KLAUSNER KAUFMAN JENSEN & LEVINSON

M E M O R A N D U M

TO: Board of Trustees

FROM: Klausner, Kaufman, Jensen & Levinson

RE: Required Minimum Distributions (RMD) Proposed Regulations & Cryptocurrencies Guidance

DATE: April 2022

Executive Summary

On February 24, 2022, the Internal Revenue Service (IRS) proposed regulations revising the required minimum distribution (RMDs) regulations to align with the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act), as well providing additional guidance. The proposed guidelines raised the age for which retirees are required to start minimum distributions from age 70½ to 72, clarified the definition of "eligible designated beneficiaries," further defined the meaning of "disability" and "chronically ill," and clarified the timing of distributing RMDs. We do want to note that on March 29, 2022, the House passed the Securing a Strong Retirement Act of 2022 (SECURE 2.0), which includes additional changes to RMDs. We will keep you updated as SECURE 2.0 moves through Congress, but thought it was prudent for you to have the most up-to-date regulations as they stand now.

Additionally, on March 10, 2022, the U.S. Department of Labor (DOL) published a compliance assistance release concerning 401(k) plans investing in cryptocurrencies. DOL expressed serious concerns about plans investing in cryptocurrencies and related products due to the significant risks of fraud, theft, and loss because of their speculative nature, custodial, recordkeeping, and valuation concerns, as well as the evolving regulatory market. While DOL regulations do not apply to public plans, Section 112.661, Florida Statutes, applies the ERISA standard of care to investment decision making. Furthermore, for plans with a member-directed component (such as share plans and DROP plans) providing cryptocurrency investment options could give rise to liability.

Below please find additional details on the IRS's proposed regulations, and the DOL's release regarding investments in cryptocurrencies.

Required Minimum Distributions

The proposed regulations incorporate changes made by the SECURE Act, including:

- Raising the age for which retirees are required to start minimum distributions from age 70½ to 72. The regulations use a birthdate rule to determine an individual's required beginning date. If the participant's birthday is prior to July 1, 1949, the required beginning date remains April 1 of the calendar year following the later in which the participant attains age 70½ and the calendar year in which the participant retires from employment. If a participant's birthdate is on or after July 1, 1949, the required beginning date is April 1 of the calendar year following the later of the calendar year in which the employee attains age 72 and the calendar year in which the participant retires.

- Clarifying the definition of "eligible designated beneficiaries." Under the SECURE Act, eligible designated beneficiaries included: a participant's surviving spouse, a participant's minor child, a beneficiary who is disabled or chronically ill, and a beneficiary who is not more than 10 years younger than the participant. Under the proposed regulations, a child reaches the age of majority upon reaching age 21. However, the proposed regulations permit defined benefit plans that have used the prior definition of age of majority to retain that plan provision.

    - Additionally, the regulations further define "disability" and "chronically ill," and include substantial documentation requirements in order to be considered "disabled" or "chronically ill."

        - For those over age 18, the standard of disability is based on whether an individual is unable to engage in substantial gainful activity. If under age 18, the beneficiary is required to have a medically determinable physical or mental impairment that results in marked and severe functional limitations, and that can be expected to result in death or to be of long-continued and indefinite duration. The determination of whether the beneficiary is disabled is made at the time of the participant's death.

- Clarifying that for defined contribution plans if the plan participant dies before their required beginning date, the timing of the required minimum distributions depends on the classification of the beneficiary:

  - An “eligible designated beneficiary,” is permitted to be paid over the lifetime of the beneficiary or receive all the participant’s distributions within 10 years of the participant’s death. However, if the “eligible designated beneficiary” dies before the participant’s distributions are fully paid, anything remaining must be distributed to the beneficiary of the “eligible designated beneficiary” within 10 years after their death.

  - A “designated beneficiary” must receive all the distributions within 10 years of the participant’s death.

  - If there is no designated beneficiary, the distributions must be paid out within 5 years of the participant’s death.

- Clarifying that for defined contribution plans, if the plan participant dies after their required beginning date, the beneficiary’s benefit must be calculated based on the beneficiary’s life expectancy. Certain circumstances, however, require full distribution as provided below:

  - If the participant’s beneficiary is not an “eligible designated beneficiary,” the participant’s benefit must be paid out by the end of the tenth calendar year following the calendar year in which the participant died.

  - If the participant’s beneficiary is an “eligible designated beneficiary” and dies, the beneficiary of the “eligible designated beneficiary” must be paid out by the end of the tenth calendar year following the calendar year in which the “eligible designated beneficiary” died.

  - If the participant’s “eligible designated beneficiary” is a minor child, the participant’s benefit must be paid out by the end of the tenth calendar year following the calendar year in which the minor reaches the age of majority.

  - If the participant’s “eligible designated beneficiary” was older than the participant, the participant’s benefit must be paid out by the end of the calendar year when the beneficiary’s remaining life expectancy is less than or equal to one.

Additionally, the proposed regulations impact rollovers of required minimum distributions.

U.S. Department of Labor Release on Plan Investments in Cryptocurrencies

DOL advised plan fiduciaries “to exercise extreme caution” before including a cryptocurrency option or other products whose value is tied to cryptocurrencies as a 401(k) plan’s investment option for plan participants.

The DOL expressed serious concerns regarding the prudence of fiduciaries exposing 401(k) plan members to investments in these products due to: significant risks of fraud, theft, and loss. DOL based these warnings on:

- the speculative and extreme price volatility of cryptocurrency investments;
- the degree of difficulty for plan members to evaluate these assets due to the lack of sufficient knowledge of these products, compared to traditional investments;
- custodial and recordkeeping issues that can be susceptible to hackers;
- the difficulty in accurately and reliably valuating cryptocurrency; and
- the complexity of complying with the evolving regulatory framework especially given that the Financial Industry Regulatory Authority (FINRA) has cautioned that cryptocurrencies have been used in illegal activity.

Given these concerns, the Employee Benefits Security Administration (EBSA) is expected to undertake an investigative program directed at plans offering 401(k) participants cryptocurrency (and related products) investments. Additionally, EBSA warned that it will likely question plan fiduciaries, who allow such investments, to explain how they are complying with their fiduciary duties of prudence and loyalty in light of the abovementioned risks.

Remember the DOL does not have any regulatory authority over governmental pension plans. Additionally, the DOL compliance assistance release is specific to 401(k) plans. Despite this, we believe it is prudent to share the release with Boards of Trustees as you consider investing plan assets in cryptocurrencies and other products whose value is tied to cryptocurrencies.

As always, if you have questions, please reach out to our office.