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Providing Retirement Benefits Can Benefit Employers

Tax benefits and new credits aim to offset the cost of setting up new retirement plans and can be a ‘big win’ for plan sponsors.

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Retirement plan creation is changing. Both 2019’s Setting Every Community Up for Retirement Enhancement Act and 2022’s SECURE 2.0 Act were designed to incentivize more employers to offer retirement benefits — the incentives are especially significant in SECURE 2.0. New plan sponsors may qualify for a variety of tax credits designed to offset the costs of offering a retirement plan, there are also more choices for plan sponsors to make about what to offer participants.

Incentives for Plan Sponsors

At a high level, the main goal of SECURE 2.0 is to increase retirement savings. To achieve that, lawmakers focused on small- and medium-sized businesses, which have historically been slow to offer retirement plans.

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SECURE 2.0 includes both expansions of existing tax benefits and new tax credits. For employers with up to 50 employees, 100% of startup costs for the plan can be covered during the first three years. Eligible businesses with 51 to 100 employees can qualify for 50% of administrative costs, capped annually at $5,000 per employer for three years.

Depending on the overall size of the plan there are also tax credits for employer contributions or profit-sharing contributions for the first five years of the plan.

Eric Droblyen, president and CEO at Employee Fiduciary, a bundled 401(k) provider, says it may seem counterintuitive to focus on tax benefits to employers, but small and medium-sized businesses often cite administrative costs as reason for not offering retirement benefits. “We’re doing a lot of education right now on the tax benefits because many would-be plan sponsors don’t know about them,” he explains. “If you’re worried about cost as an employer you can get three years with net nothing out of pocket – which is a big win.”

Matthew Hawes, a partner at law firm Morgan Lewis, adds that it is important for plan sponsors to understand that they are not going to be penalized for being fast-growing over that period. “These credits are tied to the number of participants, but they don’t fall off a cliff once you get to employee 51 or employee 101. The incentive is to start earlier in the lifecycle of the company – that way get the highest benefit and can maintain them as you grow.”

New Plan Features

Apart from incentives, SECURE 2.0 also created a number of new requirements for plan sponsors. The law includes more than 90 provisions for plan sponsors, recordkeepers, and service providers to digest.

One significant change is the addition of auto-enrollment to all new plans.

If an employer has established a plan on or after December 29, 2022, it must include an eligible automatic contribution arrangement beginning in 2025. For brand new plans setting this up is a matter of including the functionality as they start. But for companies that are creating new plans as a result of a merger or spinoff, it may

represent a change. Not all legacy plans have an auto-enrollment feature, and the new rules require it, even if the old plan didn't have it.

The 2019 SECURE Act also created a new type of multi-employer plan called the Pooled Employer Plan (PEP). The goal of this provision is to help smaller plan sponsors achieve some of the benefits of large-scale plans by cutting down on administrative costs. SECURE 2.0 went further making this option available to 403(b) plans as well. However, it's important to note that these plans still have to meet the same requirements of single employer plans and that could make issues like auto-enrollment trickier – at least in the short run. PEPs are designed to include companies that do not share commonality across ownership or industry. So shared services like auto-enrollment may require more of a heavy lift if each company has a different payroll or other service providers. meet the same requirements of single employer plans and that could make issues like auto-enrollment trickier – at least in the short run. PEPs are designed to include companies that do not share commonality across ownership or industry. So shared services like auto-enrollment may require more of a heavy lift if each company has a different payroll or other service providers.

Ari Sonneberg, a partner at The Wagner Law Group, adds that a few other provisions may add some administrative complexity. "Some part-time workers may qualify for retirement benefits, for example. We're also getting more questions about catch-up Roth contributions. These are provisions that might make an employer question whether or not to offer a plan because they come with a higher administrative burden. But they also expand savings coverage," he says.

There are also provisions that employers might see as beneficial to hiring and retaining talent, Sonneberg says. SECURE 2.0 expanded the circumstances under which participants can make hardship withdrawals. The law also supports emergency savings accounts and expands the contribution options available for participants who are working to repay student loans.

"If you're setting up a new plan, there is an opportunity here to say to current employees and potential future employees that the company now has a plan with a lot of bells and whistles which could make [a company] stand out competitively," Sonneberg says. "But there are some tradeoffs in terms of total cost and administrative burden. When you add more features, both of those things will increase."

Growing Pains

With 90 provisions to understand and implement, sources say the defined contribution retirement industry is starting a transition period that could last a couple of years. Recordkeepers and other service providers have been in a scramble to make sure their systems and software can support the new provisions but not everyone is fully up and running yet. Service providers and employers are still awaiting guidance from the IRS and Department of Labor on some provisions.

"It makes it difficult for us as recordkeepers to be waiting on this stuff because we're supposed to be in a position to be able to say to plan sponsors – here are the steps and here is the guidance but we don't have all of that yet," says Droblyen.

He adds that if plan sponsors want to get started this year or next year they might want to begin as simply as possible and add features later. "If there is documentation in place and plan sponsors can show good-faith compliance we have seen regulators be relatively lenient during times like this, but it's important to remember that's not a permanent solution. Plans eventually have to be fully compliant."

Michael Gorman, an associate at Morgan Lewis, agrees. "We saw the IRS announce an 'administrative transition period' for Roth catch-up contributions, which they had never done before. So, could we assume they do something similar for other provisions? It's possible because they've crossed the Rubicon," he says. "But we always tell our clients that they still have to be prepared to implement such that they can because a transition period may not be possible for every provision."

Tags DC plan design, retirement plan features, SECURE 2.0 Act of 2022, Setting Every Community Up for Retirement Enhancement Act of 2019, tax incentives

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