LINDA C. SLIDER

ATTORNEY AT LAW

P.O. BOX 5756
WALNUT CREEK, CALIFORNIA 94596

TEL: (925) 932-8450
FAX: (925) 938-4844
LINDA@SLIDERLAW.COM

January 18, 2023

Dear Clients and Friends:

I hope that you have all come through the recent storms safe and dry. I want to update you on the latest news about tax relief for taxpayers who reside in areas which have been hit hard by the storms. I also want to provide you with a summary of the key provisions included in the recent legislation commonly known as "SECURE 2.0", which might impact your retirement account (or your business's retirement plans).

TAX RELIEF FOR TAXPAYERS IN FEDERALLY-RECOGNIZED DISASTER AREAS. The IRS has provided disaster tax relief to victims of California storms that began on January 8, 2023. According to the IRS, storm victims who live or have a business in the federally-recognized disaster area (the "Disaster Area") now have until May 15, 2023, to file various federal individual and business tax returns and to make tax payments.

The Disaster Area includes the following California counties: Alameda, Colusa, Contra Costa, El Dorado, Fresno, Glenn, Humboldt, Kings, Lake, Los Angeles, Madera, Marin, Mariposa, Mendocino, Merced, Mono, Monterey, Napa, Orange, Placer, Riverside, Sacramento, San Benito, San Bernardino, San Diego, San Francisco, San Joaquin, San Luis Obispo, San Mateo, Santa Barbara, Santa Clara, Santa Cruz, Solano, Sonoma, Stanislaus, Sutter, Tehama, Tulare, Ventura, Yolo and Yuba .

The IRS has postponed various tax filing and payment deadlines that occurred beginning on January 8, 2023, for taxpayers (including individuals, households and businesses) who use an address located in the Disaster Area for federal tax purposes. As a result, individuals and households who live or have a business in the Disaster Area will have until May 15, 2023, to file returns and pay taxes that were originally due during this period. This tax relief includes business returns due on March 15 and business and individual returns due on April 18, 2023. In addition, farmers who forgo making an estimated tax payment in January and normally file their returns by March 1, now have until May 15, 2023, to file their 2022 return and pay any tax due.

The May 15, 2023, deadline also applies to (i) the quarterly estimated tax payments normally due on January 17, 2023, and April 19, 2023, and (ii) the quarterly payroll and excise tax returns normally due on January 31 and April 30, 2023. In addition, penalties on payroll and excise tax deposits due on or after January 8, 2023, and before January 23, 2023, will be abated if the tax deposits are made by January 23, 2023.

The IRS will automatically apply this tax relief to any taxpayer with an address in the Disaster Area. Affected taxpayers who receive a penalty notice from the IRS for a return that has a due date falling within the postponement period (January 8, 2023, to May 15, 2023) should call the phone number on the notice to have the penalty abated. In addition, taxpayers who live or have a business outside the Disaster Area but whose tax records are in the Disaster Area and taxpayers assisting in disaster relief activities can call the IRS at 866-562-5227 to ask for this tax relief.

Finally, affected taxpayers in the Disaster Area who suffered uninsured or unreimbursed disaster-related losses can choose to claim these losses on either the current year (2023) or prior year 2022 return. Affected taxpayers claiming disaster losses should write the FEMA declaration number (3691-EM) on any return claiming such a loss. Please see IRS Publication 547 for further details on claiming uninsured or unreimbursed disaster-related losses.

KEY PROVISIONS OF SECURE 2.0. In late December, 2022, Congress passed an omnibus budget bill (signed into law on December 29, 2022). This omnibus budget bill included the Setting Every Community Up for Retirement Enhancement 2.0 Act of 2022 ("SECURE 2.0"). SECURE 2.0 contains many changes that provide new benefits for individuals to improve their retirement security, new incentives for small businesses to offer (or expand) retirement plans to their employees, and new provisions for employer-provided retirement plans to ease the costs, administrative burdens, and penalties for inadvertent mistakes. Retirement plans will need to be amended to fully comply with the provisions of SECURE 2.0, but SECURE 2.0 provides for a generous extended deadline to formally adopt amendments, as long as the plan operates in compliance with SECURE 2.0 (pending adoption of retroactive amendments).

Provisions Benefiting Individuals: SECURE 2.0 contains many new provisions which will benefit individuals in their retirement planning:

- *Age Increased For Required Distributions.* Under prior law, the required beginning date ("RBD") for starting required minimum distributions ("RMDs") for IRA owners, retired employer plan members, and active-employee 5%-owners was April 1 of the year following the year in which the individual reached age 72 (the "RBD Age"). SECURE 2.0 increases the RBD Age (in two stages): (i) the RBD Age increases from the current RBD Age of 72 to age 73 for those who turn age 72 after 2022, and (i) the RBD Age increases to 75 for those who attain age 74 in 2032 or later. The increase in the RBD Age means that eligible individuals will have greater flexibility over the timing of retirement distributions in the years leading up to their RBD Age.

- *Reduced Penalty Tax On Failure To Take RMDs.* For tax years beginning after December 29, 2022, SECURE 2.0 reduces the penalty for failure to take RMDs from qualified retirement plans, including IRAs, or deferred compensation plans under Code §457(b) from the current 50% to 25% of the amount by which the distribution falls short of the required amount. The penalty is reduced to 10% if the failure to take an RMD is corrected in a timely manner. This is a most-welcome change to reduce a confiscatory penalty for even inadvertent RMD errors.

- *Bigger Catch-Up Contributions Permitted.* Starting in 2025, SECURE 2.0 increases the elective "catch-up" retirement contribution limit for employees aged 50 or older from $7,500 for 2023 ($3,500 for SIMPLE plans) to the greater of (i) $10,000 ($5,000 for SIMPLE plans), referred to as the "regular catch-up amount", or (ii) 150% of the regular catch-up amount for individuals who have attain ages 60-63. The dollar amounts are inflation-indexed after 2025. Please note that for high-income taxpayers, catch-up contributions may be restricted to Roth treatment for tax years starting after 2023.

- *More Penalty-Free Withdrawals Permitted.* Generally, a taxpayer is subject to a 10% penalty on withdrawals from retirement plans and IRA accounts (and on certain withdrawals from Roth IRA accounts) before reaching age 59 ½, with certain exceptions. SECURE 2.0 adds a number of new exceptions from the 10% penalty tax to permit individuals who encounter certain types of hardships to have greater access to their retirement funds. Please note that the effective dates for these new "penalty-free withdrawals" and the rules for withdrawals and requirements for re-payment of the withdrawal differ widely, so please exercise caution. The new penalty-free withdrawal exceptions are as follows:

    - <u>After 2023</u>, there will be an exception to the 10% penalty tax for one distribution per year of up to $1,000, for emergency expenses to meet unforeseeable or immediate financial needs relating to personal or family emergencies. The taxpayer has the option to repay the distribution within three years. No other emergency distributions are permissible during the three-year period unless repayment occurs.

    - <u>After 2023</u>, plans may permit participants that self-certify that they have experienced domestic abuse to withdraw the lesser of $10,000 (indexed for inflation) or 50% of their account, free of the 10% penalty tax. The participant has the opportunity to repay the withdrawn money from the retirement plan over three years and get a refund of income taxes on money that is repaid.

    - <u>Beginning December 29, 2025</u>, retirement plans may make penalty-free distributions of up to $2,500 per year for payment of premiums for high quality coverage under certain long term care insurance contracts.

    - <u>Retroactive for federally-declared disasters after January 25, 2021</u>, penalty-free distributions of up to $22,000 may be made from employer retirement plans or IRAs for affected individuals in federally-declared disasters. Regular tax on the distributions is taken into account as gross income over three years. Distributions can be repaid. Additionally, amounts distributed prior to the federally-declared disaster to purchase a home can be recontributed, and an employer may provide for a larger amount to be borrowed from a plan by affected individuals and for additional time for repayment of plan loans owed by affected individuals.

    - <u>Effective as of December 29, 2022</u>, penalty-free distributions are available for terminally ill participants. An illness is considered terminal if a physician certifies in writing that the illness is reasonably likely to result in death within 84 months.

    - SECURE 2.0 also contains an emergency savings provision that allows employers to offer non-highly compensated employees emergency savings accounts linked to individual account plans that automatically opt employees into these accounts at no more than 3% of their salary, capped at a maximum of $2,500. Employees can withdraw up to $1,000 once per year for personal or family emergencies without certain tax consequences.

- *Favorable Surviving Spouse Election.* For plan years after 2023, if an employee dies before RMDs have begun under an employer qualified retirement plan and the employee's surviving spouse is the designated beneficiary of the employee's retirement plan interest, the surviving spouse may elect to be treated as if the surviving spouse were the employee for purposes of calculating RMDs. If the election is made, RMDs need not begin until the employee would have had to start them. This provision allows a designated spousal beneficiary to receive a similar distribution period for lifetime distributions under an employer plan as would be permitted if the surviving spouse rolled the retirement plan interest into an IRA. IRS will prescribe the time and manner of the election, which once made may not be revoked without IRS' consent.

- *Employer Match For Student Loan Payments.* Certain employees may not be able to save for retirement because they are overwhelmed with student debt and, as a result, may miss out on available matching contributions for retirement plans. <u>For plan years after 2023</u>, SECURE 2.0 allows employers to make matching contributions under a 401(k) plan, 403(b) plan, or SIMPLE IRA for an employee's "qualified student loan payments."

- *Tax-Free Rollovers From 529 Accounts To Roth IRAs.* <u>After 2023</u>, SECURE 2.0 permits beneficiaries of 529 college savings accounts to make up to $35,000 of direct trustee-to-trustee rollovers from a 529 account to their Roth IRA without tax or penalty. The 529 account must have been open for more than 15 years, and the rollover is limited to the amount contributed to the 529 account (and its earnings) more than five years earlier. Rollovers are subject to the Roth IRA annual contribution limits, but are not limited based on the taxpayer's adjusted gross income.

- *Broadened Eligibility For ABLE Programs.* States may establish tax-exempt ABLE programs to assist persons with disabilities, which enable eligible disabled persons and their families to save for qualified expenses on a tax-favored basis. Under current law, an individual must become disabled or blind before age 26 to be eligible to establish an ABLE account. SECURE 2.0 raises the age threshold from 26 to 46. The change is effective for tax years beginning after 2025.

- *Tax-Exempt Disability Retirement Payouts For First Responders.* SECURE 2.0 allows law enforcement officers, fire fighters, paramedics, and emergency medical technicians to exclude from gross income certain service-related disability pension or annuity payments [from a 401(a), 403(a), governmental 457(b), or 403(b) plan] after they reach retirement age. The exclusion applies to amounts received for post-2026 tax years.

- *Penalty-Free Return Of Excess Contributions.* SECURE 2.0 specifies that earnings attributable to excess IRA contributions that are returned by the taxpayer's tax return due date (including extensions) are exempt from the 10% early withdrawal tax. The taxpayer must not claim a deduction for the distributed excess contribution. This applies to any determination of taxes, interest, or penalties made on or after December 29, 2022.

- *Time Limit On Excess Contribution Excise Tax.* SECURE 2.0 provides that the statute of limitations for the assessment of excise taxes on excess contributions to tax-favored accounts and accumulations on qualified retirement plans begins to run on the filing of the taxpayer's income tax return for the year of the violation and runs for three years (six years in the case of excess contributions). The starting point no longer depends on the plan's filing of an excise tax return.

- *Telehealth Exemption For HDHPs.* To facilitate the use of telehealth during the COVID pandemic, the CARES Act provided that coverage for telehealth and other remote care services would be disregarded coverage which could be provided before a High Deductible Health Plan ("HDHP") minimum deductible was satisfied without causing a loss of Health Savings Account eligibility for plan years (extended through 2022). SECURE 2.0 extends this rule for telehealth and other remote care services for all HDHP plan years beginning before 2025.

Small Employer Provisions: SECURE 2.0 contains several new provisions to encourage small employers to offer new or expanded retirement plans for their employees:

- *Bigger Tax Credit For Start-Up Retirement Plans.* SECURE 2.0 improves the small employer pension plan start-up cost credit (the "Start-Up Credit") in three ways for tax years starting after 2022. First, SECURE 2.0 makes the Start-Up Credit equal to the full amount of creditable plan start-up costs for employers with 50 or fewer employees (up to an annual cap). Previously only 50% of costs were allowed (this 50% cap still applies to employers with 51 to 100 employees). SECURE 2.0 also retroactively fixed a technical glitch that prevented employers who joined multi-employer plans in existence for more than three years from claiming the Start-Up Credit. Employers that joined a pre-existing multi-employer plan in 2000 or 2001 should consider filing amended returns to claim the Start-Up Credit. Perhaps the biggest change is that certain employer contributions for a plan's first five years now may qualify for the Start-Up Credit. The Start-Up Credit is increased by a percentage of employer contributions, up to a per-employee cap of $1,000: The increase is 100% of employer contributions in the plan's first and second tax years, 75% of employer contributions in the third year, 50% of employer contributions in the fourth, and 25% of employer contributions in the fifth. For employers with between 51 and 100 employees, the contribution portion of the credit is reduced by 2% times the number of employees above 50. In addition, no employer contribution credit is allowed for contributions for employees who make more than $100,000 (adjusted for inflation after 2023). The credit for employer contributions also is not available for elective deferrals or contributions to a defined benefit pension plan.

- *New Credit For Military Spouses.* SECURE 2.0 adds a new tax credit for employers with no more than 100 employees earning at least $5,000 for the preceding year for each military spouse who starts participating in an eligible employer defined contribution plan. Highly compensated employees are excluded from consideration. The annual credit amount for the year the spouse begins participating in the plan and each of the next two tax years is (1) $200 for each plan-participating military spouse, plus (2) up to $300 of related employer plan contributions. This new credit is available for tax years beginning after December 29, 2022.

- *Retroactive First-Year Deferrals For Sole Proprietors.* To correct the situation where a sole proprietor can't make an elective deferral for the first year to a plan created after the close of the year, SECURE 2.0 provides that (for plan years beginning after 2022 for a sole proprietor who is the only employee of an unincorporated trade or business) any elective deferral made by the sole proprietor's original tax return due date ending after or with the end of the plan's first plan year, will be treated as made before the end of that first plan year.

<u>Key Provisions For Employer-Provided Retirement Plan</u>: SECURE 2.0 includes additional provisions impacting employer-provided retirement plans:

- *Automatic Salary Deferral Enrollment.* <u>For plan years beginning after 2024,</u> SECURE 2.0 provides that a plan that permits salary deferrals generally will not be treated as a qualified cash or deferred arrangement or annuity contract unless it includes an automatic contribution arrangement (EACA) that satisfies these requirements:

  - It must allow permissible withdrawals within 90 days after the first elective contribution;

  - Automatic contributions must be 3% to 10% during a participant's first participation year, unless the participant elects out, automatically increasing by one percentage point each year to between 10% and 15% (but no more than 10% for plan years ending before 2025 for any non-"safe harbor" plan; and

  - If the participant makes no investment election, automatically contributed amounts must be invested in accordance with DOL default investment rules.

  Automatic enrollment is not required for SIMPLE 401(k) plans, plans established before December 29, 2022, governmental or church plans, plans maintained by an employer in existence for less than three years or with fewer than 11 employees.

- *New "Starter 401(K)" Plans.* SECURE 2.0 establishes two new kinds of retirement plan designs for plan years beginning after 2023, which smaller employers may be inclined to offer to employees due to their eased costs and administrative burdens:

  - A new type of Code § 401(k) plan (called a starter 401(k) deferral-only arrangement), which is a cash or deferred arrangement maintained by an eligible employer that automatically satisfies SECURE 2.0 actual deferral percentage (ADP) nondiscrimination test. An employer can generally offer this type of plan only if it maintains no other plan in that year. All employees who meet the plan's age and service requirements must be eligible to participate. The contribution percentage must be from 3% to 15%, applied uniformly. Employees may elect out or choose to contribute at a different level. No matching or nonelective contributions are permitted. Employee elective contributions for a calendar year may not exceed $6,000, adjusted for inflation, but catch-up contributions of up to

$1,000, inflation indexed, are permitted for employees aged 50 or over.

  - A new type of 403(b) plan called a safe harbor deferral-only plan, for which rules similar to those described for starter 401(k) deferral-only arrangements apply.

- *Improved Coverage For Part-Timers.* SECURE 2.0 modifies the rules that apply to long-term part-time employees under a 401(k) or 403(b) plan which is subject to ERISA, to reduce the service requirement for those employees from three years to two consecutive years, for employees who have worked for the employer at least 500 hours per year and have met the minimum age 21 requirement by the end of the two-year period. This change is effective for plan years beginning after 2024.

- *More Plan Self-Correction Permitted.* SECURE 2.0 expands the use of self-correction of plan administration failures under the IRS Employee Plans Compliance Resolution System (EPCRS) in a number of ways. First, SECURE 2.0 generally allows qualified employer plans under Code §401 and Code §403 (as well as SEPs and SIMPLE IRAs under Code §408) to self-correct certain failures (defined expansively, but not including egregious or abusive violations) without advance permission, unless (i) the failure is identified by the IRS before any corrective actions is taken, or (ii) the self-correction is not completed within a reasonable time after the failure is identified. SECURE 2.0 also directs IRS to allow custodians to use EPCRS to address various IRA failures, including failures to make required minimum distributions and attempted rollovers by non-spouse beneficiaries from inherited IRAs. These provisions are effective as of December 29, 2022, and EPCRS must be revised for these changes within two years.

- *Eased Notice Requirements For Unenrolled Participants.* For plan years after 2022, SECURE 2.0 exempts defined contribution plans from intermittent notification requirements for participants who elect not to participate and who have already received a summary plan description and any other notices related to initial eligibility. However, unenrolled participants must still receive an annual reminder notice of their eligibility to participate (with any applicable deadlines) and certain other documents they request.

- *Extended Plan Amendment Period.* The deadline for plan amendments made under SECURE 2.0 or any related IRS or Department of Labor regulation is the end of the first plan year beginning on or after January 1, 2025 (2027 for governmental and collectively bargained plans). In the interim, a plan that operates as if a retroactive amendment were already in effect generally will not be treated as violating the anti-cutback rules. SECURE 2.0 also conforms certain plan amendment deadlines under the original SECURE Act (enacted in 2019), the CARES Act (enacted in 2020), and the Taxpayer Certainty and Disaster Tax Relief Act of 2020 to these new dates.

- *Catch Up Contributions Of Highly Compensated Participants.* For tax years beginning after 2023, catch-up contributions under Code §401(k), Code §403(b), or Code §457(b) plans are subject to mandatory Roth tax treatment, for those made by participants whose wages for the preceding calendar year exceed $145,000, as annually indexed for inflation. This rule does not apply to SEPs under Code §408(k), or to SIMPLE IRAs under Code §408(p). Even plans that do not provide a designated Roth contribution feature will now be forced to include and account for designated Roth contributions to the extent that they have employees with income that exceeds the annual limitation.

- *Matching Or Nonelective Roth Contribution Option.* Before SECURE 2.0, employers were not permitted to make matching or nonelective contributions on a Roth basis. For contributions made after December 29, 2022, however, a Code §401(a) qualified plan, Code §403(b) plan, or a governmental Code §457(b) plan may permit a participant to designate some or all employer matching contributions and nonelective contributions as designated Roth contributions. This applies only to the extent that a participant is fully vested in these contributions.

- *Contribution Changes For SIMPLE Plans.* Employers with SIMPLE plans currently must either (i) make contributions for employees of 2% of compensation or (ii) match employee elective deferral contributions up to 3%. For tax years beginning after 2023, SECURE 2.0 permits an employer to make additional contributions to each employee of the plan of up to the lesser of (i) up to 10% of compensation or (ii) $5,000 (indexed for inflation). SECURE 2.0 also increases the SIMPLE annual deferral limit and the catch-up contribution at age 50 by 10%, compared to the limit that would otherwise apply in the first year this change is effective (tax years after 2023) for employers with no more than 25 employees. Employers with 26 to 100 employees can provide for higher deferral limits, but only if they either provide a 4% match or a 3% employer contribution. Similar changes to the contribution limits also apply for SIMPLE 401(k) plans.

Changes Relating To Conservation Easements: Finally, SECURE 2.0 includes some "off topic" provisions relating to charitable easements. First, SECURE 2.0 disallows a charitable deduction for an otherwise-qualified conservation easement contribution made by a partnership, S corporation, or other pass-through entity, if the amount contributed exceeds 250% of the sum of each partner/member's basis in the contributing entity. Exceptions apply where the contribution meets (1) a three-year holding period test, (2) substantially all of the contributing entity is owned by members of a family, or (3) the contribution relates to a certified historic structure (for which there is a new reporting requirement). Second, SECURE 2.0 allows taxpayers to correct easement deed language for extinguishment clauses and boundary line adjustments (substituting safe-harbor language to be issued by IRS), but not for easements involving tax shelters, contributions to which the above pass-through disallowance applies, docketed Tax Court cases, or where penalties have been finalized. The provision applies to contributions made after December 29, 2022.

This amount of information might seem overwhelming, but there is much in SECURE 2.0 that may benefit or affect you (individually) or your business. In particular, individuals stand to benefit significantly as they consider how to handle their retirement accounts and distributions. If you or your accountant would like more details about any item discussed in this letter, please do not hesitate to call.

Very truly yours,

Linda C. Slider

Linda C. Slider