Fast Fact
November 2, 2023

SECURE 2.0 ACT LOW-BALANCE DISTRIBUTION LIMIT CHANGES: A LOOK BY AGE AND TENURE

Under current law, retirement plans are allowed to force out participants with vested account balances up to and including $5,000. However, for accounts with greater than $1,000–$5,000, if not directed otherwise by the account owner, the accounts must be moved to an individual retirement account (IRA) when forced out. In contrast, for accounts with balances of $1,000 or less, a lump sum payment to the participant is allowed. Accounts of $1,000 or less may be defaulted into an IRA, but the accounts greater than $1,000 cannot be cashed out unless directed to by the participant. Plans do not have to force out participants with these low balances and can set the force-out limit below $5,000, but if they do, they must follow these distribution options based on the vested account balance.

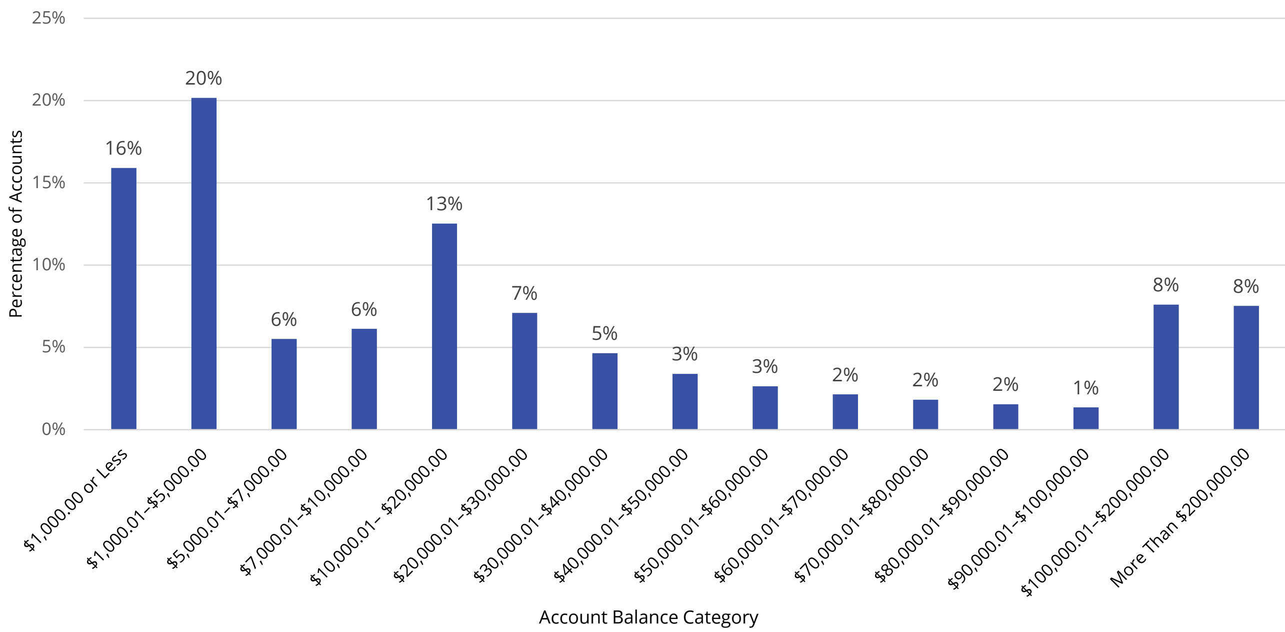
Under SECURE 2.0, the dollar limit for mandatory force-outs was increased from the $5,000 described above to $7,000 for distributions after December 31, 2023. In order to have an idea of how many additional accounts could potentially be impacted by this change, this Fast Fact builds on the cross-sectional Public Retirement Research Lab (PRRL) Database.

ABOUT THE DATA

The PRRL Database is an opt-in collaboration among public retirement plan sponsors. The analysis reflects data for two hundred and sixty-seven 457(b), 401(a), 401(k), and 403(b) defined contribution (DC) plans; over 3.0 million retirement accounts across 2.5 million state, county, city, and subdivision government employees; and $170 billion in assets as of year-end 2021. Plan sponsors receive complimentary benchmarking as a participation benefit. For more information on how to participate, please contact NAGDCA Executive Director Matt Petersen at mpetersen@nagdca.org.

As of year-end 2021, over one-third of accounts (36 percent) have balances of $5,000 or less (Figure 1). Sixteen percent of accounts in the PRRL Database have a balance of $1,000 or less, and 20 percent of accounts have a balance between $1,000.01 and $5,000.00. Overall, 42 percent of accounts have a balance of the new threshold of $7,000 (or less) that could be subject to force-out from the employer-based retirement system at separation.[1]

Figure 1
Accounts by Balance Category

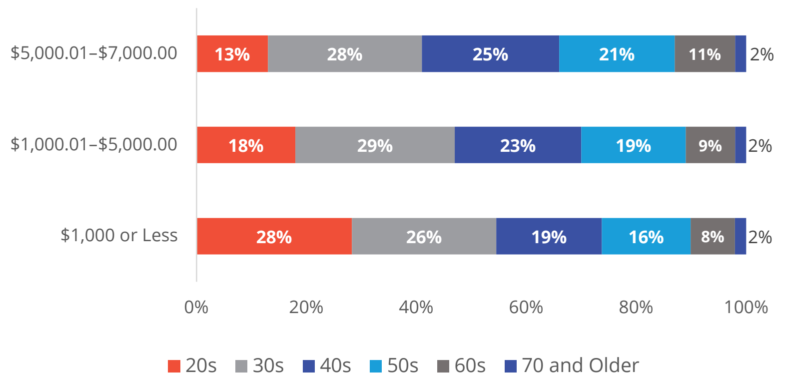


Analysis of account balances by age and tenure reveals that the force-out provision of up to $5,000 most commonly affects younger and low-tenure public plan participants. The following charts illustrate how the increased threshold expands the potential affected population of participants to those transitioning from early career to mid-career.

BY AGE

More than one-quarter (28 percent) of accounts with $1,000 or less are associated with participants in their 20s (Figure 2). Most participants affected by the threshold increase are in their 30s and 40s, accounting for 28 percent and 25 percent of participants with account balances between $5,000.01 and $7,000.00, respectively. Older participants are more likely to have higher account balances than younger employees, and they are therefore less likely to be impacted by the provision.

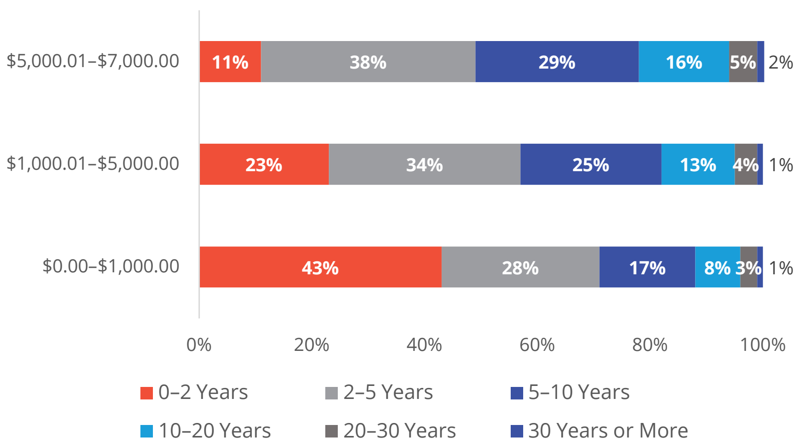
Figure 2
Age Distribution for Account Balances of $7,000 or Less



BY TENURE

Low-balance accounts are associated with individuals who are relatively new to their employer. Nearly three-quarters (71 percent) of accounts with $1,000 or less are associated with individuals with five or less years of tenure, with these accounts most commonly being associated with participants with two or less years of tenure. Most accounts newly affected by the threshold increase are held by employees with between two and five years of tenure (38 percent) and five and 10 years of tenure (29 percent). Over three-quarters (78 percent) of newly affected accounts are associated with participants with 10 or less years of tenure.

Figure 3: Tenure Distribution for Account Balances of $7,000 or Less



Note: *Limited to data with valid tenure information, reflecting 2.4 million accounts (approximately 80 percent of the PRRL dataset). Tenure "bins" exclude individuals at the minimum of the bin but include individuals at the top of the bin. For example, the "2–5 years" bin excludes individuals with precisely two years of tenure but includes individuals who have been with their employer for five years.*

CONCLUSION

Under current provisions, employers may distribute account balances for former employees if their account balances do not exceed $5,000. The SECURE 2.0 Act increased that limit from $5,000 to $7,000, effective for distributions made after December 31, 2023. The provisions governing the force-out process have traditionally affected new participants who have recently joined their employer. This impact is felt by both young individuals who are starting their careers and mid-career hires who are just beginning to participate in their current employer's retirement plan.

As of year-end 2021, approximately 36 percent of accounts have balances of $5,000 or less. The new cap of $7,000 or less increases this number by 6 percentage points to 42 percent. The age groups most impacted by this regulatory change are those in their 30s and 40s, accounting for 28 percent and 25 percent of participants with account balances between $5,000 and $7,000, respectively. Meanwhile, the tenure groups most affected by this change are those with tenures of 2–5 years and 5–10 years, representing 38 percent and 29 percent of participants, respectively. Methods to preserve the assets of those with low account balances will become even more important, as these additional affected participants may have a more limited time horizon to make up for any dollars distributed.

ABOUT PRRL

The Public Retirement Research Lab is a retirement-industry-sponsored collaborative effort of the Employee Benefit Research Institute (EBRI) and the National Association of Government Defined Contribution Administrators (NAGDCA). The PRRL analyzes data from its Public Retirement Research Database, the first-ever database specific to public-sector defined contribution data, to produce unbiased, actionable research aimed at enhancing understanding of the design and utilization of public-sector defined contribution retirement plans to better inform public plan design, management, innovation, and legislation. To learn more, visit www.prrl.org.

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ENDNOTES

1 This is a fairly rough estimate of the number of accounts impacted by the force-out provision. This number could be higher or lower because (1) not all these accounts are necessarily in plans that have a force-out provision; (2) the balances used are not the vested balance, which is what is used for the determination of the force-out; and (3) the total balances also include any rollovers into plans, but the force-out provision is calculated based on only the vested amount accumulated from direct contributions into the plan.