



# Congress Passes Legislation to encourage a “Secure” Retirement for Governmental Workers

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As 2022 drew to a close, Congress passed the SECURE 2.0 Act of 2022 (“SECURE 2.0”) by attaching it as Division T to the much larger and broader Consolidated Appropriations Act, 2023. The provisions of SECURE 2.0 had strong bipartisan support and built upon the initial improvements of the “original” Setting Every Community Up for Retirement Enhancement Act (“SECURE Act”) passed at the end of 2019. The goals of SECURE 2.0 largely mirror those of the earlier SECURE Act, the main one being to encourage more employees to not only enroll in employer-provided DC retirement plans, but also increase the amounts they are able to contribute to those plans. As an added bonus, SECURE 2.0 also made some beneficial law changes applicable solely to governmental 457(b) plans that will please both governmental employers and their employees alike.

## ENCOURAGE EMPLOYEES TO PARTICIPATE IN, AND CONTRIBUTE MORE TO, THEIR OWN RETIREMENT READINESS

SECURE 2.0 encourages more employees to enroll in employer-provided DC retirement plans, including governmental 457(b) plans, by offering a few different financial incentives, making it easier to access limited amounts of retirement savings while still working, and at the same time increasing both the amounts that participants may save and the time during which participants may hold on to their savings.

### Creating a Saver’s Matching Credit

There is an existing **nonrefundable credit** for certain individuals who make contributions to individual retirement accounts (“IRAs”) and employer-provided DC retirement plans (including governmental 457(b) plans). Unfortunately, the credit is confusing because the amount is an adjustable percentage based on an individual’s income and filing status; more significantly, because of the nonrefundable nature of the credit, it cannot be larger than an individual’s overall tax liability. This means that the credit can be reduced, or even go away completely, if an individual’s tax bill is low.

SECURE 2.0 replaces the current nonrefundable credit paid directly as part of a tax refund into a federal matching contribution that **must** be deposited into an individual’s IRA or DC retirement plan, as elected by that taxpayer. The new Savers Match contribution is intended to help ensure that the tax credit will be directly used to help build up an individual’s retirement savings.

This new and improved “Savers Match” credit will be a simple 50% of IRA or retirement plan contributions up to \$2,000 per individual. The percentage will no longer change depending on income or filing status. The match will phase out between \$41,000 and \$71,000 in the case of taxpayers filing a joint return, \$20,500 to \$35,500 for single taxpayers and those married filing separately, and \$30,750 to \$53,250 for head of household filers. Those amounts will be adjusted each year to reflect increases in the cost of living.

Separately from the new Savers Match credit itself, SECURE 2.0 also contains a separate provision that directs the Treasury Department to increase public awareness of the new and improved credit by promoting its use by low and moderate income

taxpayers. The promotion will make clear that the Saver's Match cannot be withdrawn without incurring penalties, including repayment to the Treasury Department in some cases where the Saver's Match is withdrawn before retirement.

Unfortunately, this new and improved Savers Match credit has a delayed effective date. It will not be available until taxable years beginning after December 31, 2026.

### **Allowing more penalty-free in-service withdrawals**

The Internal Revenue Code (the "Code") currently imposes a 10% penalty on withdrawals from DC retirement plans (including governmental 457(b) plans) before a participant's normal retirement age, including for an "unforeseeable emergency," unless an exception applies. This tax penalty has always had a negative impact on plan participation, as many individuals delay deferring into DC retirement plans until they have adequate cash reserves on hand to pay for emergency expenses. SECURE 2.0 amends the Code to provide for various potential exceptions to the 10% penalty for certain distributions. Among those new potential opportunities for penalty-free in-service withdrawals are plan distributions for the following reasons:

**Emergency expenses** – These are expenses that are unforeseeable or immediate financial needs relating to personal or family emergencies. Only one distribution of up to \$1,000 is permissible per year, and the participant has the option to repay the distribution within three years. No further emergency distributions will be permissible during the three-year repayment period unless repayment occurs.

These new emergency withdrawal provisions will be permitted to be added to governmental 457(b) plans after December 31, 2023.

**Domestic abuse** – A plan participant who self-certifies that they experienced domestic abuse may withdraw a small amount of money (the lesser of \$10,000, indexed for inflation, or 50% of the participant's account) from their DC retirement plan. Like the emergency withdrawals described immediately above, a participant will also be able to repay this withdrawn money back to the retirement plan over three years.

This new optional in-service withdrawal provision may be added to governmental 457(b) plans after December 31, 2023.

**Purchasing long-term care contracts ("LTC")** – A plan participant may take an in-service distribution of up to \$2,500 per year for the payment of premiums for certain specified LTC insurance contracts. It is important to note that to qualify for such an early distribution that is exempt from the additional tax, the individual must purchase certain policies that cover "qualified long-term care services" (as defined by the Code) or otherwise cover individuals who become "chronically ill" (as defined by the Code).

This new in-service withdrawal provision has a delayed effective date. Provisions allowing for in-service withdrawals for purposes of paying for such LTC premiums may be added to governmental 457(b) plans three years after the enactment of SECURE 2.0, December 29, 2025.

**Qualified federally declared disasters** – A plan participant who has been impacted by a federally declared disaster may take up to \$22,000 from their DC retirement plan. The amount of this type of distribution will be spread out as gross income over three years. Distributions can be repaid to any tax preferred retirement account within the same three-year period. In addition, amounts distributed prior to the federally declared disaster to purchase a home can be recontributed. Also of significance, an employer will also be permitted to provide individuals impacted by a federally declared disaster with a larger amount to be borrowed from the plan as a loan as well as additional time for repayment of plan loans.

Governmental employers are permitted to add these in-service withdrawals and more generous loan provisions to their plan in connection with any qualified federally declared disaster occurring on or after January 26, 2021.

### **Allowing separate emergency savings accounts linked to DC retirement plans**

SECURE 2.0 added multiple new provisions to provide all employers, including governmental employers, the option to offer their non-highly compensated employees emergency savings accounts that are directly linked to their DC retirement plan. Employers may even automatically opt employees into these accounts at no more than 3% of their salary. The portion of the separate emergency savings account attributable to the employee's contribution is capped at \$2,500 (or lower as set by the employer).

Contributions to the emergency savings account will be made on an after-tax basis and contributions made directly to the employee's DC retirement plan after reaching the cap will be directed to the employee's Roth subaccount (if they have one), or stopped until the balance attributable to the employee's contributions falls below the cap. The contributions into the emergency savings account will also be treated as elective deferrals for purposes of retirement plan matching contributions - with an annual matching cap attributable to the emergency savings contributions set at the maximum account balance – i.e., \$2,500 or lower as set by the employer.

Plan participants may take up to four withdrawals from the emergency savings account each plan year without being subject to any fees or charges solely on the basis of such withdrawals. When plan participants separate from service, they may take their emergency savings accounts as cash or roll it into the Roth subaccount of another DC retirement plan or Roth IRA.

Governmental employers may link these new, separate emergency savings accounts to their 457(b) plans in any plan year beginning after December 31, 2023.

### **Treating student loan payments as elective deferrals for purposes of matching contributions**

Although there are currently no provisions in the Code that allow an employer to make matching contributions based on a participant's repayment of student loan debt, at least one private sector employer has received a private letter ruling from the IRS that authorizes this practice.

SECURE 2.0 makes changes to the Code to expressly permit an employer to make matching contributions under a DC retirement plan with respect to “qualified student loan payments.” A qualified student loan payment is broadly defined as any indebtedness incurred by the employee solely to pay qualified higher education expenses of the employee.

Matching contributions attributable to qualified student loan payments may be made to governmental 457(b) plans that choose to adopt such matching provisions for plan years beginning after December 31, 2023.

### **Increasing age for Required Minimum Distributions (“RMDs”)**

The original SECURE Act increased the age at which participants are generally required to begin taking distributions from their retirement plans from age 70½ to age 72.

SECURE 2.0 gradually increases the age at which RMDs must begin even further over the next decade. The applicable RMD age will be 73 for someone who attains age 72 after December 31, 2022, and age 73 before January 1, 2033. For someone who attains age 74 after December 31, 2032, the applicable RMD age is 75.

### **Increasing the catch-up limit at ages 60 - 63**

The limit on catch-up contributions for 2023 will be \$7,500. SECURE 2.0 significantly increases this limit for those individuals who have reached age 60, 61, 62, and 63 by the end of the taxable year. The new maximum contribution limit for individuals in this 4-year age window will be 50% more than the regular catch-up contribution maximum effective in 2025 and will be indexed for inflation thereafter. For other changes related to catch-up contributions from SECURE 2.0, please read about the “Rothification of catch-up contributions” in the next section of this white paper.

The new increased catch-up contribution limits for those at ages 60-63 will be permitted in taxable years beginning after December 31, 2024.

### **Expanding and changing Roth-related provisions**

SECURE 2.0 contains numerous different provisions that change how DC retirement plans (including governmental 457(b) plans) treat Roth contributions and Roth subaccounts within those plans. Roth contributions are deposited into DC retirement plans on an after-tax basis and the earnings on those Roth contributions will not be subject to tax upon distribution in retirement so long as certain requirements are met. Roth contributions are popular because they provide individuals an additional source of tax-free funds from which to draw at any time in retirement.

**Rothification of catch-up contributions** – SECURE 2.0 will for the first time require all catch-up contributions made by employees who are at least 50 or older be subject to Roth tax treatment. However, an exception for that required Roth treatment will be made for those employees with annual compensation in the previous plan year of \$145,000 or less (as indexed for inflation). The required Roth tax treatment will apply to catch-up contributions beginning in taxable years beginning after December 31, 2023.

**Optional rothification of employer matching or nonelective contributions** – SECURE 2.0 will for the first time permit DC retirement plans to provide participants the option of receiving employer matching or nonelective contributions on a Roth basis. This new Roth treatment will be permitted immediately in those plans that choose to implement these new provisions.

**Removal of RMDs rules on Roth sub-accounts** – Although RMDs are not required to begin before the death of a Roth IRA owner, pre-death RMDs are currently required for participants who hold amounts in a Roth subaccount within a DC retirement plan. This makes the RMD rules apply more favorable to Roth IRAs versus Roth amounts in retirement plans.

SECURE 2.0 makes changes to the Code so that Roth subaccounts in DC retirement plans will be treated just as a Roth IRA. In other words, it eliminates the pre-death distribution requirement for Roth subaccounts within retirement plans. This will effectively shield Roth amounts in DC retirement plans from application of the RMD rules, which will increase the amount of time those Roth amounts within the retirement plan may grow tax free.

This change to the RMD rules applicable to Roth subaccounts within DC retirement plans (including governmental 457(b) plans) will begin in taxable years beginning after December 31, 2023. However, note that this change does not apply to distributions that are required with respect to years beginning before January 1, 2024, but are permitted to be paid on or after such date.

## **CHANGES APPLICABLE SOLELY TO GOVERNMENTAL 457(B) PLANS**

### **Removing the “first day of the month” rule**

Currently, participants in governmental 457(b) plans must request changes to their deferral rate before the beginning of the month in which the deferral of their compensation will be made to the plan. This rule is unique to governmental 457(b) plans and does not apply to other employer-provided DC retirement plans in the private sector. SECURE 2.0 removes this rule so that participants in governmental 457(b) plans will be allowed to make changes to their retirement plan deferral elections just like participants in a 401(k) or 403(b) plan. This means that they will be able to elect to start, stop, or change their deferral rate at any time, and such election will be effective as soon as the next payroll date after the participant’s election is implemented by the plan’s administrator. The removal of this outdated rule and the coalesce of the procedure for all DC retirement plan participants to make changes to their deferral elections will be effective for taxable years beginning on or after January 1, 2023.

### **Extending penalty-free in-service withdrawal to state and local corrections officers**

Unlike the four other opportunities to take penalty-free in-service withdrawals described earlier in this white paper, which will generally become available for all DC retirement plans, this particular change impacts solely governmental 457(b) plans.

Currently, governmental 457(b) plans may provide for “public safety employees” who are at least age 50 to take in-service withdrawals; however, the definition of “public safety employee” is limited to police officers, fire fighters, or other emergency medical personnel who work for state and local governments, as well as certain federal public safety employees.

As applied to those public safety employees who work for state and local governments, SECURE 2.0 extends the definition of “public safety employees” to include corrections officers and forensic security employees. This means that these two classifications of employees who work for state and local governments will now also be able to take a penalty-free in-service withdrawal upon reaching age 50, if the governmental 457(b) plan in which they participate allows such a withdrawal. This additional opportunity may be extended to such state and local corrections officers immediately.

## IN SUMMARY

The legal changes and additions described above are the most significant ones for which all DC retirement plan participants, and governmental 457(b) retirement plans, should be aware. However, this white paper summarizes just a portion of the very large SECURE 2.0. For a more comprehensive summary of SECURE 2.0 and to find related educational materials specifically for governmental 457(b) plans, please access the [Nationwide Retirement Solutions SECURE 2.0 hub](#).



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