

Guidance on Pension 'Linked' Emergency Savings Accounts

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Take-Away: Starting this year a qualified elective deferral retirement plan may have 'linked' to it an emergency savings account that has a balance up to \$2,500. Employer matching contributions can also be made to this savings account, but the IRS is concerned about employee-participants manipulating the savings account opportunity solely to obtain an employer's matching contribution.

Background: The SECURE Act 2.0 introduced for sponsors of 401(k), 403(b) and 457(b) [governmental] defined contribution retirement plans the option to incorporate a 'pension-linked-emergency savings account' feature. In Notice 2024-22 the IRS provides preliminary guidance regarding the anti-abuse rules that are applicable to this new qualified plan feature.

In IRS News Release IR-2024-11, the IRS provided a short summary of its reasons for Notice 2024-11: *“Guidance on reasonable measures employers who offer Pension-Linked Emergency Savings Accounts [PLESA] can take to discourage potential manipulation of the PLESA matching contribution rules can be found in Notice 2024-22, posted today on IRS.gov. The notice also requests public comment and explains how to submit comments.”*

PLESAs: A Pension-Linked Emergency Savings Account [PLESA] is an individual account as a part of a defined contribution plan that is designed to permit and encourage employees to save for financial emergencies. Key provisions for a PLESA include:

Plans Start in 2024: A PLESA can be offered for a plan year that begins after December 31, 2023.

Employer-Sponsor's Option: The addition of this option to a 'linked' qualified plan is at the employer-sponsor's discretion. It is not required or

mandatory that such a PLESA provision be added to an existing 401(k), 403(b), or 457(b) deferred compensation plan.

Matching Employer Contributions: Subject to certain restrictions, employer matching contributions are made with respect to PLESA contributions at the same rate as its contributions are to the ‘linked’ qualified defined contribution plan. Employees who are eligible to participate in their employer’s defined contribution plan and who qualify to contribute to a PLESA, if their employer offers such a savings plan, may contribute to the PLESA even if they do not participate in their employer’s defined contribution plan.

Maximum Amount: As a generalization, the maximum balance in a participant’s PLESA, attributable to contributions, is \$2,500. However, the employer can choose to set a lower limit on the PLESA balance.

Designated as Roth Account: PLESAs are treated as designated Roth accounts. Accordingly, contributions to a PLESA are not tax deductible by the plan participant, but withdrawals from the PLESA will generally be tax-free.

Withdrawal Rates: A participant who funds a PLESA can withdraw amounts held in the PLESA at least once a month, as necessary.

Abuse Concerns: The IRS’s Notice addresses specific concerns if a defined contribution plan is ‘linked’ to the PLESA option. Specifically, the SECURE Act 2.0 acknowledges concerns that sponsors may have employees who potentially use PLESA contributions merely to gain matching employer contributions without intending to retain the funds in the plan for future emergencies. Apparently, the concern is that employees may plan to make contributions with the intention of promptly requesting an ‘emergency’ withdrawal from the account, whether an unexpected financial crisis arises. As the Notice states:

Section 402A(e)(12)(A) provides that a plan of which a PLESA is a part 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. Section 402A(e)(12)(B) provides that a plan of which a PLESA is a part is not required to suspend matching contributions following any participant withdrawal of contributions, including elective deferrals and employee contributions, whether matched and whether or not made pursuant to an automatic contribution arrangement.”

Anti-Abuse Provisions: Statutory provisions under IRC 402A(e) that limit an employee’s manipulation of the defined contribution plan rules to cause matching employer contributions to exceed the intended maximum amounts or frequency, include:

Order of Matching Contributions: Any matching contributions made under the plan are treated first as attributable to a participant’s elective deferrals other than PLESA contributions. Therefore, any elective deferrals a participant makes under the underlying qualified plan will be matched first and will thus lower the availability of matching contributions that will be made on account of the participant’s contributions to his/her PLESA.[IRC 402A(e)(6)(B).]

Limitations on Annual Matching Contributions: Matching employer contributions on account of employee contributions to a PLESA cannot exceed the maximum account balance of \$2,500, which will be adjusted annually, or to a lower amount if that lower amount is set by the plan sponsor for the plan year. [IRC 402A(e)(3)(A)(i.)] Thus, a lower limit on the portion of the PLESA balance attributable to participant contributions would result in a correspondingly lower cap on annual employer matching contributions that would be required under IRC 402A(e)(6)(A.)

Rules that Mitigate Risk: The Notice goes on to state that a sponsor may regard these two anti-abuse rules as sufficient to mitigate the risk of employees manipulating the PLESA rules to obtain matching employer contributions. *“A plan sponsor might view these provisions as sufficient anti-abuse provisions, and therefore decide to not impose any other restrictions meant to prevent manipulation of matching contributions. In such a case, for example, a plan sponsor may consider a participant as not manipulating the matching contribution rules if the participant made a \$2,500 contribution in one year, received the matching contribution on such amount, and then took \$2,500 in distributions that year and repeated that pattern in subsequent years.”*

Unreasonable Anti-Abuse Rules: The Notice also identified some procedures that it deems to be unreasonable for a plan sponsor to impose on a PLESA, but it is not an exhaustive list. Those IRS examples of unreasonable anti-abuse rules include: (i) a plan may not provide that matching contributions already made on account of participant contributions to the PLESA will be forfeited by reason of a participant's withdrawal from a PLESA; (ii) a plan may not suspend a participant's ability to contribute to the participant's PLESA on account of a withdrawal from the PLESA; and (iii) a plan may not suspend matching contributions made on account of participant elective deferrals to the underlying 'linked' defined contribution plan.

Conclusion: It will be interesting to see just how many defined contribution plan sponsors take steps to amend their qualified plans to include matching contributions to a PLESA. It will also be interesting to see the proposed comments that the IRS will receive during this year as it attempts to create implementing Regulations for pension 'linked' emergency savings accounts while addressing what it perceives to be potential abuses if an employer chooses to make matching contributions to the savings plans. Expect to hear a lot more about this new SECURE Act 2.0 saving opportunity throughout 2024.