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CARES Act Makes Important Qualified Plan Changes

In the midst of the COVID-19 emergency employers and employees are asking if their employer sponsored retirement plan or IRAs may be used to provide financial relief?

Congress, recognizing that qualified plan and IRA money may represent a significant source of funds during this economic crisis, made several temporary changes to qualified plan and IRA rules. The CARES Act (Coronavirus Aid, Relief and Economic Security Act) makes access to your qualified plan funds easier and with slightly reduced tax consequences. It also protects retirees from having to make certain financial transactions during a very volatile economic climate.

Waiver of 10% Early Withdrawal Penalty

Generally, if you take a withdrawal from your IRA or other retirement plan prior to age 59 ½ you generally must pay a 10% penalty tax on the withdrawal. The CARES Act provides for a limited waiver of this 10% penalty under the following circumstances:

- Distribution is taken after 1/1/2020
- You (your spouse or dependent) are either (a) diagnosed with COVID – 19, or (b) you experience adverse financial consequences
- Withdraw no more than $100,000 (this is an aggregate amount from all eligible qualified plans).

This withdrawal will be subject to ordinary income tax, however you may spread the income ratably over three years.

You may also choose to recontribute the funds and may do so within three years of the withdrawal without regard to regular contribution caps.

Increase in Loan Availability

The Act also increases the amount of a loan a participant can take from their salary deferral plan, such as a 401(k).*

- Prior to the CARES Act, the available loan was generally 50% of the present value of the participant's account. Under the Act it increases to 100%.
- Prior to the Act, the maximum loan amount is $50,000. Under the Act it increases to $100,000 but only for 180 days from the date of enactment.

Significantly, this is an optional benefit that may be – but is not required to be – made available by plan sponsors.

The due date of repayment of an outstanding loan of any qualified individual that occurs from the date of enactment to December 31, 2020 is delayed for one year. Subsequent loan payments must be adjusted to reflect the delay and any interest that accrues during the delay.

The legislation permits retirement plans to adopt these rules immediately, even if the plan does not currently allow for hardship distributions or loans, provided the plan is amended on or before the last day of the first plan year beginning on or after Jan. 1, 2020, or later if prescribed by the Treasury Secretary.

*These changes may apply to 403(b) and 457(b) plans as well to the extent the plan permits the loans.

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Qualified Plan / IRA Provisions – Waiver of Required Minimum Distributions

If you have funds in an IRA or other retirement account (such as 401(k)) you are subject to a required minimum distribution beginning at age 72. The required minimum distribution has been suspended for 2020. This includes 401(k) plans and profit sharing plans, 403(a) and 403(b) plans and 457(b) plans. It does not, however, waive the required minimum distributions for defined benefit plans.

FAQs

In addition to the CARES Act, Congress also introduced two other COVID-19 relief bills in the past few weeks. Here are some frequently asked questions to also consider for qualified plans and IRAs:

Q: If a company is struggling financially in connection with the COVID-19 emergency and is considering layoffs, could layoffs potentially affect that business's retirement plan?

A: Yes. Employers will want to consider whether partial plan termination rules may affect their retirement plan when determining whether to move forward with layoffs. The general rule is that a partial plan termination may occur when plan participation decreases by 20 percent or more. However, the ultimate determination is based on a facts and circumstances analysis by the IRS. The partial plan termination rules would require an employer to fully (100%) vest all participants affected by a partial plan termination. Keep in mind that a partial plan termination could occur as a result of a single group layoff or multiple group layoffs.

Q: If your retirement plan's investment performance is declining in connection with the COVID-19 emergency, should our plan fiduciaries revisit investments?

A: Plan fiduciaries have an ongoing responsibility to monitor the investment options offered under their retirement plans. In a normal environment, plan fiduciaries should review the plan's investment funds on a quarterly basis. In light of the COVID-19 emergency and the impact on the financial markets, it may be prudent for plan fiduciaries to review the plan fund menu more frequently. In addition, plan fiduciaries should check the plan's investment policy to determine what, if any, actions are required in this case. Plan fiduciaries should continue to monitor investment performance, consult with their plan's investment advisors and plan financial advisors, and document steps taken to monitor the plan's investment performance.

Concluding thoughts

It is vital that your decisions regarding your own qualified retirement account or IRA not be made in a vacuum. The economic crisis brought on by the COVID-19 emergency is very real and may be very extreme for some people. Consult with your financial advisor and your tax professional to assess any action you may take today. Qualified plan rules are highly complex and highly regulated. It is important to make many of these decisions with the guidance of professionals who can help you see the big picture.