POLLARD
& Associates, Inc.
Consultants, Actuaries and Administrators of Pension
and Profit Sharing Plans Since 1970

One North Park Drive, Suite 104
Hunt Valley, MD 21030-1816
410.771.3035
fax 410.771.3036
pollardpensions.com

New Roth Rules & Options Under SECURE 2.0

Summary as of August 29, 2023

Roth Catch-Up Contributions – Delayed Effective Date

On Friday August 25, 2023, the IRS released guidance postponing the SECURE 2.0 Roth Catch-up contribution requirement. The guidance grants a two-year delay to the effective date of this provision which would have mandated that Catch-up contributions beginning January 1, 2024 be designated Roth contributions for employees earning more than $145,000. Because of the delay granted by the IRS, Catch-up contributions can continue to be made on a pre-tax basis, regardless of income, through December 31, 2025. The new rules outlined below won't become effective until January 1, 2026.

The IRS intends to issue more detailed guidance about this rule during the next two years. We will provide updates as they are available.

Roth Catch-Up Contributions required for Employees who earn in excess of $145,000 - (Required Provision)

Beginning in 2024 (now delayed until 2026), any employee whose W2 for the prior year exceeds $145,000 will be required to make their age 50+ Catch-up contribution as a Roth contribution. Pay from an unrelated Employer is not considered; the $145,000 threshold is based on pay from the Employer sponsoring the Plan. This provision was added by Congress in order to increase government revenue to offset the cost of other provisions under SECURE 2.0, allowing it to be revenue neutral. Participants in this category will no longer be able to make their Catch-up contributions on a pre-tax basis. If they are by mistake made pre-tax, the plan will be required to either recharacterize them or refund them in order to remain compliant.

If your Plan currently does not have Roth provisions, you will be required to add Roth provisions in order for participants to continue to make Catch-up contributions. If you elect not to add Roth provisions, you will have to remove the Catch-up provisions entirely from your plan.

The $145,000 threshold is based on W2 income only; it does not include distributions for S-Corporation owners. Therefore, if an S-Corp shareholder has a W-2 of $125,000 for example, plus distribution of $100,000, he or she can continue to make Catch-up contributions pre-tax.

This restriction does not appear to apply to Sole Practitioners or Partners whose earned income is reported on a Schedule C or K-1, so these individuals can presumably continue to make Catch-up contributions on a pre-tax basis, pending further IRS guidance.

The $145,000 threshold amount will be subject to cost-of-living increases each year. Please note this limit is separate from the Highly-Compensated Employee threshold, which for 2023 is $150,000.

Roth Balances no longer required to be included for purposes of calculating a Participant's Required Minimum Distribution (RMD) – (Required Provision)

For participant RMD calculations beginning in 2024, Roth account balances will no longer be included. This will put Roth plan balances in the same position for RMD purposes as Roth IRAs and will result in reduced RMD withdrawals.

Calculations for satisfying 2023 RMD requirements must still include Roth balances even if taken as late as April 1, 2024 (for a first time RMD payment).

No action is needed on your part for this change. We will automatically exclude Roth balances in our 2024 RMD calculations.

Roth Employer Contributions – (Optional Provision)

A provision that Congress made effective immediately with the passage of Secure 2.0 is one that would allow a Plan to allow their participants the option to have their Company contributions (Safe Harbor, Match and/or Profit Sharing) made directly to the Plan as Roth contributions. This feature is only available to defined contribution plans with a 401(k) or 403(b) feature; Profit Sharing only plans are not eligible for this option.

From a practical standpoint, this provision is not yet operable since there are no IRS guidelines yet to implement it. At this point, we don't know yet when guidance may be available. Nor do we know how the tax reporting on this election will have to be made. In the meantime, a provision that is already operative is one that allows participants to elect an in-plan Roth conversion of any portion of their fully vested account balance in order to accomplish a similar result.

As attractive as this option may be, especially to younger, low-income tax bracket employees, a big deterrent may be that current income taxes will be due on the amount contributed and will have to be paid with personal funds. It will remain to be seen if the immediate tax impact of this election may dissuade participants from electing this option.

Our goal in this notification is to make our Plan Sponsors aware of this provision, but also to recommend that you wait until all the technicalities are worked out before implementation. 401(k) Investment Providers are not currently set up to allow for this provision operationally. Once further guidance and logistics are available, we will be ready to provide recommendations for your specific Plan needs.