USI CONSULTING GROUP

M&L

Market & Legal Update

JANUARY 2025

Stay on top of the latest market developments and legal and regulatory updates that may affect your business.

MARKET UPDATE | Unprecedented Three in a Row?

Following two phenomenal years of back-to-back 20% plus gains for the S&P 500 in 2023 and 2024, investors aren't sure what to expect in 2025. Will we see an unprecedented third straight year of 20% plus returns or will returns be far more muted? Well, if January is any indication, three in a row may certainly be on the table. Equities posted a solid month across the board with the S&P 500 Index tacking on 2.8%, the Dow Industrials jumping 4.8%, and the tech-intensive NASDAQ adding 1.6%. Even outside of the U.S., markets surged, with the MSCI EAFE Index gaining an impressive 5.3%.

Market Return Indexes	Jan 2025	2024	2023
Dow Jones Industrial Average	4.8%	15.0%	16.2%
S&P 500	2.8%	25.0%	26.3%
NASDAQ (price change)	1.6%	28.6%	43.4%
MSCI Eur. Australasia Far East	5.3%	3.8%	18.2%
MSCI Emerging Markets	1.8%	7.5%	9.8%
Bloomberg High Yield	1.4%	8.2%	13.4%
Bloomberg U.S. Aggregate Bond	0.5%	1.3%	5.5%
Yield Data	**Jan 2025**	**Dec 2024**	**Nov 2024**
U.S. 10-Year Treasury Yield	4.58%	4.58%	4.18%

In mid-December the expectations for future Fed rate cuts in 2025 declined from a relatively optimistic four cuts to a more muted one to two cuts. Inflation numbers remain somewhat sticky and the threat of mass deportations and a possible tariff war loom. On February 1st, President Trump imposed 25% tariffs on imports from Mexico and Canada, as well as a 10% duty on China. Energy resources from Canada will have a lower 10% tariff. On February 3rd, both Canada and Mexico reached deals with President Trump to delay tariffs for 30 days. These tariffs on imports will likely raise prices on various imported goods and service-related costs, potentially contributing to inflation.

Whether additional tariffs are implemented and to what extent remains to be seen, but these tariffs may further complicate the Fed's decisions and could possibly delay further interest rate cuts.

December inflation data was relatively solid, particularly on the housing front. Headline CPI clocked in at 2.9%, which was in line with expectations, while core CPI came in at 3.2%, lower than the 3.3% that economists had predicted. Shelter prices, which comprise about a third of the CPI weighting, rose by 0.3% in December but were up 4.6% from a year ago, which was the smallest one-year gain since January 2022. As such, shelter costs contributed 1.6% to the 2.9% headline inflation rate. On the last day of the month, the Fed's preferred inflation gauge, the Personal Consumption Expenditures, was released. Both headline and Core PCE were in line with expectations, coming in at 2.6% and 2.8% respectively. While these numbers were somewhat promising, they still indicate that the Fed has more work to do to push inflation further down to its 2.0% target.

Moreover, job growth numbers in the December employment report came in much stronger than economists had expected, as the economy added 256,000 jobs in the month, far outpacing the expectation of 165,000. The strong report was almost certainly a consideration when the Fed decided to hold rates steady at their January meeting. Further, the report raised concerns that the Fed could hold off on rate cuts in the near term being that it would not have to stimulate the economy and could even consider interest rate hikes should inflation prove stickier than expected. As such, rate cuts may not be as near to the top of the agenda as some had hoped and in the Fed meeting minutes which were released on January 29th, they removed language noting that inflation had made progress toward the Fed's 2% goal, stating only that "inflation remains somewhat elevated."

On the economic growth front, GDP growth in the fourth quarter came in lower than expected, at 2.3%. This was below the 2.6% GDP growth expected by economists surveyed by Bloomberg and lower than the 3.1% reported for the third quarter. The consumer continued to be resilient, as increases in consumer spending and government spending contributed to economic growth in the quarter while decreases in business investment offset some of those gains. For 2024, the US economy grew at a 2.8% pace, which was a bit below the 2.9% GDP growth in 2023. The Fed expects real GDP to grow more slowly in 2025 at about 2.1%

The economy added **256,000 jobs** in the month, far outpacing the expectation of 165,000.

After two phenomenal years in 2023 and 2024, the prospects for the stock market in 2025 are relatively unknown but January was certainly a good start. While trendline GDP growth and increased corporate earnings supported by AI productivity gains could support equity markets in 2025, elevated valuations and policy uncertainty generate unpredictability. The same could be said for the bond markets, as the pace and magnitude of rate cuts are still up in the air. And finally, with the new administration in place, the economic landscape in 2025 is also a mystery to this point. President Trump's tariff and immigration policies are still evolving and could negatively impact inflation, while the expectation that the administration will work to reduce regulation and cut taxes could further boost corporate profits and economic growth. As such, it will certainly be interesting to see what 2025 has to offer on all fronts.

SECURE 2.0 Act Updates: Roth Catch-up and Automatic Enrollment

In January, the IRS issued proposed regulations providing much needed guidance on implementing two key provisions of the SECURE 2.0 Act: Roth Catch-up Contributions and Mandatory Automatic Enrollment. This article aims to provide you with information you need to know.

Roth Catch-up Contributions Required for High-Wage Earners

The Roth Catch-up Rule

Beginning January 1, 2026, participants in 401(k), 403(b), and governmental 457(b) plans who earned more than $145,000 in FICA wages in the prior year will be required to make catch-up contributions on a Roth (after-tax) basis rather than a pre-tax basis. The $145,000 threshold will be adjusted annually for inflation.

- The requirement to make catch-up contributions as Roth does not apply to the catch-up contributions of individuals who did not receive FICA wages in the prior year even if they earned income above $145,000 (e.g., self-employed individuals, partners, or governmental employees whose services are excluded from Social Security).
- The $145,000 threshold is determined based on FICA wages earned from the participant's common-law employer sponsoring the plan, without applying the controlled group rules. In other words, a plan administrator should not aggregate a participant's FICA wages with one employer with the FICA wages of another participating employer when applying the $145,000 limitation.
- SECURE 2.0 requires that a plan allowing employees to make Roth catch-up contributions must permit *all catch-up* eligible participants to make such contributions and cannot restrict the Roth treatment solely to high-wage earners subject to the rule. Plans also cannot mandate that all catch-up contributions be made as Roth for participants not subject to the rule. Those not subject to the rule may choose to make catch-up contributions on either a pre-tax or Roth basis.

Deemed Roth Elections

For high-wage earners subject to the rule, the proposed regulations clarify that plan administrators may treat a participant's pre-tax contribution election as a deemed Roth election with respect to catch-up contributions so long as the plan allows participants to make a new election reducing or ceasing elective deferrals.

No Requirement to Have a Roth Program (optional)

Plans that wish to allow high-wage earners subject to the rule to make catch-up contributions must have a Roth feature. Plans that do not have a Roth feature cannot permit Roth catch-up contributions. Amending the plan to add a Roth feature is *optional* for the employer. However, if a plan does not include a Roth feature, high-wage earners will be unable to make catch-up contributions, even though participants not subject to the rule can continue to make pre-tax catch-up contributions. The proposed regulations clarify that this would not create a non-discrimination issue.

Correction Methods

Recognizing the administrative complexities of implementing this provision, the proposed regulations outline correction methods for addressing failures related to the rule (e.g., failing to treat a pre-tax catch-up deferral as a Roth deferral for individuals subject to the rule). The correction methods include a Form W-2 correction, an in-plan Roth rollover correction, or a distribution of the errant pre-tax contributions (including earnings). The deadline for such corrections is generally April 15th of the calendar year following the year in which the deferral was made. A plan may use any of the correction methods noted above, but must apply the same method consistently for all affected participants in a given year. To utilize these correction methods, a plan must also have established practices and procedures designed to comply with the Roth catch-up rule.

Increased Catch-up Limit

The proposed regulations also address another SECURE 2.0 provision related to catch-up contributions. Beginning January 1, 2025, the catch-up contribution limit is increased for participants ages 60 through 63. If the plan permits, these individuals may make contributions up to the greater of $10,000 (indexed for inflation), or 150% of the normal age 50 catch-up limit from the prior year. For 2025, the limit is $11,250. The proposed regulations clarify that this provision is optional and employers do not have to allow for the increased catch-up limit and can apply the normal catch-up limit to all eligible participants regardless of their age.

Mandatory Automatic Enrollment Requirement

As of the date of enactment, December 29, 2022, the Secure 2.0 Act added Internal Revenue Code Section 414A which requires 401(k) and 403(b) plans with elective deferral features to comply with requirements for automatic enrollment of plan participants beginning January 1, 2025. However, many plans are exempt from the automatic enrollment requirement ("AE Requirements") including SIMPLE 401(k) plans, governmental and church plans, and certain new and small businesses. In addition, and most importantly, all plans established prior to the date of enactment - December 29, 2022 - are exempt from the mandatory automatic enrollment requirement. In other words, plans established before December 29, 2022 are not required to implement automatic enrollment.

Required Terms

Plans subject to the AE Requirements are required to adopt an eligible automatic contribution arrangement (an "EACA") that:

- Automatically enroll all participants eligible to make elective deferrals at a uniform contribution rate initially between 3% and 10% of compensation.
- For individuals who have not made affirmative elections, annually increase the deferral rate by 1% up to a minimum of 10% and maximum of 15% of compensation.
- Provide automatically enrolled participants with the opportunity to withdraw such automatic contributions within 90 days of the first payroll date that such automatic contributions were withheld from their wages.

The automatic enrollment provisions must apply to all employees eligible to make elective deferrals into the plan who have not otherwise made an affirmative election. This includes union employees, long-term part-time employees, and employees hired prior to the effective date of AE Requirements.

Exceptions to the Automatic Enrollment Requirements

In addition to the exemption of "pre-enactment" plans discussed above, small businesses and new businesses are excepted from the AE Requirements. The proposed regulations clarify how the new business and small business exceptions are applied.

- New Businesses - Employers which have been in existence for less than three years are exempt from the AE requirements. Under the proposed regulations the AE requirements apply to plans of a new business in the first plan year in which, as of the first day of such plan year, the employer has been in existence for three (3) years. In addition, if a new employer is a successor to a prior employer, it will not qualify for the new business exception.
- Small Businesses - A plan sponsored by an employer who normally employs ten or fewer employees is exempt from the AE requirements. The proposed regulations adopt the employee counting method used for COBRA coverage requirements. AE requirements apply to a plan as of the first plan year that begins one year after the first taxable year that the employer exceeded the ten-employee threshold.

Application to MEP

The proposed regulations also addressed questions arising from participation in Multiple Employer Plans ("MEPs"). Whether automatic enrollment requirements apply in a MEP is determined on an employer-by-employer basis. As such, the merger of a pre-enactment plan excepted from the automatic enrollment requirement into a MEP established after December 29, 2022 would not cause the plan to lose it excepted status and likewise a merger of a plan established after December 29, 2022 into a MEP established prior would not cause the MEP as a whole to become subject to the automatic enrollment requirements.

Next Steps & How USICG Assists

Employers should review their plans to determine how they will best implement the new AE Requirements and Roth catch-up rules. The IRS generally considers employers that operate their plans in accordance with proposed regulations to be in good faith compliance with the applicable rules. The IRS further indicated that final regulations will be effective for taxable years beginning six months after their issuance.

The USICG team can help answer any questions that you have regarding the AE Requirements or Roth catch-up contribution rules. As soon as additional information becomes available or final regulations are published, we will provide updates to inform you about such guidance and its impact on plan compliance and administration.

Retirement Resources for You

USI Consulting Group's team of experts is happy to assist employers with all retirement plan compliance matters and changes in the market, including those discussed here, to help you mitigate risk and financial impact to your organization.

To learn more, please contact your local USICG representative, visit our Contact Us page or reach out to us at information@usicg.com.

Find the address and telephone number of your local USI Consulting Group office here.

Follow USICG on LinkedIn to stay up to date with retirement news!

For previous market and legal commentaries please click here.

This communication is published for general informational purposes and is not intended as advice or a recommendation specific to your plan. Neither USI nor its affiliates and/or employees/agents offer legal or tax advice.

An index is a measure of value changes in a representative grouping of stocks, bonds, or other securities. Indexes are used primarily for comparative performance measurement and as a gauge of movements in financial markets. You can not invest directly in an index and, for comparative purposes; they do not reflect the effect of the various fees inherent in actual investment vehicles.

The S&P 500 Index is a market value weighted index showing the change in the aggregate market value of 500 U.S. stocks. It is a commonly used measure of stock market total return performance.

The Dow Jones Industrial Average is a price weighted index comprised of 30 actively traded blue chip stocks; primarily industrial companies, but including some service oriented firms.

The NASDAQ Composite Index is a market-value weighted index that measures all domestic and non-U.S. based securities listed on the NASDAQ Stock Market.

Gross Domestic Product (GDP) is the market value of the goods and services produced by labor and property in the U.S. It is comprised of consumer and government purchases, net exports of goods and services, and private domestic investments. The Commerce Department releases figures for GDP on a quarterly basis. Inflation adjusted GDP (or real GDP) is used to measure growth of the U.S. economy.

The MSCI Europe and Australasia, Far East Equity Index (EAFE) is a market capitalization weighted unmanaged index developed by Morgan Stanley Capital International to measure approximately 1,100 securities in 21 major overseas stock markets. It is a commonly used measure for foreign stock market performance.

The Barclays Capital U.S. Aggregate Index covers the U.S. Dollar denominated investment grade, fixed-rate, taxable bond market of SEC-registered securities.

The Barclays Capital U.S. Corporate High Yield Index covers the U.S. Dollar denominated, non-investment grade, fixed income, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's Fitch, and S&P is Ba1/BB+/BB+ or below.

The MSCI Emerging Markets Index (EM) is a free-float-adjusted market-capitalization index developed by Morgan Stanley Capital International. It is designed to measure the equity market performance of 26 emerging market countries.

The 10 Year Treasury Yield is the interest rate the U.S. government pays to borrow money for a 10-year period. In addition to influencing how much the government pays to borrow over this time-frame, the 10-year Treasury Yields also determines how much investors earn by investing in this debt and it is a good indicator of investor sentiment.

The higher the yield, the better the economic outlook.

Market Update is a monthly publication circulated by USI Advisors, Inc. and is designed to highlight various market and economic information. It is not intended to interpret laws or regulations.

This report has been prepared solely for informational purposes, based upon information generally available to the public from sources believed to be reliable, but no representation or warranty is given with respect to its completeness. This report is not designed to be a comprehensive analysis of any topic discussed herein, and should not be relied upon as the only source of information. Additionally, this report is not intended to represent advice or a recommendation of any kind, as it does not consider the specific investment objectives, financial situation and/or particular needs of any individual client.

Investment Advice provided by USI Advisors, Inc. Under certain arrangements, securities offered to the Plan through USI Securities, Inc. Member FINRA/SIPC. 95 Glastonbury Blvd., Suite 102, Glastonbury, CT 06033. USI Consulting Group is an affiliate of both USI Advisors, Inc. and USI Securities, Inc.

Connect with us today | information@usicg.com | 860.633.5283 | usicg.com |