 31, 2026.

12. Individual retirement plan statute of limitations for excise tax on excess contributions and certain accumulations

Present Law

Excise taxes

If an individual makes excess contributions to an individual retirement account[392] or individual retirement annuity,[393] an excise tax in the amount equal to six percent of the amount of the excess contributions to such individual's IRAs (determined as of the close of the taxable year) is imposed for each taxable year as long as the amount of the excess contributions remain in the plan.[394] However, the amount of the tax for any taxable year is limited to that it does not exceed six percent of the value of the account or annuity (determined as of the close of the taxable year).

An "excess contribution" generally means the excess (if any) of the amount of contributions made to the individual's IRAs (other than a Roth IRA) for the taxable year over the amount allowable as a deduction for such contributions.[395] For 2021, the total contributions an individual could make to his or her traditional and Roth IRAs was the lesser of $6,000 ($7,000 if the participant was age 50 or older), or the individual's taxable compensation for the year.

In addition, an excise tax on "certain accumulations" applies if the amount distributed during a taxable year of a participant or beneficiary of a qualified retirement plan[396] or any eligible deferred compensation plan,[397] is less than the minimum required distribution for such taxable year. The excise tax is equal to 50 percent of the amount by which such minimum required distribution exceeds the actual amount distributed during the taxable year and is imposed on the individual required to take the distribution. The Secretary may waive the excise tax where the taxpayer establishes (to the satisfaction of the Secretary) that the failure was due to reasonable error and reasonable steps are taken to remedy the shortfall.

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[392] Sec. 408(a).

[393] Sec. 408(b).

[394] Sec. 4973.

[395] Under section 219.

[396] As defined in section 4974(d) and including a section 401(a) qualified plan, a section 403(a) annuity plan, a section 403(b) tax-sheltered annuity, and an IRA (a section 408 individual retirement account or annuity).

[397] As defined in section 457(b).

Statute of limitations

In general, the statute of limitations with respect to a tax liability starts to run within three years after the return is filed.[398] The term "return" means the return required to be filed by the taxpayer relating to the particular type of tax (and does not include a return of any person from whom the taxpayer has received an item of income, gain, loss, deduction, or credit). With respect to the excise taxes imposed on excess contributions and certain accumulations,[399] Form 5329, Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts, is the return that needs to be filed to start the statute of limitations.[400] Unless Form 5329 is filed with the Form 1040, the statute of limitations will not begin to run.[401]

Description of Proposal

The proposal provides that for purposes of any excise tax imposed on excess contributions or on certain accumulations in connection with an IRA, the return referred to in this section shall be the income tax return filed by the person on whom the tax is imposed for the year in which the act (or failure to act) giving rise to the liability for such tax occurred. The filing of Form 5329 will generally no longer be required to start the three-year statute of limitations.

In the case of a person who is not required to file an income tax return for such year, (1) the relevant return is the income tax return that such person would have been required to file but for the fact that such person was not required to file such return, and (2) the three-year statute of limitations period is deemed to begin on the date by which the return would have been required to be filed (excluding any extension thereof).

Effective Date

The proposal is effective on the date of enactment.

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[398] Sec. 6501(a).

[399] Secs. 4973 and 4974, respectively.

[400] Internal Revenue Service, Internal Revenue Manual, Forms Reporting More Than One Item of Tax, Ch. 25.6, sec. 25.6.1.9.4.3 (May 2, 2019).

[401] *Ibid.* at 25.6.1.9.4.3(6)(b). "The period of limitations on assessment for the miscellaneous excise taxes does not begin with the filing of the Form 1040. The other miscellaneous excise taxes carry their own period of assessment based on when the Form 5329 is received for assessment." See also, *Robert K. Paschall, et ux. V. Commissioner*, 137 T.C. 8 (2011). "We hold that the filing of the Forms 1040 did not start the statute of limitations running for purposes of the section 4973 excise tax in the absence of accompanying Forms 5329."

13. Requirement to provide paper statements in certain cases

<u>Present Law</u>

<u>Pension benefit statement</u>

ERISA requires plan administrators to periodically furnish participants and beneficiaries with statements describing the individual's benefit under the plan. Such requirements depend in part on the type of plan and the individual to whom the statement is provided.[402]

In general, a benefit statement is required to indicate, on the basis of the latest available information: (1) the total benefits accrued; (2) the vested accrued benefit or the earliest date on which the accrued benefit will become vested; and (3) an explanation of any permitted disparity or floor-offset arrangement that may be applied in determining accrued benefits under the plan.[403] With respect to information on vested benefits, the Secretary of Labor is required to provide that the requirements are met if, at least annually, the plan: (1) updates the information on vested benefits that is provided in the benefit statement; or (2) provides in a separate statement information as is necessary to enable participants and beneficiaries to determine their vested benefits. The benefit statement must be written in a manner calculated to be understood by the average plan participant.

If a plan administrator fails to provide a required benefit statement to a participant or beneficiary, the participant or beneficiary may bring a civil action to recover from the plan administrator $100 a day, within the court's discretion, or other relief that the court deems proper.

<u>Requirements for defined contribution plans</u>

The administrator of a defined contribution plan is required to provide a benefit statement (1) to a participant or beneficiary who has the right to direct the investment of the assets in his or her account, at least quarterly, (2) to any other participant or other beneficiary who has his or her own account under the plan, at least annually, and (3) to other beneficiaries, upon written request, but limited to one request during any 12-month period.

A benefit statement provided with respect to a defined contribution plan must include the value of each investment to which assets in the individual's account are allocated (determined as of the plan's most recent valuation date), including the value of any assets held in the form of employer securities (without regard to whether the securities were contributed by the employer or acquired at the direction of the individual). In at least one benefit statement provided during a

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[402] ERISA sec. 105. The requirement does not apply to a one-participant retirement plan described in section 101(i)(8)(B) of ERISA.

[403] Sec. 401(l). Under the permitted disparity rules, contributions or benefits may be provided at a higher rate with respect to compensation above a specified level and at a lower rate with respect to compensation up to the specified level. In addition, benefits under a defined benefit plan may be offset by a portion of a participant's expected social security benefits. Under a floor-offset arrangement, benefits under a defined benefit pension plan are reduced by benefits under a defined contribution plan.

12-month period, the statement must include a lifetime income disclosure that sets forth the lifetime income stream equivalent of the total benefits accrued with respect to the participant or beneficiary.[404]

A quarterly benefit statement provided to a participant or beneficiary who has the right to direct investments must also include: (1) an explanation of any limitations or restrictions on any right of the individual to direct an investment; (2) an explanation, written in a manner calculated to be understood by the average plan participant, of the importance, for the long-term retirement security of participants and beneficiaries, of a well-balanced and diversified investment portfolio, including a statement of the risk that holding more than 20 percent of a portfolio in the security of one entity (such as employer securities) may not be adequately diversified; and (3) a notice directing the participant or beneficiary to the Department of Labor's website for sources of information on individual investing and diversification.

Requirements for defined benefit plans

The administrator of a defined benefit plan is required either: (1) to furnish a benefit statement at least once every three years to each participant who has a vested accrued benefit under the plan and who is employed by the employer at the time the benefit statements are furnished to participants; or (2) to furnish at least annually to each such participant notice of the availability of a benefit statement and the manner in which the participant can obtain it. The Secretary of Labor is authorized to provide that years in which no employee or former employee benefits under the plan need not be taken into account in determining the three-year period.

The administrator of a defined benefit pension plan is also required to furnish a benefit statement to a participant or beneficiary upon written request, limited to one request during any 12–month period.

In the case of a statement provided to a participant with respect to a defined benefit plan (other than at the participant's request), information may be based on reasonable estimates determined under regulations prescribed by the Secretary of Labor in consultation with the Pension Benefit Guaranty Corporation.

Delivery of pension benefit statement

The pension benefit statement may be delivered in written, electronic, or other appropriate form to the extent such form is reasonably accessible to the recipient. Department of Labor regulations provide guidance on the disclosure of the pension benefit statement, in

[404] ERISA sec. 105(a)(2)(B)(iii). The term "lifetime income stream equivalent of the total benefits accrued" means the amount of monthly payments the participant or beneficiary would receive if the total accrued benefits of such participant or beneficiary were used to provide lifetime income streams, based on assumptions specified in rules prescribed by the Secretary. Lifetime income streams for this purpose are a qualified joint and survivor annuity (as defined in ERISA section 205(d)), based on assumptions specified in rules prescribed by the Secretary of Labor, including the assumption that the participant or beneficiary has a spouse of equal age, and a single life annuity. Such lifetime income streams may have a term certain or other features to the extent permitted under rules prescribed by the Secretary of Labor.

addition to other required statements and information.[405] Under the regulations, the plan administrator generally must use measures reasonably calculated to ensure actual receipt of the material by plan participants, beneficiaries, and other specified individuals. The guidance includes two safe harbors pursuant to which an administrator may disclose information electronically and be treated as meeting this requirement.

2002 safe harbor

Under the first safe harbor, provided by regulation in 2002 ("2002 safe harbor"), a plan administrator is treated as meeting the above requirement if the administrator takes appropriate and necessary measures reasonably calculated to ensure that the system for furnishing documents (1) results in actual receipt of transmitted information, and (2) protects the confidentiality of personal information relating to the individual's accounts and benefits.[406] In addition, electronically-delivered documents must be prepared and furnished in a manner that is consistent with the style, format, and content requirements applicable to the particular document. Notice (either electronic or non-electronic) must also be provided at the time the document is furnished electronically that apprises the individual of the significance of the document when it is not otherwise reasonably evident and of the right to request and obtain a paper version. The plan must provide any paper versions that are requested.

The 2002 safe harbor applies only to individuals who generally either (1) have the ability to effectively access electronic documents at work, and access to the employer or plan sponsor's electronic information system is an integral part of the individual's duties; or (2) have consented to receiving documents electronically, have not withdrawn such consent, and were provided a statement prior to consent that contains certain required disclosures regarding such consent. Additional information must be furnished upon certain changes to hardware or software requirements.

Alternative safe harbor

Under a safe harbor that is an alternative to the 2002 safe harbor ("alternative safe harbor"), a plan administrator is deemed to meet the requirement relating to taking measures reasonably calculated to ensure actual receipt of covered documents if the plan administrator complies with certain notice, access, and other requirements described in the regulations.[407] For this purpose, covered documents are generally documents that the plan administrator is required to furnish to participants and beneficiaries under ERISA, except documents required to be furnished only upon request.

In order to satisfy the alternative safe harbor, a notice of internet availability must be furnished at the time the covered document is made available on the website. Subject to certain additional rules, a notice of internet availability may be provided annually and apply to multiple covered documents. The notice must comply with certain content requirements and must be

[405] 29 C.F.R. sec. 2520.104b-1.

[406] 29 C.F.R. sec. 2520.104b-1(c).

[407] 29 C.F.R. sec. 2520.104b-31.

written in a manner reasonably calculated to be understood by the average plan participant. Certain requirements also apply to the website where the covered documents are posted.

If an individual requests a paper version of a covered document, under the alternative safe harbor, the plan administrator must promptly furnish such paper version free of charge. Additional requirements relating to the opting out of electronic delivery apply, including that individual must be able to globally opt out of electronic delivery. In addition, the plan administrator must furnish to each individual, prior to the administrator's reliance on the safe harbor, a paper notification that covered documents will be furnished electronically. Such paper notice must include certain information, including the electronic address that will be used for the individual and any necessary instructions. Special rules apply to separated participants.

Under the alternative safe harbor, a plan administrator is also permitted to satisfy the safe harbor by using an email address to furnish covered documents to an individual, provided certain requirements are met.

The alternative safe harbor only applies to participants, beneficiaries, and other individuals entitled to receive disclosures if the individual provides an electronic address at which the individual may receive a written notice of internet availability or email of covered documents, or if the individual is assigned an electronic address for employment-related purposes.

Description of Proposal

The proposal modifies the requirement under ERISA relating to the delivery of pension benefit statements to generally require that, for a defined contribution plan, at least one such statement with respect to an individual must be provided on paper in written form for each calendar year. Similarly, for a defined benefit plan, at least one pension benefit statement with respect to an individual must be provided on paper every three years. An exception applies to (1) a plan that discloses documents using the 2002 safe harbor (subject to the modifications to this safe harbor described below); or (2) a plan that permits participants and beneficiaries to request electronic delivery of pension benefit statements, if the participant or beneficiary makes such a request and the statement is so delivered.

The proposal also directs the Secretary of Labor to make certain amendments to its regulations. With respect to the 2002 safe harbor,[408] the Secretary of Labor is directed to update the regulation no later than December 31, 2021 to provide that a plan may furnish pension benefit statements[409] electronically only if, in addition to meeting other requirements under the regulations, the plan (1) furnishes each participant and beneficiary a one-time initial paper notice, prior to the electronic delivery of any pension benefit statement, of the participant's right to request that all documents required to be disclosed under title I of ERISA be furnished on paper, and (2) furnishes each participant who is separated from service at least one paper pension

[408] 29 C.F.R. sec. 2520.104b-1(c).

[409] The pension benefit statement that is required to be provided on paper under the proposal at least once per calendar year for a defined contribution plan and at least once every three years for a defined benefit plan.

benefit statement each year, unless the participant requests electronic delivery of such statements (and such statements are so delivered).

In addition, the Secretary must update guidance governing electronic disclosure (other than the 2002 safe harbor) no later than December 31, 2021 to the extent necessary to ensure the following, with respect to a plan that discloses required documents or statements electronically:

- A participant or beneficiary under such a plan is permitted the opportunity to request that any disclosure required to be delivered on paper under applicable guidance by the Department of Labor is furnished by electronic delivery;
- Each paper statement furnished under such a plan includes (1) an explanation of how to request that all such statements, and any other document required to be disclosed, be furnished by electronic delivery; and (2) contact information for the plan sponsor, including a telephone number;
- The plan may not charge any fee to a participant or beneficiary for the delivery of paper statements;
- Each paper pension benefit statement identifies each plan document required to be disclosed and includes information about how a participant or beneficiary may access each such document;
- Each document required to be disclosed that is furnished by electronic delivery includes an explanation of how to request that all such documents be furnished on paper; and
- A plan is permitted to furnish a duplicate electronic statement in any case in which the plan furnishes a paper pension benefit statement.

Effective Date

The proposal applies to plan years beginning after December 31, 2022.

14. Separate application of top heavy rules to defined contribution plans covering excludible employees

Present Law

Top-heavy requirements apply to limit the extent to which accumulated benefits or account balances under a qualified retirement plan can be concentrated with key employees.[410] Whereas the general nondiscrimination requirements are designed to test annual contributions or benefits for highly compensated employees, compared to those of non-highly compensated employees, the top-heavy rules test the portion of the total plan contributions or benefits that have accumulated for the benefit of key employees as a group. If a plan is top-heavy, minimum contributions or benefits must be provided for non-key employees and, in some cases, faster vesting is required. In general, for a defined contribution plan, this minimum contribution is

[410] Secs. 401(a)(10)(B) and 416.

three percent of the participant's compensation; however, such contribution is limited by the percentage at which contributions are made for the key employee with the highest percentage of contributions.

For this purpose, a key employee is an officer with annual compensation greater than $185,000 (for 2021), a five-percent owner, or a one-percent owner with compensation in excess of $150,000. A defined benefit plan generally is top-heavy if the present value of cumulative accrued benefits for key employees exceeds 60 percent of the cumulative accrued benefits for all employees. A defined contribution plan is top-heavy if the aggregate of accounts for key employees exceeds 60 percent of the aggregate accounts for all employees. The nature of the top-heavy test is such that a plan of a large business with many employees is unlikely to be top-heavy. The top-heavy requirements are therefore viewed as primarily affecting plans of smaller employers in which the owners participate.

Description of Proposal

Under the proposal, if a top-heavy defined contribution plan covers employees who do not meet the minimum age and service requirements under the Code,[411] and the plan satisfies the top-heavy minimum contribution requirement separately with respect to such employees, such employees may be excluded from consideration in determining whether any plan of the employer satisfies the top-heavy minimum contribution requirement.

Effective Date

The proposal applies to plan years beginning after date of enactment.

15. Repayment of qualified birth or adoption distributions limited to three years

Present Law

Distributions from tax-favored retirement plans

A distribution from a qualified retirement plan, a tax-sheltered annuity plan (a "section 403(b) plan"), an eligible deferred compensation plan of a State or local government employer (a "governmental section 457(b) plan"), or an IRA generally is included in income for the year distributed.[412] These plans are referred to collectively as "eligible retirement plans." In addition, unless an exception applies, a distribution from a qualified retirement plan, a

[411] Qualified plans generally cannot delay an employee's participation in the plan beyond the later of completion of one year of service (*i.e.*, a 12-month period with at least 1,000 hours of service) or attainment of age 21. Sec. 410(a)(1).

[412] Secs. 401(a), 403(a), 403(b), 457(b), and 408. Under section 3405, distributions from these plans are generally subject to income tax withholding unless the recipient elects otherwise. In addition, certain distributions from a qualified retirement plan, a section 403(b) plan, or a governmental section 457(b) plan are subject to mandatory income tax withholding at a 20-percent rate unless the distribution is rolled over.

section 403(b) plan, or an IRA received before age 59½ is subject to a 10-percent additional tax (referred to as the "early withdrawal tax") on the amount includible in income.[413]

In general, a distribution from an eligible retirement plan may be rolled over to another eligible retirement plan within 60 days, in which case the amount rolled over generally is not includible in income. The IRS has the authority to waive the 60-day requirement if failure to waive the requirement would be against equity or good conscience, including cases of casualty, disaster, or other events beyond the reasonable control of the individual.

The terms of a qualified retirement plan, section 403(b) plan, or governmental section 457(b) plan generally determine when distributions are permitted. However, in some cases, restrictions may apply to distributions before an employee's termination of employment, referred to as "in-service" distributions. Despite such restrictions, an in-service distribution may be permitted in the case of financial hardship or an unforeseeable emergency.

Distributions in the event of a qualified birth or adoption

An exception to the 10-percent early withdrawal tax applies in the case of a qualified birth or adoption distribution from an applicable eligible retirement plan (as defined). In addition, qualified birth or adoption distributions may be recontributed to an individual's applicable eligible retirement plans, subject to certain requirements.

A qualified birth or adoption distribution is a permissible distribution from an applicable eligible retirement plan which, for this purpose, encompasses eligible retirement plans other than defined benefit plans, including qualified retirement plans, section 403(b) plans, governmental section 457(b) plans, and IRAs.[414]

A qualified birth or adoption distribution is a distribution from an applicable eligible retirement plan to an individual if made during the one-year period beginning on the date on which a child of the individual is born or on which the legal adoption by the individual of an eligible adoptee is finalized. An eligible adoptee means any individual (other than a child of the taxpayer's spouse) who has not attained age 18 or is physically or mentally incapable of self-support. The name, age, and taxpayer identification number of the child or eligible adoptee to which any qualified birth or adoption distribution relates must be provided on the tax return of the individual taxpayer for the taxable year.

The maximum aggregate amount which may be treated as qualified birth or adoption distributions by any individual with respect to a birth or adoption is $5,000. The maximum aggregate amount applies on an individual basis. Therefore, each spouse separately may receive a maximum aggregate amount of $5,000 of qualified birth or adoption distributions (with respect

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[413] Sec. 72(t). Under present law, the 10-percent early withdrawal tax does not apply to distributions from a governmental section 457(b) plan.

[414] A qualified birth or adoption distribution is subject to income tax withholding unless the recipient elects otherwise. Mandatory 20-percent withholding does not apply.

to a birth or adoption) from applicable eligible retirement plans in which each spouse participates or holds accounts.

An employer plan is not treated as violating any Code requirement merely because it treats a distribution (that would otherwise be a qualified birth or adoption distribution) to an individual as a qualified birth or adoption distribution, provided that the aggregate amount of such distributions to that individual from plans maintained by the employer and members of the employer's controlled group[415] does not exceed $5,000. Under such circumstances an employer plan is not treated as violating any Code requirement merely because an individual might receive total distributions in excess of $5,000 as a result of distributions from plans of other employers or IRAs.

Recontributions to applicable eligible retirement plans

Generally, any portion of a qualified birth or adoption distribution may, at any time after the date on which the distribution was received, be recontributed to an applicable eligible retirement plan to which a rollover can be made. Such a recontribution is treated as a rollover and thus is not includible in income. If an employer adds the ability for plan participants to receive qualified birth or adoption distributions from a plan, the plan must permit an employee who has received qualified birth or adoption distributions from that plan to recontribute only up to the amount that was distributed from that plan to that employee, provided the employee otherwise is eligible to make contributions (other than recontributions of qualified birth or adoption distributions) to that plan. Any portion of a qualified birth or adoption distribution from an individual's applicable eligible retirement plans (whether employer plans or IRAs) may be recontributed to an IRA held by such an individual which is an applicable eligible retirement plan to which a rollover can be made.

Description of Proposal

Under the proposal, a recontribution of any portion of a qualified birth or adoption distribution, may, at any time during the three-year period beginning on the day after the date on which the distribution was received, be recontributed to an applicable eligible retirement plan to which a rollover can be made.

Effective Date

The proposal provides that the amendment made to this section will take effect as if included in the enactment of section 113 of the Setting Every Community Up for Retirement Enhancement Act of 2019.[416]

[415] The term "controlled group" means any group treated as a single employer under subsection (b), (c), (m), or (o) of section 414.

[416] Sec. 113 of Div. O of the Further Consolidated Appropriations Act, 2020, Pub. L. No. 116-94, December 20, 2019.

16. Employer may rely on employee certifying that deemed hardship distribution conditions are met

Present Law

Section 401(k) plan and section 403(b) plan hardship distributions

A qualified defined contribution plan may include a qualified cash or deferred arrangement, under which employees may elect to have contributions made to the plan (referred to as "elective deferrals") rather than receive the same amount as current compensation (referred to as a "section 401(k) plan"). A section 403(b) plan may also include an elective deferral arrangement. Amounts attributable to elective deferrals under a section 401(k) plan or a section 403(b) plan generally cannot be distributed before the occurrence of one or more specified events, including financial hardship of the employee.[417]

A hardship distribution from a section 401(k) plan may include, in addition to the employee's elective deferrals, qualified matching contributions, qualified nonelective contributions, and earnings on any of these amounts.[418] A hardship distribution from a section 403(b) plan may include elective deferrals, but not earnings on those deferrals.[419] Qualified matching contributions and qualified nonelective contributions to a section 403(b) plan that are in a custodial account are not eligible to be distributed on account of hardship.[420] A distribution under a section 401(k) plan is not treated as failing to be on account of hardship solely because the employee does not take any available plan loan. Distributions on account of hardship may be subject to an additional 10-percent early withdrawal tax.[421]

Applicable Treasury regulations provide that a distribution is made on account of hardship only if the distribution is made on account of an immediate and heavy financial need of the employee and is necessary to satisfy the financial need.[422] Generally, the determination of whether an employee has an immediate and heavy financial need is based on the relevant facts and circumstances. However, a distribution is deemed to be made on account of an immediate and heavy financial need if it is for: (1) generally, deductible expenses for medical care;[423] (2)

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[417] Secs. 401(k)(2)(B)(i)(IV) and 403(b)(7)(A)(i)(V) and (11)(B). Other types of contributions may also be subject to this restriction.

[418] Sec. 401(k)(14). Qualified matching contributions (as defined in section 401(k)(3)(D)(ii)(I)) and qualified nonelective contributions (as defined in section 401(m)(4)(C)) may be used to enable the plan to satisfy certain nondiscrimination tests, to prevent discrimination in favor of highly compensated employees.

[419] Sec. 403(b)(11).

[420] Treas. Reg. sec. 1.403(b)-6(c).

[421] Sec. 72(t).

[422] Treas. Reg. secs. 1.401(k)-1(d)(3); 1.403(b)-6(d)(2).

[423] Expenses for (or necessary to obtain) medical care that would be deductible under section 213(d), determined without regard to the limitations in section 213(a) (relating to the applicable percentage of adjusted gross

costs directly related to the purchase of a principal residence for the employee (excluding mortgage payments); (3) payment of tuition, related educational fees, and room and board expenses, for up to the next 12 months of post-secondary education for the employee, the employee's spouse, child, or dependent,[424] or for a primary beneficiary under the plan; (4) payments necessary to prevent the eviction of the employee from the employee's principal residence or foreclosure on the mortgage on that residence; (5) payments for burial or funeral expenses for the employee's deceased parent, spouse, child, or dependent, or for a deceased primary beneficiary under the plan; (6) expenses for the repair of damage to the employee's principal residence that would qualify for the casualty deduction;[425] or (7) expenses and losses (including loss of income) incurred by the employee on account of a federally-declared disaster.[426]

A distribution is treated as necessary to satisfy the financial need under the Treasury regulations only to the extent that the amount of the distribution does not exceed the amount required. In addition, in order to be treated as necessary to satisfy the financial need, the following requirements must be met: (1) the employee has obtained all other currently available distributions under all plans of the employer; (2) the employee has provided to the plan administrator a written representation that he or she has insufficient cash or other liquid assets reasonably available to satisfy the need; and (3) the plan administrator does not have actual knowledge contrary to the representation.[427]

Governmental section 457(b) plan distributions upon unforeseeable emergency

An eligible deferred compensation plan of a governmental employer (referred to as a "governmental section 457(b) plan") is generally similar to a qualified cash or deferred arrangement under a section 401(k) plan in that it consists of elective deferrals made at the election of an employee. Such deferrals generally may not be distributed from the plan before the occurrence of one or more specified events, including when the participant is faced with an unforeseeable emergency.[428]

Under Treasury regulations, the unforeseeable emergency must be defined in the plan as a severe financial hardship of the participant or beneficiary resulting from an illness or accident

income and the recipients of the medical care) provided that, if the recipient of the medical care is not listed in section 213(a), the recipient is a primary beneficiary under the plan.

[424] As defined in section 152 without regard to section 152(b)(1), (b)(2), and (d)(1)(B).

[425] Under section 165 (determined without regard to section 165(h)(5) and whether the loss exceeds 10 percent of adjusted gross income).

[426] A disaster declared by the Federal Emergency Management Agency ("FEMA") under the Robert T. Stafford Disaster Relief and Emergency Assistance Act, Pub. L. No. 100–707, provided that the employee's principal residence or principal place of employment at the time of the disaster was located in an area designated by FEMA for individual assistance with respect to the disaster.

[427] Treas. Reg. sec. 1.401(k)-1(d)(3)(iii).

[428] Sec. 457(d)(1)(A)(iii).

of the participant or beneficiary, or the participant's or beneficiary's spouse or dependent;[429] loss of the participant's or beneficiary's property due to casualty;[430] or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the participant or the beneficiary.[431] The Treasury regulations provide the following as examples of unforeseeable emergencies: (1) the imminent foreclosure of or eviction from the participant's or beneficiary's primary residence; (2) the need to pay for medical expenses, including non-refundable deductibles, as well as for the cost of prescription drug medication; and (3) the need to pay for the funeral expenses of a spouse or a dependent of a participant or beneficiary. The purchase of a home and the payment of college tuition are not unforeseeable emergencies, unless such expenses otherwise qualify.

In general, under the regulations, whether a participant or beneficiary is faced with an unforeseeable emergency permitting a distribution is to be determined based on the relevant facts and circumstances of each case, but, in any case, a distribution on account of unforeseeable emergency may not be made to the extent that such emergency is or may be relieved through reimbursement or compensation from insurance or otherwise, by liquidation of the participant's assets, to the extent the liquidation of such assets would not itself cause severe financial hardship, or by cessation of deferrals under the plan. Distributions on account of an unforeseeable emergency must be limited to the amount reasonably necessary to satisfy the emergency need.

Description of Proposal

Under the proposal, in determining whether a distribution is due to an employee hardship, the plan administrator of a section 401(k) plan or a section 403(b) plan may rely on the employee's certification that the distribution is on account of a financial need of a type that is deemed in Treasury regulations to be an immediate and heavy financial need. Thus, if the employee certifies that the financial need for the hardship distribution is one of the types of deemed immediate and heavy financial needs that are described in the Treasury regulations,[432] such as funeral expenses for the employee's deceased parent, the distribution is treated as being made on account of an immediate and heavy financial need. In addition, under the proposal, the plan administrator may rely on the employee's certification that the distribution is not in excess of the amount required to satisfy the financial need.

Similarly, with respect to a governmental section 457(b) plan, in determining whether a participant's distribution is made when the participant is faced with an unforeseeable emergency, a plan administrator may rely on the participant's certification that the distribution is on account of an unforeseeable emergency of a type that is specifically described in Treasury regulations as

[429] As defined in section 152, and, for taxable years beginning on or after January 1, 2005, without regard to section 152(b)(1), (b)(2), and (d)(1)(B).

[430] This includes the need to rebuild a home following damage to a home not otherwise covered by homeowner's insurance, such as damage that is the result of a natural disaster.

[431] Treas. Reg. sec. 1.457-6(c)(2).

[432] Treas. Reg. sec. 1.401(k)-1(d)(3)(ii)(B), or any successor regulation.

an unforeseeable emergency[433] and that the distribution does not exceed the amount reasonably necessary to satisfy the emergency need.

Effective Date

The proposal is effective for plan years beginning after December 31, 2021.

17. Penalty-free withdrawals from retirement plans for individuals in case of domestic abuse

Present Law

Distributions from tax-favored retirement plans

A distribution from a tax-qualified plan described in section 401(a) (a "qualified retirement plan"), a tax-sheltered annuity plan (a "section 403(b) plan"), an eligible deferred compensation plan of a State or local government employer (a "governmental section 457(b) plan"), or an individual retirement arrangement (an "IRA") generally is included in income for the year distributed.[434] These plans are referred to collectively as "eligible retirement plans."[435] In addition, unless an exception applies, a distribution from a qualified retirement plan, a section 403(b) plan, or an IRA received before age 59½ is subject to a 10-percent additional tax (referred to as the "early withdrawal tax") on the amount includible in income.[436]

In general, a distribution from an eligible retirement plan may be rolled over to another eligible retirement plan within 60 days, in which case the amount rolled over generally is not includible in income. The IRS has the authority to waive the 60-day requirement if failure to waive the requirement would be against equity or good conscience, including cases of casualty, disaster, or other events beyond the reasonable control of the individual.[437]

The terms of a qualified retirement plan, section 403(b) plan, or governmental section 457(b) plan generally determine when distributions are permitted. However, for many types of plans, restrictions apply to distributions before an employee's termination of employment, referred to as "in-service" distributions or withdrawals. Despite such restrictions, an in-service distribution from a qualified retirement plan that includes a qualified cash-or-

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[433] Treas. Reg. sec. 1.457-6(c)(2)(i), or any successor regulation.

[434] Secs. 401(a), 403(a), 403(b), 457(b), and 408. Under section 3405, distributions from these plans are generally subject to income tax withholding unless the recipient elects otherwise. In addition, certain distributions from a qualified retirement plan, a section 403(b) plan, or a governmental section 457(b) plan are subject to mandatory income tax withholding at a 20-percent rate unless the distribution is rolled over.

[435] Sec. 402(c)(8)(B). Eligible retirement plans also include annuity plans described in section 403(a).

[436] Sec. 72(t). The 10-percent early withdrawal tax does not apply to distributions from a governmental section 457(b) plan.

[437] Rev. Proc. 2016-47, 2016-37 I.R.B. 346, provides for a self-certification procedure (subject to verification on audit) that may be used by a taxpayer claiming eligibility for a waiver of the 60-day requirement with respect to a rollover into a plan or IRA in certain specified circumstances.

deferred arrangement (a "section 401(k) plan") or a section 403(b) plan may be permitted in the case of financial hardship. Similarly, a governmental section 457(b) plan may permit distributions in the case of an unforeseeable emergency. Under a qualified retirement plan that is a pension plan (*i.e.*, defined benefit pension plan or money purchase pension plan), distributions generally may be made only in the event of retirement, death, disability, or other separation from service, although in-service distributions may be permitted after age 59½.[438]

Description of Proposal

Under the proposal, an exception to the 10-percent early withdrawal tax applies in the case of an eligible distribution to a domestic abuse victim. In addition, such eligible distributions may be recontributed to applicable eligible retirement plans, subject to certain requirements.

Eligible distributions to a domestic abuse victim

The proposal provides that an eligible distribution to a domestic abuse victim is a distribution from an applicable eligible retirement plan to an individual if made during the one-year period beginning on a date on which the individual is a victim of domestic abuse by a spouse or domestic partner. Domestic abuse is defined under the proposal as physical, psychological, sexual, emotional, or economic abuse, including efforts to control, isolate, humiliate, or intimidate the victim, or to undermine the victim's ability to reason independently, including by means of abuse of the victim's child or another family member living in the household. In making such a distribution, a plan administrator may rely on the participant's certification that the distribution is an eligible distribution to a domestic abuse victim.

An applicable eligible retirement plan, for this purpose, encompasses eligible retirement plans other than defined benefit plans, including qualified retirement plans, section 403(b) plans, governmental section 457(b) plans, and IRAs.[439] The maximum aggregate amount which may be treated as an eligible distribution to a domestic abuse victim by an individual is the lesser of $10,000 or 50 percent of the value of the employee's account under the plan.[440] An eligible distribution to a domestic abuse victim is treated as meeting requirements relating to the timing of distributions under a section 401(k) plan, section 403(b) plan, or governmental section 457(b) plan.

Under the proposal, an employer plan is not treated as violating any Code requirement merely because it treats a distribution to an individual (that would otherwise be an eligible distribution to a domestic abuse victim) as an eligible distribution to a domestic abuse victim, provided that the aggregate amount of such distributions to that individual from plans maintained

[438] Sec. 401(a)(36); Treas. Reg. secs. 1.401-1(b)(1)(i) and 1.401(a)-1(b)(1)(i). Section 401(k) plans, section 403(b) plans, and governmental section 457(b) plans also may permit in-service distributions after age 59 ½.

[439] An eligible distribution to a domestic abuse victim is subject to income tax withholding unless the recipient elects otherwise. Mandatory 20-percent withholding does not apply.

[440] 50 percent of the present value of the nonforfeitable accrued benefit of the employee under the plan.

by the employer and members of the employer's controlled group[441] does not exceed the lesser of $10,000 or 50 percent of the value of the employee's accounts under the plans of the employer's controlled group. Thus, under such circumstances an employer plan is not treated as violating any Code requirement merely because an individual might receive, for example, total distributions in excess of $10,000 as a result of distributions from plans of other employers or IRAs.

Recontributions to applicable eligible retirement plans

The proposal provides that any portion of an eligible distribution to a domestic abuse victim may generally, at any time after the date on which the distribution was received, be recontributed to an applicable eligible retirement plan to which a rollover can be made. Such a recontribution is treated as a rollover and thus is not includible in income. If an employer adds the ability for plan participants to receive eligible distributions to domestic abuse victims from a plan, the plan must permit an employee who has received such an eligible distribution from that plan to recontribute only up to the amount that was distributed from that plan to that employee, provided the employee otherwise is eligible to make contributions (other than recontributions of eligible distributions to domestic abuse victims) to that plan. Any portion of an eligible distribution to a domestic abuse victim from an individual's applicable eligible retirement plans (whether employer plans or IRAs) may be recontributed to an IRA held by such an individual which is an applicable eligible retirement plan to which a rollover can be made.

Effective Date

The proposal is effective for distributions made after the date of enactment.

18. Reform of family attribution rule

Present Law

Nondiscrimination requirements

A qualified retirement plan is prohibited from discriminating in favor of highly compensated employees, referred to as the nondiscrimination requirements. These requirements are intended to ensure that a qualified retirement plan provides meaningful benefits to an employer's rank-and-file employees as well as highly compensated employees so that qualified retirement plans achieve the goal of retirement security for both lower-paid and higher-paid employees. The nondiscrimination requirements consist of a minimum coverage requirement and general nondiscrimination requirements.[442] For purposes of these requirements, an employee generally is treated as highly compensated if the employee (1) was a five-percent

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[441] The term "controlled group" means any group treated as a single employer under subsection (b), (c), (m), or (o) of section 414.

[442] Sections 401(a)(3) and 410(b) address the minimum coverage requirement; section 401(a)(4) describes the general nondiscrimination requirements, with related rules in section 401(a)(5). Detailed regulations implement the statutory requirements. Governmental plans are generally exempt from these requirements.

owner of the employer at any time during the year or the preceding year, or (2) had compensation for the preceding year in excess of $130,000 (for 2021).[443]

The minimum coverage and general nondiscrimination requirements apply annually on the basis of the plan year. In applying these requirements, as discussed below, employees of all members of a controlled group or affiliated service group are treated as employed by a single employer. Employees who have not satisfied minimum age and service conditions under the plan, certain nonresident aliens, and employees covered by a collective bargaining agreement are generally disregarded.[444] However, a plan that covers employees with less than a year of service or who are under age 21 must generally include those employees in any nondiscrimination test for the year but can test the plan for nondiscrimination in two parts: (1) by separately testing the portion of the plan covering employees who have not completed a year of service or are under age 21 and treating all of the employer's employees with less than a year of service or under age 21 as the only employees of the employer; and (2) then testing the rest of the plan taking into account the rest of the employees of the employer and excluding those employees. If a plan does not satisfy the nondiscrimination requirements on its own, it may in some circumstances be aggregated with another plan, and the two plans tested together as a single plan.

Aggregation rules for groups under common control

In general, in applying the requirements for tax-favored treatment for retirement plans, employees of employers (including corporations and other entities) that are members of a group under common control are treated as employed by a single employer (referred to as aggregation rules).[445] For example, in applying the nondiscrimination requirements, the employees of all the members of a group, and the benefits provided under plans maintained by any member of the group, are generally taken into account. In the case of taxable entities, common control is generally based on the percentage of equity ownership with a general threshold of 80 percent ownership. Other tests apply for entities that do not involve ownership.

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[443] Sec. 414(q). At the election of the employer, employees who are highly compensated based on compensation may be limited to the top 20 percent highest paid employees. A non-highly compensated employee is an employee other than a highly compensated employee.

[444] A plan or portion of a plan covering collectively bargained employees is generally deemed to satisfy the nondiscrimination requirements.

[445] Sec. 414(c) and the regulations thereunder provide for aggregation of groups under common control. Section 414(b), (m) and (o) also provide aggregation rules for a controlled group of corporations and affiliated service groups. Under section 414(t), the aggregation rules apply also for purposes of various benefits other than retirement benefits. In addition, other provisions incorporate the aggregation rules by reference, such as section 4980H, requiring certain employers to offer health coverage to full-time employees.

Family attribution rules

The family attribution rules address the scenarios in which a person, such as a family member, is treated as having an ownership interest in a business.[446] For example, a spouse is generally attributed their spouse's ownership unless certain criteria are satisfied.[447]

One common exception to spousal attribution is for individuals who are legally separated under a divorce decree.[448] Other exceptions include spouses who do not directly own any stock in the business during the taxpayer year, a spouse who is neither an employee or director nor participates in the management of the business at any time during the year, where no more than 50 percent of the business' gross income derives from passive investments, and where the stock is transferable (i.e., is not subject to restrictions) that are in favor of the individual or his or her minor children (e.g., the business owner cannot be required to offer a right of first refusal to his or her spouse or their children before selling the business to a third party).

A parent is generally attributed the ownership of a minor child under the age of 21 and is attributed the ownership of an adult child, age 21 or older, if the parent owns more than 50 percent of the business. A minor child is attributed the ownership of a parent while an adult child is attributed the ownership of a parent only if the adult child owns more than 50 percent of the business. There is no exception to the application of the family attribution rules for a minor child of individuals who are separated or divorced. For example, ownership of a business may be attributed to a divorced spouse through his or her minor child to the extent the exceptions for marital attribution do not apply.

The application of these rules is impacted by the laws on familial property ownership in community property state. In such a state, spouses may be deemed to own half of the property acquired during a marriage, except under limited circumstances. Accordingly, spouses in community property states may fail to satisfy the criteria that a spouse does not directly own any stock in the business during the taxpayer year.

Description of Proposal

The proposal adds special rules to address family attribution and to disregard community property laws for purposes of determining ownership of a business.[449] For purposes of applying the attribution rules,[450] community property laws are disregarded for purposes of determining ownership. In addition, the stock of an individual not attributed under section 1563(e)(5) to the individual's spouse shall not be attributed to such spouse by reason of section 1563(e)(6)(A),

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[446] Family attribution can address interests owned between spouses or among parents and children or grandparents and grandchildren.

[447] Sec. 1563(e)(5). For example, if a husband and wife each owned 25 percent of a business, generally both spouses would be treated as owning 50 percent of that business.

[448] Sec. 1563(e).

[449] Sec. 414(m)(6)(B).

[450] Under sec. 1563.

which addresses minor children. Except as provided by the Secretary, stock in different corporations that is attributed to a child under section 1563(e)(6)(A) from each parent, but that is not attributed to such parents as spouses under section 1563(e)(5), shall not by itself result in such corporations being members of the same controlled group. If these modifications under the proposal causes two or more entities to be a controlled group, or an affiliated service group, or to no longer be in a controlled group or affiliated service group, such change shall be treated as a transaction to which the special minimum coverage rule for certain dispositions or acquisitions applies.[451]

Effective Date

The proposal applies to plan years beginning on or after the date of enactment.

19. Amendments to increase benefit accruals under plan for previous plan year allowed until employer tax return due date

Present Law

Present law provides a remedial amendment period during which, under certain circumstances, a retirement plan may be amended retroactively in order to comply with the tax qualification requirements.[452] In general, plan amendments to reflect changes in the law generally must be made by the time prescribed by law for filing the income tax return of the employer for the employer's taxable year in which the change in law occurs (including extensions). Discretionary amendments must be adopted by the end of the plan year.[453] The Secretary may extend the time by which plan amendments need to be made.

Section 201 of the Setting Every Community Up for Retirement Enhancement (the "SECURE" Act)[454] provides that if an employer adopts a qualified retirement plan after the close of a taxable year but before the time prescribed by law for filing the return of tax of the employer for the taxable year (including extensions thereof), the employer may elect to treat the plan as having been adopted as of the last day of the taxable year.

Description of Proposal

Under the proposal, if an employer amends a stock bonus, pension, profit-sharing, or annuity plan to increase benefits accrued under the plan effective for the preceding plan year (other than increasing the amount of matching contributions),[455] the amendment would not otherwise cause the plan to fail to meet any of qualification requirements, and the amendment is

[451] Sec. 410(b)(6)(C).

[452] Sec. 401(b).

[453] Rev. Proc. 2016-37, .2016-29 I.R.B. 136, June 29, 2016.

[454] Sec. 201 of Div. O. of the Further Consolidated Appropriations Act, 2020, Pub. L. No. 116-94, December 20, 2019.

[455] As defined in subsection 401(m)(4)(A).

adopted before the time prescribed by law for filing the return of the employer for a taxable year (including extensions) during which the amendment is effective, the employer may elect to treat such amendment as having been adopted as of the last day of the plan year in which the amendment is effective.

Effective Date

The proposal applies to amendments made in plan years beginning after December 31, 2022.

20. Retroactive first year elective deferrals for sole proprietors

Present Law

Present law provides a remedial amendment period during which, under certain circumstances, a retirement plan may be amended retroactively in order to comply with the tax qualification requirements.[456] In general, plan amendments to reflect changes in the law generally must be made by the time prescribed by law for filing the income tax return of the employer for the employer's taxable year in which the change in law occurs (including extensions). The Secretary of the Treasury may extend the time by which plan amendments need to be made.

Section 201 of the Setting Every Community Up for Retirement Enhancement (the "SECURE" Act)[457] provides that if an employer adopts a qualified retirement plan after the close of a taxable year but before the time prescribed by law for filing the return of tax of the employer for the taxable year (including extensions thereof), the employer may elect to treat the plan as having been adopted as of the last day of the taxable year. That provision permits employers to establish and fund a qualified plan by the due date for filing the employer's return for the preceding plan year. However, that provision does not override rules requiring certain plan provisions to be in effect during a plan year, such as the provision for elective deferrals under a qualified cash or deferral arrangement (generally referred to as a "401(k) plan").[458]

Under section 201 of the SECURE Act, a section 401(k) plan of a sole proprietor can be funded with employer contributions as of the due date for the business's return, but the elective deferrals must be made as of December 31 of the prior year. However, an individual is deemed to have made a contribution to an individual retirement plan for a taxable year if it is contributed after the taxable year has ended but is made "on account of" that year and before the due date for

[456] Sec. 401(b).

[457] Sec. 201 of Div. O. of the Further Consolidated Appropriations Act, 2020, Pub. L. No. 116-94, December 20, 2019.

[458] Treas. Reg. sec. 1.401(k)-1(e)(2)(ii).

filing the IRA owner's tax return, (generally) for that year without extensions, (generally, April 15).[459]

Description of Proposal

The proposal provides that in the case of an individual who owns the entire interest in an unincorporated trade or business, and who is the only employee of such trade or business, any elective deferral[460] under a section 401(k) plan to which the preceding sentence applies which is made by such individual before the time for filing the return of such individual for the taxable year (determined without regard to any extensions) shall be treated as having been made before the end of the plan's first plan year. This extension of time would only apply to the first plan year in which the section 401(k) plan is established.

Effective Date

The proposal is effective for plan years beginning after the date of enactment.

21. Limiting cessation of IRA treatment to portion of account involved in a prohibited transaction

Present Law

Background on prohibited transactions may be found in section A.12. of this document.

Disqualification of IRA in certain prohibited transactions

If an individual for whose benefit an IRA is established (or such individual's beneficiary) engages in a prohibited transaction with respect to the IRA, the IRA loses its tax-favored status and ceases to be an IRA as of the first day of the taxable year in which the prohibited transaction occurs.[461] As a result, the IRA is treated as distributing to the individual on the first day of that taxable year the fair market value of all of the assets in the account. If the fair market value of the IRA assets exceeds the basis in the account, the individual has taxable gain that is includible in gross income. If the individual is under age 59½, the individual may also be subject to the 10-percent tax on early distributions.[462] The individual and the individual's beneficiaries are exempt, however, from the excise tax that otherwise applies to prohibited transactions.[463]

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[459] Sec. 219(f)(3). For taxpayers affected by a federally declared disaster, the IRS has the authority to postpone various tax deadlines for a period of up to one year. Sec. 7508A and ERISA sec. 518

[460] As defined in section 402(g)(3).

[461] Sec. 408(e)(2). "Prohibited transaction" means a transaction prohibited by section 4975.

[462] Sec. 72(t).

[463] Sec. 4975(c)(3).

Description of Proposal

The proposal modifies the disqualification rule that applies when an IRA owner or beneficiary engages in a prohibited transaction so that only the portion of the IRA that is used in the prohibited transaction is treated as distributed to the individual. Thus, under the proposal, if an IRA owner or beneficiary engages in a prohibited transaction with respect to the IRA, the portion of the account used in the transaction is treated as distributed to the individual as of the first day of the taxable year in which the transaction occurred (using fair market value of the portion on that first day).

Effective Date

The proposal applies to taxable years beginning after date of enactment.

D. Technical Amendments

1. Amendments relating to Setting Every Community Up for Retirement Enhancement Act of 2019

Present Law

Increase in age for required beginning date for mandatory distributions

The Setting Every Community Up for Retirement Enhancement Act of 2019 ("SECURE Act") changed the age on which the required beginning date for required minimum distributions was based, from age 70½ to age 72.[464] Background on these rules may be found in section A.5. of this document.

Difficulty of care payments

The SECURE Act also modified certain retirement contribution limits as they apply to "difficulty of care" payments.[465] A difficulty of care payment is compensation for providing the additional care needed for certain qualified foster individuals.[466] Such payments are excludable from gross income. Generally, the amount that may be contributed to an IRA is limited by the compensation that is includible in an individual's gross income for the taxable year.[467] However, the SECURE Act modified the limit on nondeductible contributions to a traditional IRA to generally allow an individual to contribute a difficulty of care payment.[468] Under the SECURE Act, if the deductible amount of IRA contributions in effect for a taxable year (which is tied to the amount of nondeductible contributions that may be made) exceeds the individual's compensation that is includible in gross income, the individual may elect to increase the limit on nondeductible contributions by the amount of the difficulty of care payment (or, if less, the excess of the deductible amount of IRA contributions over the individual's compensation for the year).

Excise tax on excess IRA contributions

To the extent that contributions to an IRA exceed the contribution limits, the individual is subject to an excise tax equal to six percent of the excess amount.[469] This excise tax generally applies each year until the excess amount is distributed.

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[464] Pub. L. No. 116-94, Division O, sec. 114.

[465] Pub. L. No. 116-94, Division O, sec. 116.

[466] Sec. 131(c).

[467] Secs. 408(o)(2) and 408A(c)(2).

[468] Sec. 408(o)(5).

[469] Secs. 4973(b) and (f).

Description of Proposal[470]

The proposal clarifies that the increase in the age on which the required beginning date for required minimum distributions is based (to age 72) does not change the general requirement to actuarially increase the accrued benefit of an employee who retires in a calendar year after the year the employee attains age 70½ (other than a five-percent owner) to take into account the period after age 70½ in which the employee was not receiving any benefits under the plan.[471]

The proposal also clarifies that the excise tax on excess contributions to an IRA generally does not apply to difficulty of care payments contributed to an IRA.[472]

Effective Date

The amendments made by the proposal are effective as if included in the section of the SECURE Act to which the amendment relates.

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[470] In addition to the clarifications described below, the proposal fixes a clerical error in section 72(t).

[471] Sec. 401(a)(9)(C)(iii).

[472] The excise tax does not apply to any designated nondeductible contribution to an IRA that does not exceed the limit on nondeductible contributions by reason of the individual's election to increase such limit to account for the difficulty of care payment. Sec. 4973(b) (as amended by this proposal).

E. Administrative Provisions

1. Provisions relating to plan amendments

Present Law

Present law provides a remedial amendment period during which, under certain circumstances, a retirement plan may be amended retroactively in order to comply with tax qualification requirements.[473] In general, plan amendments to reflect changes in the law generally must be made by the time prescribed by law for filing the income tax return of the employer for the employer's taxable year in which the change in law occurs (including extensions). The Secretary may extend the time by which plan amendments need to be made.

The Code and ERISA provide that, in general, accrued benefits cannot be reduced by a plan amendment.[474] This prohibition on the reduction of accrued benefits is commonly referred to as the "anti-cut-back rule."

Description of Proposal

The proposal permits certain plan amendments made pursuant to the changes in the Act, or regulations issued thereunder, to be retroactively effective. If a plan amendment meets the requirements of the proposal, then the plan will be treated as being operated in accordance with its terms, and the amendment will not violate the anti-cut-back rule. In order for this treatment to apply, the plan must be operated as if the plan amendment were in effect, and the amendment is required to be made on or before the last day of the first plan year beginning on or after January 1, 2023 (or such later date as the Secretary may prescribe). However, if the plan is a governmental plan, the amendment is required to be made on or before the last day of the first plan year beginning on or after January 1, 2025 (or such later date as the Secretary may prescribe).

If the amendment is required to be made to retain qualified status as a result of the changes in the law (or regulations), the amendment is required to be made retroactively effective as of the date on which the change became effective with respect to the plan and the plan is required to be operated in compliance until the amendment is made. Amendments that are not required to retain qualified status but that are made pursuant to the changes made by the Act (or applicable regulations) may be made retroactively effective as of the first day the amendment is effective.

A plan amendment will not be considered to be pursuant to the Act (or applicable regulations) if it has an effective date before the effective date of the proposal under the Act (or regulations) to which it relates. Similarly, the proposal does not provide relief from the anti-cut-back rule for periods prior to the effective date of the relevant proposal (or regulations) or the plan amendment. The Secretary (or the Secretary's delegate) is authorized to provide exceptions

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[473] Sec. 401(b).

[474] Code sec. 411(d)(6); ERISA sec. 204(g).

to the relief from the prohibition on reductions in accrued benefits. It is intended that the Secretary will not permit inappropriate reductions in contributions or benefits that are not directly related to the proposals under the Act.

The proposal also amends the deadlines for certain plan amendments made pursuant to the SECURE Act and the Coronavirus Aid, Relief, and Economic Security Act, to conform with the deadlines provided under this proposal.[475]

Effective Date

The proposal is effective on date of enactment.

[475] The proposal modifies the general deadlines for plan amendments under the SECURE Act (section 601 of the SECURE Act), and the deadlines for amendments relating to coronavirus-related distributions and the waiver of required minimum distributions under the Coronavirus Aid, Relief, and Economic Security Act, Pub. L. No. 116-136, sections 2202 and 2203.

F. Revenue Provisions

1. SIMPLE and SEP Roth IRAs

Present Law

An IRA is generally established by an individual for whom the IRA is maintained.[476] In some cases, an employer may establish IRAs on behalf of employees and provide retirement contributions to the IRAs. In addition, IRA treatment may apply to accounts maintained for employees under a trust created by an employer (or an employee association) for the exclusive benefit of employees or their beneficiaries, provided that the trust complies with the relevant IRA requirements and separate accounting is maintained for the interest of each employee or beneficiary.[477] In that case, the assets of the trust may be held in a common fund for the account of all individuals who have an interest in the trust.

There are two basic types of IRAs: traditional IRAs, to which deductible or nondeductible contributions can be made, and Roth IRAs, contributions to which are not deductible. The total contributions made to all IRAs for a year cannot exceed $6,000 (for 2021), plus an additional $1,000 (not indexed) in catch-up contributions for individuals age 50 or older. Certain individuals are not permitted to make deductible contributions to a traditional IRA or to make contributions to a Roth IRA, depending on their income.

Distributions from traditional IRAs are generally includible in income, except to the extent a portion of the distribution is treated as a recovery of the individual's basis (if any). Qualified distributions from a Roth IRA are excluded from income;[478] other distributions from a Roth IRA are includible in income to the extent of earnings. IRA distributions generally can be rolled over to another IRA or qualified retirement plan; however, a distribution from a Roth IRA generally can be rolled over only to another Roth IRA or a designated Roth account.

Savings Incentive Match Plan for Employees ("SIMPLE") plans and Simplified Employee Pension ("SEP") plans are special types of employer-sponsored retirement plans to which the employer makes contributions to IRAs established for each of the employer's

[476] Secs. 219, 408, and 408A provide the rules for IRAs. Under section 408(a)(2) and (n), only certain entities are permitted to be the trustee of an IRA. The trustee of an IRA generally must be a bank, an insured credit union, or a corporation subject to supervision and examination by the Commissioner of Banking or other officer in charge of the administration of the banking laws of the State in which it is incorporated. Alternatively, an IRA trustee may be another person who demonstrates to the satisfaction of the Secretary that the manner in which the person will administer the IRA will be consistent with the IRA requirements.

[477] Sec. 408(c).

[478] A qualified distribution is a distribution that (1) is made after the five-taxable-year period beginning with the first taxable year for which the individual first made a contribution to a Roth IRA, and (2) is made after attainment of age 59½, on account of death or disability, or is made for first-time homebuyer expenses of up to $10,000. Sec. 408A(d)(2).

employees in accordance with the Code requirements for each type of plan.[479] SIMPLE IRAs and SEPs may not be designated as Roth IRAs.[480]

SIMPLE IRA plans

An employer is generally eligible to establish a SIMPLE IRA plan if it had no more than 100 employees who received at least $5,000 of compensation from the employer in the preceding year.[481] Contributions to a SIMPLE IRA plan may include employee salary reduction contributions (i.e., elective deferrals) and employer contributions either in the form of matching contributions up to three percent of an employee's compensation or nonelective contributions of a flat two percent of compensation regardless of the employee's elective deferral.

SIMPLE IRA plans may be designed so that the employee will receive cash compensation unless the employee affirmatively elects to make elective deferrals to the plan. Alternatively, a plan may provide that elective deferrals are made at a specified rate (when the employee becomes eligible to participate) unless the employee elects otherwise (i.e., affirmatively elects not to make contributions or to make contributions at a different rate). This alternative plan design is referred to as automatic enrollment. Starting with taxable years after December 31, 2019, eligible employers are allowed a credit of $500 per year for up to three years for startup costs for new SIMPLE IRA plans that include automatic enrollment. An employer is also allowed a credit of $500 per year for up to three years if it converts an existing plan to an automatic enrollment design.

There is an annual threshold on the amount of an elective deferral that an employee may make to a SIMPLE IRA plan (subject to cost of living adjustments). The salary reduction contributions under a SIMPLE IRA plan count toward the overall annual limit on elective deferrals an employee may make to this and other plans permitting elective deferrals. For 2021, the annual contribution limit for SIMPLE IRA plans is $13,500. If permitted by the SIMPLE IRA plan, participants who are age 50 or above at the end of the calendar year may also make catch up contributions, the limit for which is $3,000 in 2021.

SEP IRA plans

A Simplified Employee Pension ("SEP") plan is a special type of employer-sponsored retirement plan whereby only the employer makes contributions to the plan.[482] Unlike SIMPLE IRA plans, any size employer may establish a SEP plan. The amount of the contribution to the SEP IRA plan is up to the lesser of 25 percent of the employee's compensation or the dollar limit applicable to contributions to a qualified defined contribution plan ($58,000 for 2021).[483] A

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[479] Secs. 408(p), (k).

[480] Sec. 408A(f)(1).

[481] Sec. 408(p).

[482] Sec. 408(k).

[483] *Ibid.*

traditional IRA is set up for each eligible employee, and all contributions must be fully vested. Any employee must be eligible to participate in the SEP if the employee has (1) attained age 21, (2) performed services for the employer during at least three of the immediately preceding five years, and (3) received at least $650 (for 2021) in compensation from the employer for the year.[484] Contributions to a SEP generally must bear a uniform relationship to compensation.

Effective for taxable years beginning before January 1, 1997, certain employers with no more than 25 employees could maintain a salary reduction SEP ("SARSEP") under which employees could make elective deferrals. The SARSEP rules were generally repealed with the enactment of the SIMPLE plan rules. However, contributions may continue to be made to SARSEPs that were established before 1997. Salary reduction contributions to a SARSEP are subject to the same limit that applies to elective deferrals under a section 401(k) plan ($19,500 for 2021). An individual who has attained age 50 before the end of the taxable year may also make catch-up contributions to a SARSEP up to a limit of $6,500 (for 2021).

Roth Contributions

Elective deferrals are generally made on a pre-tax basis. However, certain retirement plans, such as section 401(k), section 403(b), and governmental 457(b) plans, may include a qualified Roth contribution program under which elective deferrals are made on an after-tax basis (designated Roth contributions), and attributable distributions are excluded from income. The annual dollar limit on a participant's designated Roth contributions is the same as the limit on elective deferrals, reduced by the participant's elective deferrals that are not designated Roth contributions. Designated Roth contributions are generally treated the same as any other elective deferral for certain purposes, including the restrictions on distributions.

Description of Proposal

Under the proposal, a SEP and a SIMPLE IRA are permitted to be designated as Roth IRAs. Contributions to a SEP or SIMPLE IRA that is a designated Roth IRA are not excludable from gross income (employer contributions as well as elective deferrals), and qualified distributions from such Roth IRAs are excludable from gross income. With respect to SEP and SIMPLE IRAs, an individual retirement plan that is designated as a Roth IRA shall not be treated as a SEP or SIMPLE IRA unless the employee elects for the plan to be treated as such (at such time and in such manner as the Secretary may provide). In the case of any payment or distribution out of a SIMPLE IRA, with respect to which an election has been made and which is received during the two-year period beginning on the date the individual first participated in any salary reduction arrangement in a SIMPLE IRA maintained by the individual's employer,[485] a "qualified rollover distribution" shall not include any payment or distribution paid into an account other than a SIMPLE IRA.

The contribution limit for Roth IRAs generally is increased by the contributions made on the individual's behalf to the SIMPLE IRA or SEP for the taxable year, subject to certain limits.

[484] The annual compensation limit for SEPs is $290,000.

[485] Sec. 72(t)(6).

In this case of a SIMPLE IRA, the Roth IRA contribution limit is increased only to the extent that the contributions made on the individual's behalf (1) do not exceed the sum of the limit on elective contributions to a SIMPLE IRA and the required employer contribution to such IRA,[486] and (2) do not cause the individual's elective contributions to exceed the elective deferral limit.[487] In the case of a SEP plan, the Roth IRA contribution limit is increased only to the extent that the contributions made on the individual's behalf do not exceed the annual contribution limit applicable to SEPs.[488]

Effective Date

The proposal applies to taxable years beginning after December 31, 2021.

2. Hardship withdrawal rules for 403(b) plans

Present Law

Background on rules related to hardship distributions under a section 403(b) plan may be found in section C.16. of this document.

Description of Proposal

The proposal conforms the hardship distribution rules for section 403(b) plans to those of section 401(k) plans. Thus, the proposal provides that in addition to elective deferrals, a section 403(b) plan may distribute, on account of an employee's hardship, qualified nonelective contributions,[489] qualified matching contributions,[490] and earnings on any of these contributions (including on elective deferrals).

Effective Date

The proposal is effective for plan years beginning after December 31, 2021.

3. Elective deferrals generally limited to the regular contribution limit

Present Law

Defined contribution plan limits

Qualified retirement plans (and other tax-favored employer-sponsored retirement plans) are accorded special tax treatment and fall into two categories: defined benefit plans and defined

[486] Sec. 408(p)(2).

[487] Sec. 402(g)(1) (taking into account any additional elective deferrals permitted as catch-up contributions under section 414(v)).

[488] Sec. 408(j).

[489] As defined in section 401(m)(4)(C).

[490] As defined in section 401(k)(3)(D)(ii)(I).

contribution plans. A defined contribution plan is a type of qualified retirement plan whereby contributions, earnings, and losses are allocated to a separate account for each participant.

Defined contribution plans may provide for nonelective contributions and matching contributions by employers and pre-tax (that is, contributions are either excluded from income or deductible) or after-tax contributions by employees. Total contributions made to an employee's account for a year cannot exceed the lesser of $58,000 (for 2021) or the employee's compensation.

Under certain types of defined contribution plans, including section 401(k) plans, section 403(b) plans, or governmental section 457(b) plans, an employee may elect to have contributions (elective deferrals) made to the plan, rather than receive the same amount in cash. The maximum annual amount of elective deferrals that can be made by an employee for a year is $19,500 (for 2021) or, if less, the employee's compensation.[491] For an employee who attains age 50 by the end of the year, the dollar limit on elective deferrals is increased by $6,500 (for 2021) (called "catch-up contributions").[492] Elective deferrals generally cannot be distributed from the plan before the employee's severance from employment, death, disability or attainment of age 59½ or in the case of hardship or plan termination.

Catch-up contributions

Certain retirement plans may permit employees to make catch-up contributions, subject to certain limitations. Employees aged 50 or older may make catchup contributions to a section 401(k), section 403(b), and governmental 457(b) plans, up to $6,500 in 2021 (indexed for inflation). If elective deferral and catch-up contributions are made to both a qualified defined contribution plan and a section 403(b) plan for the same employee, a single limit applies to the elective deferrals under both plans. Special contribution limits apply to certain employees under a section 403(b) plan maintained by a church. In addition, under a special catch-up rule, an increased elective deferral limit applies under a plan maintained by an educational organization, hospital, home health service agency, health and welfare service agency, church, or convention or association of churches in the case of employees who have completed 15 years of service. In this case, the limit is increased by the least of (1) $3,000, (2) $15,000, reduced by the employee's total elective deferrals in prior years, and (3) $5,000 times the employee's years of service, reduced by the employee's total elective deferrals in prior years.[493]

The section 457(b) plan limits apply separately from the combined limit applicable to section 401(k) and 403(b) plan contributions, so that an employee covered by a governmental section 457(b) plan and a section 401(k) or 403(b) plan can contribute the full amount to each

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[491] Secs. 402(g); 457(c). This limit applies to total elective deferrals under all of a participant's section 401(k) plans and section 403(b) plans but applies separately to any governmental section 457(b) plan.

[492] Sec. 414(v).

[493] Because contributions to a defined contribution plan cannot exceed an employee's compensation, contributions for an employee are generally not permitted after termination of employment. However, under a special rule, a former employee may be deemed to receive compensation for up to five years after termination of employment for purposes of receiving employer nonelective contributions under a section 403(b) plan.

plan. In addition, under a special catch-up rule, for one or more of the participant's last three years before normal retirement age, the otherwise applicable limit is increased to the lesser of (1) two times the normal annual limit ($39,000 for 2021) or (2) the sum of the otherwise applicable limit for the year plus the amount by which the limit applicable in preceding years of participation exceeded the deferrals for that year.

Roth contributions

Elective deferrals are generally made on a pre-tax basis. However, certain retirement plans, such as section 401(k), section 403(b), and governmental section 457(b) plans, may include a qualified Roth contribution program under which elective deferrals are made on an after-tax basis (designated Roth contributions), and qualified distributions are excluded from income.[494] A qualified distribution is a distribution that (1) is made after the five-taxable-year period beginning with the first taxable year for which the individual first made the contribution, and (2) is made after attainment of age 59½, or on account of death or disability.

Description of Proposal

Under the proposal, a section 401(a) qualified plan, section 403(b) plan, or governmental section 457(b) plan that permits an eligible participant to make catch-up contributions must require such contributions to be designated Roth contributions. The proposal does not apply to a Savings Incentive Match Plan for Employees ("SIMPLE") IRA or Simplified Employee Pension ("SEP") plan.

Effective Date

The proposal applies to taxable years beginning after December 31, 2021.

4. Optional treatment of employer matching contributions as Roth contributions

Present Law

Defined Contribution Plan Contributions

Defined contribution plans may provide for nonelective contributions and matching contributions by employers and pre-tax (that is, contributions are either excluded from income or deductible) or after-tax contributions by employees. Total contributions made to an employee's account for a year cannot exceed the lesser of $58,000 (for 2021) or the employee's compensation. The deduction for employer contributions to a defined contribution plan for a year is generally limited to 25 percent of the participants' compensation. A participant must at all times be fully vested in his or her own contributions to a defined contribution plan and must

[494] Sec. 402A.

vest in employer contributions under three-year cliff vesting or two-to-six-year graduated vesting.[495]

Defined contribution plans can be further categorized into different types, such as profit-sharing plans, stock bonus plans, or money purchase plans, and may include special features, such as a qualified cash or deferred arrangement (section 401(k)) or an employee stock ownership plan ("ESOP"). Under a common type of retirement arrangement, a section 401(k) plan, an employee may elect to have contributions (elective deferrals) made to the plan, rather than receive the same amount in cash. For 2021, elective deferrals of up to $19,500 may be made, plus, for employees aged 50 or older, up to $6,500 in catch-up contributions. Elective deferrals generally cannot be distributed from the plan before the employee's severance from employment, death, disability, or attainment of age 59½ or in the case of hardship or plan termination.

Designated Roth contributions

Elective deferrals are generally made on a pre-tax basis.[496] However, certain defined contributions plans, such as a section 401(k), 403(b), or governmental 457(b) plan, may include a qualified Roth contribution program under which elective deferrals are made on an after-tax basis (designated Roth contributions), but certain distributions ("qualified distributions"), including earnings, are excluded from income.[497] A qualified distribution is a distribution that (1) is made after the five-taxable-year period beginning with the first taxable year for which the individual first made the contribution, and (2) is made after attainment of age 59½, or on account of death or disability.

Employer Contributions

Employers generally are not required to make contributions to a defined contribution plan, but many employers make matching contributions or nonelective contributions. Matching contributions are employer contributions that are made only if the employee makes contributions and can relate to pre-tax elective deferrals, designated Roth contributions, or other after-tax contributions. Matching contributions are generally based on a formula that is a percentage of the employee's contribution to the plan. Alternatively, matching contributions may be made by the employer to the plan that are a flat dollar amount up to a particular percentage of the employee's compensation.

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[495] Under the automatic enrollment 401(k) safe harbor, the matching and nonelective contributions are allowed to become 100 percent vested only after two years of service (rather than being required to be immediately vested when made).

[496] Section 401(k) plans may be designed so that elective deferrals are made only if the employee affirmatively elects them. However, a section 401(k) plan may provide for "automatic enrollment," under which elective deferrals are made at a specified rate unless the employee affirmatively elects not to make contributions or to make contributions at a different rate. Various rules have been developed to provide favorable treatment for plans that provide for automatic enrollment, subject to certain notice requirements.

[497] Sec. 402A.

In contrast, nonelective contributions are made without regard to whether the employee makes pre-tax or after-tax contributions. Nonelective contributions by an employer are based on a fixed or discretionary formula that could take into account the participant's years of service or age. Nonelective contributions could also generally be a flat dollar amount to the plan for each eligible employee.

If an employee makes elective deferrals that are designated Roth contributions to a defined contribution plan, the employer may not make matching or nonelective contributions on a Roth basis. The employer may only allocate contributions to match designated Roth contributions into a pre-tax account.

Description of Proposal

Under the proposal, a section 401(a) qualified plan, a section 403(b) plan, or a governmental 457(b) plan may permit an employee to designate matching contributions as designated Roth contributions. An employer matching contribution that is a designated Roth contribution shall not be excludable from gross income.

Effective Date

The proposal applies to contributions made after the date of the enactment.