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Retirement Plan Provision Updates

CARES Act (Coronavirus Aid, Relief, and Economic Security Act)

March 2020

The following information provides practical action items for managing your organization's retirement plan through periods of financial stress.

The CARES Act was passed into law on Friday (March 27th), making roughly $2 trillion in financial aid available to individuals, small businesses, big corporations, and local governments to blunt the economic devastation caused by COVID-19. Aside from the aid, the CARES Act also included provisions for retirement plans, temporarily expanding distribution and loan rights for employees who have been impacted by COVID-19. Below is a summary of those provisions along with instructions on how to properly suspend employer contributions in your organization's retirement plan.

First – the CARE Act Provisions

1. **"Coronavirus Related Distributions" (CRDs):** A provision in the CARES Act waives the 10% early withdrawal penalty for distributions up to $100,000 from a qualified retirement account if an employee is impacted by COVID-19, as defined:

   a. They have been diagnosed with COVID-19;
   b. They have a spouse or dependent diagnosed with COVID-19;
   c. They experience adverse financial consequences as a result of being quarantined, furloughed, laid off, having work hours reduced, or being unable to work due to lack of childcare due to COVID-19;
   d. The closing or reducing hours of a business owned or operated by the individual due to COVID-19 (this is for the 'gig' workers out there);
   e. Or other factors as determined by the Treasury Secretary.

Considerations: These withdrawals are allowed for the calendar year 2020, and the window closes in 2021. Finally, the burden of proof for CRDs lies on the employee, not the employer.

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Paying back the CRDs: Employees have 3 years to pay back their distribution. The clock starts the day after the distribution was received. If they cannot pay back the CRD, the outstanding amount is subject to income tax, but that tax is payable over 3 years. When taking a CRD, federal income tax withholding is not required.

2. **Loan limits increased for new loans:** For the next 180 days, loan limits have been increased to $100,000 or 100% of the vested account balance. This expires on September 23rd, 2020. The only participants allowed to take advantage of these higher loan limits are those directly impacted by COVID-19 and fall under the same CRD qualifications listed above.

3. **Existing loans are also impacted (for CRD-qualified employees):** If your plan currently has existing loans, those loan payments may be delayed for up to 1 year. Again, this only applies to impacted employees, as defined in the CRD qualifications listed above.

Considerations: Remember that this applies to COVID-impacted employees only. For these delayed loans, you will have to recalculate/re-amortize the loan, and there will be additional interest due to the extra year of the loan period. This extension provision seems to be mandatory, but only for COVID-impacted employees. Missed loan payments by employees who are not considered qualified individuals will trigger default and deemed distributions.

4. **RMDs aren't required this year:** Congress also allowed this "RMD Holiday" in 2009 in response to the Great Recession. This makes sense; your RMD calculation would have been based on your December 31, 2019 value, which was (likely) higher than your current account value. This means you don't have to "sell low" to meet your RMD obligation. This holiday also includes an individual's first RMD which is attributable to 2019 (not paid by Jan. 1, 2020). For example, if a participant turned 70½ in 2019 and has a Required Beginning Date of April 1, 2020:

    a. But has not yet taken the distribution—then no distribution is required in 2020 (for the 2019 distribution year).
    b. Took an RMD after Dec. 31, 2019, it is subject to the waiver for 2020 and the amount can be rolled over.

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c. But, if the distribution was taken in 2019, no relief is available.

In summary – employees impacted by COVID-19 can take up to $100,000 from their 401k accounts – either a distribution or a loan – to help stay afloat during this difficult time. These provisions can be utilized immediately; you will, however, need to amend your plan. You won't be required to do so until the last day of the first plan year beginning on or after January 1st, 2022.

Next – Making Mid-Year Changes to Your 401k Plan

The CARES Act provisions go a long way in helping employees blunt the impact of the COVID-caused recession, but what options do organizations have in periods of financial stress? For those organizations making an employer contribution to their retirement plan, suspension goes a long way in providing temporary relief. Below is some guidance on how to properly suspend an employer contribution, based on the type of contribution you have.

Suspending a Safe Harbor Contribution

Of all the employer contribution types, suspending safe harbor contributions has the most formal requirements. First, you need to amend your Plan Document and notify all employees in writing of the intention to suspend (be sure to include the date of suspension). The suspension date must be at least thirty days from the date of notification. Thirty days after formally notifying employees, you may stop your Safe Harbor contribution.

Considerations: Determine whether you have a pay period safe harbor match or an annual safe harbor match. If you have an annual match, you have additional time to make the deposits (you can wait until year-end). If you have a pay period match, you must make the match no later than the quarter following the quarter it was due. Here's a tip – if you have a pay period patch, retroactively amend your plan to make it an annual match to give you more time to make the safe harbor deposit.

Be aware that suspending the Safe Harbor contribution opens your plan up to top-heavy testing as well as ADP/ACP Testing, which could create the need to make corrective refunds to owners and Highly Compensated Employees (HCEs).

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Suspending a Discretionary Match

This is the easiest type of employer contribution to suspend. Because it's labeled as 'discretionary' in the Plan Document, simply stop making the contribution at any time. It goes without saying, but notifying your employees in advance of the suspension is our recommended approach.

Suspending a Fixed Match

A fixed match is one that has been stated in the Plan Document. Because it is present in the Plan Document, you must amend the plan document which triggers a Summary of Material Modification, or SMM, which must be distributed to all participants 210 days after the end of the year. Technically, this means you can suspend the match after the Plan Document is amended and not formally notify participants until July of 2021.

A suggested best practice is to announce the intention to suspend, suspend the fixed match, and send the SMM within a reasonable time frame.

In summary – organizations that make employer contributions to their retirement plans can suspend them to weather this COVID-19 storm. If you plan on suspending your contribution, follow guidance to make sure you do it the right way.

Lastly – Implications for Temporary Layoffs

If you're planning on laying off a significant amount of your workforce (or already have), bear in mind it could have implications on your retirement plan. If you're laying off 20% of your workforce for reasons other than routine turnover (like losses due to COVID-19), your plan could be subject to the IRS' Partial Termination Rules. If your plan qualifies AND it has a match/profit sharing contribution subject to a vesting schedule, you have to make those laid-off employees 100% vested in the employer's contributions. For businesses impacted by COVID-19, you will generally need to account for all affected participants laid off due to COVID-19 during the current plan year to make this determination. If they're rehired after 2-8 weeks, you may be able to avoid being labeled as a partial termination.

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