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How the Earn Act Might Affect Employers

The U.S. House of Representatives passed the Setting Every Community Up for Retirement Enhancement (SECURE) Act, known informally as "SECURE 2.0," in March 2022. The Senate's counterpart consists of two bills, the Retirement Improvement and Savings Enhancement to Supplement Healthy Investments for the Nest Egg (RISE & SHINE) Act and the Enhancing American Retirement Now (EARN) Act. The Senate Health, Education, Labor and Pensions panel advanced the RISE & SHINE Act on June 21, 2022. The Senate Finance Committee advanced the EARN Act two days later. The next step is for the full Senate to consider the bills, although it is not clear when that will happen. The EARN Act builds on the SECURE Act in several important ways that could affect employers. The following offers an overview of a few of the EARN Act's provisions.

Expanded or modified contribution limits

The EARN Act makes several changes to employer-matching contributions to various retirement plans.

Roth Contributions

Roth contributions take place on an "after-tax" basis, meaning that employees can contribute money on which they have already paid federal income tax. In contrast, pretax contributions occur before employers withhold federal income tax, and the employee pays tax when they withdraw the money years later.

Current law only allows pretax employer-matching contributions to 401(k) and 403(b) plans. The EARN Act would allow employees to choose to have employers match their contributions on a Roth after-tax basis instead. The SECURE Act contains similar provisions. Starting in 2024, employees would also be able to choose Roth treatment of contributions to SIMPLE and SEP plans.

SIMPLE Contributions

The EARN Act would increase certain contribution limits for SIMPLE IRAs and SIMPLE 401(k) plans. Right now, the limit for employee elective deferral contributions to either type of plan is $14,000 per year. SIMPLE IRAs are only available for employees of small employers whose matching contributions are either:

- 3% of employee compensation deferred; or
- 2% of compensation.

Under the EARN Act, the annual contribution limit for both types of plans for employers with up to 25 employees would be $16,500 (indexed) beginning in 2024. The catch-up contribution for those employers would be $4,750 per year (indexed). The same limits would be available to employees with at least 26 but no more than 100 employees if they provide either:

- 4% matching contribution; or
- 3% contribution.

Student loan payments as elective deferrals

The EARN Act would expand employers' ability to make matching contributions to 401(k) plans, 403(b) plans and SIMPLE IRAs. Currently, employees can designate an amount to be withheld from their paychecks and contributed to a retirement plan, known as an elective-deferral contribution. Employers can match those amounts up to a certain point.

Under current law, therefore, if an employee chose to have $100 deducted from each paycheck as an elective-deferral contribution, the employer could match that amount. The EARN Act would allow employees to treat certain student loan payments as elective-deferral contributions. In addition to matching a $100 deduction from the employee's paycheck, the employer could match a $100 student loan payment.

Automatic enrollment safe harbor for 401(k) plans

Employers can automatically deduct elective deferrals from the paychecks of eligible employees for certain retirement plans, such as 401(k)s or SIMPLE IRAs, unless an employee chooses to contribute to a different plan or not to contribute at all.

Employers must comply with nondiscrimination rules in various circumstances. These rules state that a plan's contributions or benefits may not discriminate against employees on the basis of the amount of compensation they receive. "Safe harbor" provisions are available that exempt plans from annual nondiscrimination compliance tests.

The EARN Act would establish a new safe harbor test for 401(k) plans that use automatic enrollment starting in 2024. It would also provide a tax credit for employers with no more than 100 employees who use this automatic-enrollment safe harbor plan. The credit would be in the amount of the employer's matching contributions up to a maximum of 2% of an employee's annual compensation.