NOVA 401(k) ASSOCIATES

October 30, 2020

Mr. Eric Slack
Director, Employee Plans
Internal Revenue Service
999 North Capitol Street NE
Washington, DC 20002

Re: IRS Notice 2020-68

Dear Mr. Slack:

Nova 401(k) Associates and our affiliate, Administrative Fiduciary Services Inc. (collectively "NOVA"), are writing to provide comments with respect to IRS Notice 2020-68 (the "Notice"). Nova is a third-party administrator serving over 6,500 employers. Our current practice also includes multiple employer plans ('MEPs'). Nova's primary focus is on employers with fewer than 2,000 employees. Our affiliate, Administrative Fiduciary Services Inc. ('AFS') serves as an independent administrative fiduciary and provides administrative fiduciary services and support.

Recommendations

Nova recommends the Internal Revenue Service ("IRS") clarify that the reasoning of Part II, Section A, Q&A A-3 of the Notice is also applicable to the start-up credit of IRC § 45E such that the credit would be available to an employer joining a MEP in the same way that the credit would be available if each employer participating in the MEP were the sponsor of a single-employer plan.

Nova recommends the IRS provide a reasonable fresh start date of January 1, 2016, for recognizing service of a long-term part-time ("LTPT") employee for purposes of vesting.

Nova recommends the IRS clarify that the rules relating to LTPT employees do not apply to a plan whose eligibility conditions provide for participation at a time earlier than would be required under IRC § 401(k)(2)(D)(ii).

Nova recommends the IRS clarify that a non-service or age-related condition of participation may be applied to exclude LTPT employees who fall within the excluded class.

Nova recommends the IRS allow an employer to choose whether, and to what extent, to treat distributions under its plans as qualified birth adoption distributions in the same manner as is permitted or coronavirus distributions by Section 2., C of IRS Notice 2020-50.

Nova recommends the IRS update the guidance provided in IRS Notice 2020-50 Section 3, to clarify whether the recontribution requirements set forth in Part II, Section D, Q&A D-13 with respect to qualified birth/adoption distributions would apply to corona-virus-related distributions.

Discussion

On December 20, 2019, the Setting Every Community Up for Retirement Enhancement Act of 2019 ("SECURE Act") was signed into law by President Trump. Many of the SECURE Act's provisions became effective in 2020. Others, such as those pertaining to LTPT employees and pooled employer MEPs, become effective in 2021. It should be noted, however, the provisions regarding the crediting of vesting service of LTPT employees will be retroactively effective when they are first applied in 2021. As a result of these immediate effective dates, there is an urgent need for guidance.

Tax Credits under IRC §§ 45T and 45E

The SECURE Act added new IRC § 45T to make available a business tax credit for certain eligible employers who maintain an eligible automatic contribution arrangement ("EACA"). The Secure Act also substantially increased the startup business tax credit available under IRC § 45E to certain eligible employers who adopt a new plan. To qualify for the startup tax credit, the eligible employer is not permitted to have had a qualified plan for the 3-taxable year period immediately preceding the first taxable year for which the credit is taken.[1]

In the Notice, the IRS provided guidance on how an employer joining a MEP would be treated for purposes of the new credit under IRC § 45T. The Notice provides:

> The IRC § 45T credit applies to an eligible employer that participates in a MEP in the same way that the credit would apply if each employer participating in the MEP were the sponsor of a single-employer plan maintained by the eligible employer.[2]

Nova believes this guidance would be equally applicable in the context of an eligible employer joining a MEP. As such, the employees of any unrelated employer participating in the MEP would not be attributed to any other employer participating in the MEP. Additionally, the adoption of the MEP as a new plan by an eligible employer would qualify as the adoption of a new plan (assuming the employer had not sponsored a qualified plan during the 3-taxable year look back period. In other words, the eligible employer will not be precluded from qualifying for the credit because the MEP had been in existence during the 3-taxable year look back period.

Nova recommends that the Internal Revenue Service ("IRS") clarify that the reasoning of Part II, Section A, Q&A A-3 of the Notice is also applicable to the start-up credit of IRC § 45E such that the credit would be available to an employer joining a MEP in the same way that the credit would be available if each employer participating in the MEP were the sponsor of a single-employer plan.

Long-Term Part-Time Employees Vesting Credit

[1] IRC § 45E(c)(2).
[2] IRS Notice 2020-68, Section A, Q&A 3.

The SECURE Act amended IRC §401(k)(2)(D) to provide that a cash or deferred arrangement ("CODA") may not require as a condition of participation that an employee complete a period of service that extends beyond the earlier of: (i) the period permitted under IRC § 410(a)(1) (disregarding §410(a)(1)(B)(i)); or (ii) subject to IRC §401(k)(15), the first period of three consecutive 12-month periods during which the employee has completed at least 500 hours of service. The SECURE Act provides that for purposes of crediting eligibility service, 12-month periods beginning before January 1, 2021, shall not be considered.[3]

The SECURE Act also provides special rules for crediting vesting service for employees who are eligible to participate in a CODA solely by the reason of being a LTPT employee. IRC § 401(k)(15)(B)(iii) provides that these employees shall be credited with a year of vesting service for each 12-month period in which the employee had at least 500 hours of service. Unlike eligibility service, there is no specific exclusion for service rendered before the effective date, January 1, 2021.

The failure of the SECURE Act to specifically exclude service before January 1, 2021, for purposes of vesting credit will, for many plan sponsors and plan administrators, cause difficult, if not impossible, compliance challenges. This is due to the retroactive effect of this change in the law. It is unreasonable to expect employers to have detailed time records sufficient to comply with the law going back many, many years. The 1000-hour standard has been in effect since the passage of ERISA. Many employers will have great difficulty recreating records that were not shared with their recordkeeper and may not be maintained by their current payroll provider. For this reason, the IRS should provide for a reasonable fresh start date. Nova believes January 1, 2016 would be a reasonable compromise.

Nova recommends that the IRS provide a reasonable fresh start date of January 1, 2016, for recognizing service of a long-term part-time ("LTPT") employee for purposes of vesting.

Long-Term Part-Time Employees – Immediate Eligibility

The SECURE Act provides several special rules for employees in a CODA solely by the reason of being a LTPT employee. For example, the special vesting rules discussed above are only applicable to these employees. This has raised questions as to whether the special rules for LTPT employees would ever apply in a plan that has more liberal eligibility requirements that would allow for participation earlier than the completion of 3 consecutive 12-month computation periods during which the employee completed 500 hours of service.

For example, many 401(k) plans allow for immediate participation with monthly entry dates. Another common practice is to require completion of 6 months of service without regard to hours worked. In either case, part-time employees will be eligible to participate long before qualifying as a LTPT employee. As a result, there are no employees participating in the CODA solely by reason of being classified as a LTPT employee and LTPT rules should have no application. Guidance should clarify and confirm this analysis.

[3] PL 116-94, Division O, Section 112(b).

Nova recommends that the IRS clarify that the rules relating to LTPT employees to do not apply to a plan whose eligibility conditions provide for participation at a time earlier than would be required under IRC § 401(k)(D)(ii).

Long-Term Part-time Employees - Non-Service-Related Conditions of Participation

IRC § 410(a)(1) generally prohibits plans from requiring completion of more than a year of service as a condition of participation. A special rule allows some plans to require completion of 2 years of service provided accrued benefits are always fully vested.[4] IRC § 401(k)(2)(D) prohibits the use of the 2-year rule for a CODA. Additionally, the SECURE Act amended IRC § 401(k)(2)(D) to require participation upon the earlier of: completion of a traditional year of service; or the completion of 3 consecutive 12-month periods during which the employee was credited with at least 500 hours of service.

The regulations under IRC § 410(a) very specifically permit a plan sponsor to place conditions on participation that are not age or service related:

> Section 410(a), §1.410(a)-(4), and this section relate solely to age and service conditions and do not preclude a plan from establishing conditions, other than conditions relating to age or service, which must be satisfied by plan participants. For example, such provisions would not preclude a qualified plan from requiring, as a condition of participation, that an employee be employed within a specified job classification.[5]

NOVA strongly believes that nothing in the amendments made by the SECURE Act would preclude the use of non-service-related conditions of participation. Obviously, any such condition could not have the effect of imposing an age or service requirement.[6] An employer who, for valid business reasons, excludes a class of employees from plan participation should not be forced to enroll LTPT employees who would not otherwise be eligible. If Congress intended any different result it would have provided for such in the SECURE Act.

Nova recommends that the IRS clarify that a non-service or age-related conditions of participation may be applied to exclude LTPT employees who fall with the excluded class.

Qualified Birth/Adoption Distributions

The SECURE Act amended IRC § 72(t)(2) to provide a new exception from the 10% additional tax on an early distribution from a qualified plan for qualified birth/adoption distributions. A qualified birth/adoption distribution is defined as any distribution from an applicable eligible retirement plan made during the 1-year period beginning on the date on which the child of the individual is born or the legal adoption is finalized.[7] Qualified birth/adoption distributions are not treated as eligible rollover distributions for purposes of IRC §§ 401(a)(31), 402(f), and 3405.[8]

[4] IRC § 410(a)(1)(B).
[5] Treas. Reg. §1.410(a)-3(d).
[6] Treas. Reg. §1.410(a)-3(e).
[7] IRC § 72(t)(2)(H)(iii).
[8] IRC § 72(t)(2)(H)(vi).

The Notice addresses the treatment of a qualified birth/adoption distribution regarding rollovers, the IRC § 402(f) notice, and income tax withholding as follows:

> Q. D-15: Is a qualified birth or adoption distribution treated by an applicable eligible retirement plan as an eligible rollover distribution for purposes of the direct rollover rules, § 402(f) notice requirements, and the mandatory withholding rules?
> A. D-15: No. A qualified birth or adoption distribution is not treated as an eligible rollover distribution for purposes of the direct rollover rules of § 401(a)(31), the notice requirement under § 402(f), and the mandatory withholding rules under § 3405. Thus, the plan is not required to offer an individual a direct rollover with respect to a qualified birth or adoption distribution. In addition, the plan administrator is not required to provide a § 402(f) notice. Finally, the plan administrator or payor of the qualified birth or adoption distribution is not required to withhold an amount equal to 20% of the distribution, as generally is required in § 3405(c)(1). However, a qualified birth or adoption distribution is subject to the voluntary withholding requirements of § 3405(b) and § 35.3405-1T. [9]

The wording in Q&A 15 is very similar to the wording in Notice 2020-50 with respect to coronavirus-related distributions.[10] This makes perfect sense because a coronavirus-related distribution is subject to the same rollover, IRC § 402(f) notice, and withholding obligations as a qualified/birth adoption distribution. However, Notice 2020-50 goes on to permit an employer to choose whether a distribution will be treated as coronavirus-related distribution with the caveat that the plan must be consistent if it permits coronavirus related distributions from accounts restricted under IRC §§401(k)(2)(B)(i), 403(b)(7)(A)(i), 403(b)(7), 403(b)(11) or 457(d)(1)(A).[11] This option for coronavirus-related distributions was not provided for qualified birth/adoption distributions. Nova believes it imperative that the IRS provide employers and plans with this same flexibility in dealing with qualified birth/adoption distributions for the same policy reasons as are applicable to coronavirus-related distributions.

The problem with both coronavirus-related distributions and qualified birth/adoption distributions is that in many cases, the plan will not know whether a distribution is a qualified distribution if it does not otherwise permit coronavirus-related or qualified birth/adoption distributions. An individual may have terminated service in years past and in 2020 requests and receives a cash-out distribution. If that individual had a child born or legally adopted within 1 year of the distribution date, up to $5,000 of the distribution would qualify as a birth/adoption distribution. The plan would have no way of knowing that it qualified and therefore no way of applying the voluntary withholding rules for up to $5,000 of the distribution.

A similar problem exists for corona-virus related distributions. An individual who terminated service in years past may request a cash-out distribution on or before December 30, 2020. If the individual is a qualified individual, the distribution will qualify without the employer necessarily knowing. Notice 2020-50 addressed this problem by permitting employers to choose, whether, and to what extent, to treat

[9] Notice 2020-68, Sec. D, Q&A D-15
[10] Notice 2020-50, Sec. 2, B.
[11] Notice 2020-50, Sec. 2, C.

distributions under its plans as coronavirus-related distributions.[12] Notice 2020-50 makes it clear that a plan that permits in-service distribution of restricted amounts would need to be consistent in the treatment of similar distributions. That is a very fair requirement in that in such circumstances, the plan will have actual knowledge that the distribution qualifies. Nova believes the policy reasons behind this approach to coronavirus- related distributions is equally applicable to qualified/birth adoption distributions.[13]

Nova recommends that the IRS allow an employer to choose whether, and to what extent, to treat distributions under its plans as qualified birth adoption distributions in the same as is permitted for coronavirus distributions by Section 2, C of IRS Notice 2020-50.

Recontribution of Qualified Birth/ Adoption Distributions and Corona Virus-Related Distributions

The Notice addresses the circumstances under which a plan is required to accept a recontribution from an individual of a qualified birth/adoption distribution. Part II, Section D, Q&A D-13 of the Notice provides:

> An applicable eligible retirement plan must accept the recontribution of a qualified birth or adoption distribution from an individual if the following apply: (a) the plan permits qualified birth or adoption distributions; (b) the individual received a qualified birth or adoption distribution from that plan; and (c) the individual is eligible to make a rollover contribution to that plan at the time the individual wishes to recontribute the qualified birth or adoption distribution to the plan.

It would appear that similar rules should apply with respect to a recontribution of a corona virus-related distribution. The wording in IRC § 72(t)(2)(H)(v)(I) regarding qualified birth/adoption distributions is virtually identical to that found in Section 2202(a)(3)(A) of the Coronavirus Aid, Relief, and Economic Security Act of 2020 ("CARES Act"). However, the guidance provided in Section 3, B of Notice 2020-50 does not track the wording in Notice 2020-68. It reads as follows:

> In general, it is anticipated that eligible retirement plans will accept recontributions of coronavirus-related distributions, which are to be treated as rollover contributions. However, eligible retirement plans generally are not required to accept rollover contributions. For example, if a plan does not accept any rollover contributions, the plan is not required to change its terms or procedures to accept recontributions of coronavirus-related distributions.

As a result of the wording in IRS Notice 2020-50, many practitioners concluded that a plan is never required to accept a recontribution of a corona virus-related distribution. In light of the Notice, many are now questioning whether the wording in IRS Notice 2020-50 was intended to be more narrowly construed. Specifically, whether the requirements found in Part II, Section D, Q&A D-13 of the Notice are

[12] *Id*.

[13] For similar reasons, the same treatment has been provided for disaster related distributions. See Notice 2005-92, Sec. 2, C.

applied in a similar fashion for corona virus-related distributions. If the IRS so intends, Nova believes the IRS should clearly say so in clarifying guidance.

Nova recommends the IRS update the guidance provided in IRS Notice 2020-50 Section 3, B to clarify whether the recontribution requirements set forth in Part II, Section D, Q&A D-13 of the Notice with respect to qualified birth/adoption distributions would apply to corona-virus-related distributions.

Conclusion

Nova very much appreciates the work done by the IRS and Treasury Department to provide much needed guidance on the SECURE Act. We urge you to move forward as quickly as possible with more comprehensive guidance. We look forward to working with on this and other regulatory initiatives related to SECURE. The primary contributors to this letter were Steve Vest, Charlene DeMartini, Sue Harper, Joseph Redd, and Craig P. Hoffman. Should you have any questions, please feel free to contact Craig Hoffman at choffman@nova401k.com.

Sincerely,

/s/_____
Karen N. Smith
President