HOT OFF THE PRESS

IRS ANNOUNCES LIMITS FOR 2020

ON NOVEMBER 6TH, 2019, THE IRS ANNOUNCED THE COST OF LIVING ADJUSTMENTS AFFECTING THE DOLLAR LIMITATIONS FOR RETIREMENT PLANS. Contribution and benefit increases are based on a calculated change in the Consumer Price Index and are intended to allow participant contributions and benefits to keep up with the "cost of living" from year to year. Here are some highlights from the 2020 changes:

- The elective deferral limit for 2020 has increased from $19,000 to $19,500. This deferral limit applies to each participant on a calendar year basis. The limit applies to 401(k) plans, including Roth and pre-tax contributions, 403(b) and 457(b) plans.
- Catch-Up contributions increased to $6,500 and are available to all participants age 50 or older in 2020.
- The 2020 annual contribution limit has increased to $57,000. This limit indicates the maximum allowable dollar amount that can be contributed to a participant's retirement account in a defined contribution plan. The limit includes both employee and employer contributions as well as any allocated forfeitures. For those over age 50, the annual addition limit increases by $6,500 to include catch-up contributions.
- The annual benefit limit which applies to participants in a defined benefit plan has increased to $230,000 for 2020.
- Compensation thresholds that affect retirement plans have also increased for 2020. The maximum amount of compensation that can be considered in retirement plan compliance has been raised to $285,000. In addition, income subject to Social Security taxation has increased to $137,700 and thresholds for determining key and highly compensated employees have increased to $185,000 and $130,000 respectively.

Annual Plan Limits	2020	2019	2018
Contribution and Benefit Limits			
Elective Deferral Limit	$19,500	$19,000	$18,500
Catch-Up contributions	$6,500	$6,000	$6,000
Annual Contribution Limit	$57,000	$56,000	$55,000
Annual Contribution Limit including Catch-Up Contributions	$63,500	$62,000	$61,000
Annual Benefit Limit	$230,000	$225,000	$220,000
Compensation Limits			
Maximum Plan Compensation	$285,000	$280,000	$275,000
Income Subject to Social Security	$137,700	$132,900	$128,400
Key EE Compensation Threshold	$185,000	$180,000	$175,000
Highly Compensated EE Threshold	$130,000	$125,000	$120,000
IRA Limits			
SIMPLE Plan Elective Deferrals	$13,500	$13,000	$12,500
SIMPLE Catch-Up Contributions	$3,000	$3,000	$3,000
Individual Retirement Account (IRA)	$6,000	$6,000	$5,500
IRA Catch-Up Contribution	$1,000	$1,000	$1,000

The increases in the annual limits allow employers and participants to contribute more toward retirement.

If you have any questions on how these increases can affect your plan, please contact your McCloud & Associates, Inc. representative. ■

SAFE HARBOR 401(K) PLAN DESIGN

BEING THE BEARER OF BAD NEWS ISN'T FUN. When the third-party administration firm relays that aspects of the annual compliance testing have failed causing many of the company's executives to receive taxable distributions from the plan, it isn't a great day for the HR manager. The administrator explains that the regulations require testing to prevent highly paid employees from receiving disproportionately greater benefits than other employees. At a much-needed lunch that day, the HR manager learns from a colleague that they once had the same issue but adopted a "safe harbor" design to solve the problem.

In their 61st Annual Survey of Profit Sharing and 401(k) Plans, the Plan Sponsor Council of America reports that, of the 605 plan sponsor respondents to the survey, 42% reported using a safe harbor design. Since December 1st, 2019 marks the last day to make a safe harbor election for 2020 calendar year plans, understanding the pros and cons of these elections will help you decide if a safe harbor design is the right choice for your plan.

Each year in a non-safe harbor plan, a series of nondiscrimination tests are performed to demonstrate that the contribution rates for highly compensated employees (HCEs) are not disproportionately larger than those for non-HCEs (NHCEs). HCEs are generally owners of more than 5% of the company and any employee with compensation in the prior plan year over a specified level ($125,000 for 2019). If a plan elects to be "safe harbor" for any given year, the compliance testing can be

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> ***— Plan Sponsor Council of America***

avoided by meeting the safe harbor standards. One of the main reasons for adopting a safe harbor design is to allow HCEs to defer up to the maximum dollar limit ($19,000 for 2019) without the potential limitation of the participation rate of the NHCE group.

So, what's the trade off? In order to satisfy a safe harbor election, the employer is required to comply with safe harbor standards which include the following:

- Contribute an employer match or nonelective contribution that satisfies safe harbor requirements. Several matching formulas can qualify but none less than 100% of the first 3% of salary deferred plus 50% of the next 2% deferred (4% total). A non-elective contribution can also be selected which must be at least 3% of pay to all eligible NHCEs. Though not required, the contribution can be made on behalf of HCEs as well.
- The contributions used to satisfy the safe harbor plus any gains must be 100% vested at all times.
- Annually, a notice must be issued to participants announcing the plan's intent to comply with safe harbor provisions for the upcoming year. The notice must contain the basic features of the plan and must be distributed 30 to 90 days prior to the beginning of the plan year for which safe harbor provisions will be implemented. So, for a calendar year plan to elect safe harbor for 2020, notice must be given to participants no later than December 1, 2019.

Does your plan include an automatic enrollment feature? If so, a modified version of the safe harbor plan is available for you. The rules for so-called Qualified Automatic Contribution Arrangements (QACA) are similar to the regular safe harbor rules, except that the QACA matching requirement is 100% of the first 1% of compensation deferred, plus 50% of the next 5% of compensation deferred (maximum match of 3.5%). In addition, safe harbor contributions under the QACA must be 100% vested after two years of service rather than the immediate vesting required of traditional safe harbor plans. The participant notice

must contain additional information describing the automatic enrollment features.

A safe harbor design is an excellent way for many employers to get the most out of their 401(k) plans. By eliminating nondiscrimination testing, all employees can contribute up to the annual deferral limit and not be concerned about the possibility of refunds after year-end. If you think a safe harbor option is right for your plan, contact your account representative at McCloud & Associates, Inc. ■

THE FINAL RULE ON HARDSHIP DISTRIBUTIONS

ON SEPT. 23, THE IRS PUBLISHED A FINAL RULE THAT RELAXES SEVERAL EXISTING RESTRICTIONS ON PARTICIPANT HARDSHIP DISTRIBUTIONS FROM DEFINED CONTRIBUTION PLANS. Some of these changes are mandatory, requiring employers to make the changes by Jan. 1, 2020, while others are optional. Though the IRS had issued the proposed regulations in 2018, the final regulations clarify a few key provisions:

- **The Loan-First Rule.** The new rule removes the requirement that participants exhaust their ability to take a loan from the plan before being granted a hardship. This provision is not mandatory as some plan sponsors view the “loan first” requirement as helpful to participants. Unlike participant loans, hardships permanently reduce a participant’s balance and are subject to income taxes and a 10% early withdrawal penalty if the participant is under age 59½. So, taking a loan first may be in the participant’s best interest.
- **The Six-Month Rule.** Starting January 1st, 2020, plans will no longer be required to suspend participant salary deferral elections following a hardship distribution. Prior to the final rule, the inability for the participant to continue contributing to the plan and the lost opportunity to receive matching contributions further compounded the leakage from a participant’s account caused by the withdrawal.
- **More withdrawal sources available.** In 2020, earnings on 401(k) plans are available for hardship distributions as well as safe harbor or profit-sharing contributions.

Upcoming Compliance Deadlines for Calendar-Year Plans (12/31)

December 2019

1st

Participant Notices – Annual notices due for Safe Harbor elections, Qualified Default Contributions (QDIA), and Automatic Contribution Arrangements (EACA or QACA).

31st

Participant Notices – Annual notices due for ERISA 404(c) and Fee Disclosure.

Discretionary Amendments – Deadline to adopt discretionary plan amendments for calendar-year plans. If changes have been made to your retirement plan this year, the amendment documenting this change must be signed by the last day of the plan year in which it became effective.

Required Minimum Distributions – Participants who have attained age 70½, and have begun receiving distributions from their account, are required to receive a distribution each year prior to December 31st.

January 2020

31st

IRS Form 945 – Deadline to file IRS Form 945 to report income tax withheld from qualified plan distributions made during the prior plan year. The deadline may be extended to February 10th if taxes were deposited on time during the prior plan year.

IRS Form 1099-R – Deadline to distribute Form 1099-R to participants and beneficiaries who received a distribution or a deemed distribution during prior plan year. A deemed distribution can occur if a participant fails to make timely loan repayments.

IRS Form W-2 – Deadline to distribute Form W-2, which must reflect aggregate value of employer-provided employee benefits.

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CONTACT US:

McCloud & Associates, Inc.
200 W. Mill Street
Liberty, MO 64068
816.792.3838
info@mccloudandassociatesinc.com
www.mccloudandassociatesinc.com

- **Disaster Related Expenses.** The new rule adds a seventh category as an acceptable reason for a hardship withdrawal. Disaster related expenses for an employee who lived or worked in a federally declared disaster area is now a safe harbor category that automatically counts as a hardship withdrawal. The other six acceptable hardship reasons are:
  - Medical care expenses for the participant, his/her spouse, dependent, or beneficiaries,
  - Costs directly related to the participant's purchase of his/her primary residence (not including mortgage payments),
  - Amounts necessary to prevent the participant's eviction from, or foreclosure on, the participant's primary residence,
  - Funeral expenses for the participant, his/her spouse, dependents, or beneficiaries,
  - Tuition expenses (fees, room and board, etc.) for the next 12 months of post-secondary education for the participant, his/her spouse, dependents, or beneficiaries,
  - Expenses incurred to repair damage or make improvements to the participant's primary residence. Repairs must fall under the IRS's description of a casualty loss. Damages must be sudden, unexpected or unusual and cannot be from progressive deterioration (normal wear and tear).
- **Showing Financial Need.** Under the rules currently in place, employers and plan administrators must take into account "all relevant facts and circumstances" to determine if a hardship withdrawal is necessary. The new rule requires only that a distribution not exceed what an employee needs and that employees certify that they lack enough cash to meet their financial needs. Plan administrators can rely on that certification unless they have knowledge to the contrary. Plans are required to apply this standard starting in 2020.

For plan sponsors who use "pre-approved" plan documents for their 401(k) plans, the due date to amend your plan for the new regulations is the same as the tax filing deadline (including extensions) for the year in which the provisions become effective. For example, if the new rule is effective on January 1st, 2020 for a plan sponsor with a calendar fiscal year, the due date for amending the plan is the due date of the plan sponsor's 2020 return including extensions. Regardless of the amendment date, compliance must begin on January 1st, 2020. For those who maintain individually designed plans, the deadline will be December 31st, 2021 regardless of plan year.

Plan Sponsors that took action on the proposed regulations should review their plan and operational processes to ensure compliance with the new rules and can contact us with any questions.

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