MEMO# 35604

January 30, 2024

IRS and DOL Guidance on Pension Linked Emergency Savings Accounts

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TO: ICI Members
Pension Committee
Pension Operations Advisory Committee SUBJECTS: Pension
Tax RE: IRS and DOL Guidance on Pension Linked Emergency Savings Accounts

IRS and DOL each recently issued guidance related to pension-linked emergency savings accounts (PLESAs).[1] PLESAs, which were created by § 127 of the SECURE 2.0 Act,[2] are optional short-term savings accounts for non-highly compensated individuals which are established and maintained as part of a defined contribution (DC) plan (including a 401(k) plan).

PLESAs Under Section 127

Effective for plan years beginning after December 31, 2023, § 127 permits employers to offer, as part of a DC plan, a PLESA to non-highly compensated employees. The employer may automatically enroll such employees into the PLESA at a deferral rate of no more than three percent of compensation, with a cap of no more than $2,500 (indexed) on the amount of the PLESA balance attributable to participant contributions. Subject to this PLESA balance limit, there is no limit on a participant's annual contributions to a PLESA other than the tax qualification contribution limits under the Internal Revenue Code (Code). Contributions to a PLESA are treated as Roth contributions, but there is no required holding period or other requirement to receive tax free distributions. Plans also must permit withdrawals from a PLESA at least once per month at a participant's discretion, with no substantiation of an emergency or other need. Contributions are treated as elective deferrals for purposes of employer matching contributions on PLESA contributions; any such employer match will be deposited into a participant's retirement plan account, with an annual cap on employer matches of the lesser of $2,500 or the plan's cap on participant balances in a PLESA (no employer contributions are permitted into a PLESA). Funds in a PLESA must be invested in cash or in a principal preservation product.

The first four withdrawals from a PLESA account each plan year may not be subject to any fees or charges solely on the basis of such withdrawals (additional withdrawals in a plan year may be subject to reasonable fees, such as fees for paper checks). In-service distributions from a PLESA are not subject to the 10 percent early distribution penalty under Code § 72(t), and may not be rolled over into another retirement account (including a Roth IRA). At separation from service employees may either take a distribution of their PLESA as cash or roll the balance into a Roth account in the same plan or to a Roth IRA. In addition to anti-abuse rules designed to discourage abuse of matching contributions (discussed in detail below), § 127 also requires certain notices and disclosures to participants, regulations to be prescribed by DOL and Treasury/IRS, and a report to Congress by these agencies.

IRS Notice 2024-22

Notice 2024-22 provides interim guidance under new Code § 402A(e)(12), which sets out anti-abuse rules designed to mitigate against abuse of matching contributions.[3] Subsection (12) provides that a plan which includes a PLESA:

(A) may employ reasonable procedures to limit the frequency or amount of matching contributions with respect to contributions to such account, solely to the extent necessary to prevent manipulation of the rules of the plan to cause matching contributions to exceed the intended amounts or frequency, and

(B) shall not be required to suspend matching contributions following any participant withdrawal of contributions, including elective deferrals and employee contributions, whether or not matched and whether or not made pursuant to an automatic contribution arrangement [for PLESA deferrals].

Notice 2024-22 provides additional color on how a plan sponsor can comply with subsection (12), specifying both statutory and procedural methods. One, the Notice highlights statutory provisions intended to limit manipulation of the PLESA rules.

- Order of matching contributions, § 402A(e)(6)(B). Section 402A(e)(6)(B) provides that, for purposes of any applicable limits on matching contributions, any matching contributions under a plan are treated first as attributable to participant elective deferrals other than PLESA contributions. The effect of this ordering is that matching contributions available based on participant PLESA contributions will be reduced.
- Limitation on annual matching contributions, § 402A(e)(6)(A). Section 402A(e)(6)(A) places two limitations on matching contributions. One, the rate of matching contributions on behalf of PLESA contributions shall be the same as the rate of any matching contributions made to a participant's account based on their elective contributions. Two, the total PLESA matching contributions for a plan year shall not exceed the participant's maximum PLESA account balance during that plan year.

A plan sponsor is not required to implement any anti-abuse provisions other than these statutory requirements. As the Notice states: "[a] plan sponsor might view these provisions as sufficient anti-abuse provisions, and therefore decide not to impose any other restrictions meant to prevent manipulation of matching contributions." The Notice further clarifies that if a participant in successive years contributes the maximum amount permitted to a PLESA, receives a match on this amount, and then takes a distribution equal to their contribution; a sponsor could consider this pattern as not manipulating the matching contribution rules. The Notice also observes that limiting PLESA withdrawals to once per month (the minimum required frequency under § 127) may be considered by a sponsor as a sufficient constraint against manipulation of PLESA matching contributions.

Notice 2024-22 also elaborates on reasonable procedures under subsection (12)(A). As a threshold matter, the Notice confirms that procedures are not required. To the extent that a plan sponsor elects to implement procedures, an anti-abuse procedure will be considered reasonable if it "balances the interests of participants in using the PLESA for its intended purpose with the interests of plan sponsors in preventing manipulation of the plan's matching contribution rules." To assist in this evaluation, the Notice highlights the following non-exhaustive list of procedures that IRS consider unreasonable.

- Forfeiture of matching contributions. A sponsor cannot provide that a withdrawal from a PLESA would result in a forfeiture of matching contributions made based on a participant's contributions to a PLESA.
- Suspension of participant contributions to a PLESA. Withdrawal from a PLESA cannot result in a suspension of a participant's ability to contribute to the PLESA.
- Suspension of matching contributions under the plan. A plan cannot suspend matching contributions attributable to participant elective deferrals to the underlying DC plan.

Finally, the Notice clarifies the IRS' position that Revenue Rulings 74-55 and 74-56 (discussing as relevant plan withdrawal provisions and the risk that they may raise the potential for manipulation of allocations in a plan) do not apply in the context of PLESAs - the Notice indicates that parties had requested this clarification.

IRS requests comments on Notice 2024-22 by April 5, 2024. Comments are specifically requested on:

- The Notice or any other aspect of § 127; and
- Additional suggested examples of reasonable anti-abuse procedures.

ICI is evaluating whether we will be submitting a comment letter. To this end, we welcome any thoughts members may have.

DOL FAQs

DOL issued the FAQs the week after Notice 2024-22 was released. The DOL FAQs provide general compliance information to assist parties in understanding the new PLESA provisions. Unlike Notice 2024-22, DOL does not request comments on the DOL FAQs, though it does provide a staff contact person for any questions. We highlight below a number of significant points in the DOL FAQs.

Participation and Contributions

ERISA § 801(c)(1)(A)(i) provides that a PLESA cannot have a minimum contribution or account balance requirement. FAQ 5 clarifies that notwithstanding this limitation, certain requirements would be considered a "not unreasonable administrative practice." A plan can require that contributions be made in whole dollars; or that percentage contributions be no less than one percent or that any contribution percentages must be in whole percentages, in each case provided that these limits are applied uniformly and that participants also can elect to make contributions in whole dollar increments. Notably, FAQ 5 also states DOL's view that § 801(c) prohibits "any policy requiring closure and distribution of a PLESA based on a minimum balance requirement."[4]

In determining the limit on participant PLESA balances, FAQ 7 provides that a plan can consider either the total balance of the PLESA (including earnings on contributions), or only the portion of the PLESA comprised of participant contributions.

FAQ 9 addresses the timing for depositing PLESA contributions into a participant's PLESA, clarifying that the same rules under 29 C.F.R. § 2510.3-102 for the timing of participant contributions to an individual account plan also apply to PLESA contributions. As such, participant contributions to a PLESA must be deposited as of the earliest date that such contributions can reasonably be segregated from the employer's general assets, but in no case later than the 15th business day of the month following the month in which the contribution is either withheld or received by the employer.

PLESA Investments

ERISA § 801(c)(1)(A)(iii) outlines the permitted investment of PLESA assets. PLESA assets may (as determined by a plan sponsor/plan fiduciary) be held as cash, in an interest-bearing deposit account, or in an investment product designed to (i) maintain the value invested over the term of investment, (ii) preserve principal and provide a reasonable rate of return (whether or not guaranteed), consistent with the PLESA's need for liquidity, and (iii) offered by a state or federally regulated financial institution.

FAQs 14 and 15 provide additional detail. One, a selected investment product satisfying the requirements of ERISA § 801(c)(1)(A)(iii) may be considered prudent regardless of the type of financial institution issuing or underwriting it, the industry such institution operates in, or the principal regulators of the product or its issuer or underwriter. Additionally, consistent with the goals for PLESA asset investment of capital preservation and liquidity, DOL clarifies that an investment product with liquidity constraints such as plan or participant level surrender charges would generally be incompatible with these objectives.

DOL expects that a plan's QDIA generally would not be an appropriate PLESA investment vehicle. If, however, a plan has designated a limited duration QDIA as provided for under the 404(c) regulations,[5] this QDIA may be designated for investment of PLESA contributions.

Reporting and Disclosure

FAQs 17 - 20 address reporting and disclosure obligations for PLESAs. SECURE 2.0 Act § 127(f)(3) specifically grants the Secretaries of Labor and Treasury authority to issue model notices for PLESAs. FAQ 17 notes that IRS and DOL "are evaluating whether, and the extent to which, a model notice is feasible and may be helpful in future guidance."

FAQ 19 confirms that, pending additional guidance, provided the disclosures required for PLESAs by ERISA § 801(d)(3)(A) and (B) are satisfied, this information does not also need to be included in pension benefit statements under ERISA § 105 or in disclosures required under 29 C.F.R. § 2550.404a-5.

Lastly, FAQ 20 discusses Form 5500 reporting requirements in connection with PLESAs. DOL states that it is working on adding a PLESA feature code to both Form 5500 and Form 5500-SF, as well as instructions that filers should aggregate and report PLESA information such as contributions, investments, fees and expenses, and distributions, in the relevant line items, including in any applicable schedules or attachments.

DOL also notes that it is evaluating whether to make additional changes to annual returns/reports to collect data DOL needs to complete the report to Congress on PLESAs mandated by ERISA § 804(1).

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Notes

[1] Notice 2024-22 (IRS Jan. 12, 2024), available at https://www.irs.gov/pub/irs-drop/n-24-22.pdf ("Notice 2024-22"); FAQs: Pension-Linked Emergency Savings Accounts (DOL Jan. 17, 2024), available at https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/faqs/pension-linked-emergency-savings-accounts ("DOL FAQs"). Treasury/IRS and DOL consulted with one another in crafting the above-refenced guidance, as required by § 127(e).

[2] For a discussion of the SECURE 2.0 Act, see ICI Memorandum No. 34795 (Jan. 12, 2023), available at https://www.ici.org/memo34795.

[3] SECURE 2.0 Act § 127(b) adds similar text to Title I of ERISA, adding a new ERISA § 801(f) (codified at 29 U.S.C. § 1193(f)).

[4] This calls into question whether, under DOL's view, a plan could force an involuntary distribution of the PLESA at termination of employment (involuntary distributions generally are available under Code § 411(a)(11) for accounts valued at $7,000 or less). Such a position would raise various administrative issues and likely would be unworkable.

[5] See 29 C.F.R. § 2550.404c-5(e)(4)(iv).