

## Publications

# CARES Act Brings Immediate Changes for 401(k) Plans

## ATTORNEYS &amp; PROFESSIONALS

**David Ashner**[dashner@groom.com](mailto:dashner@groom.com)

202-861-6330

**Kim Boberg**[kboberg@groom.com](mailto:kboberg@groom.com)

202-861-2606

**Mark Carolan**[mcarolan@groom.com](mailto:mcarolan@groom.com)

202-861-5424

**Elizabeth Thomas Dold**[edold@groom.com](mailto:edold@groom.com)

202-861-5406

**Kelly A. Geloneck**[kgeloneck@groom.com](mailto:kgeloneck@groom.com)

202-861-5418

**David Levine**[dlevine@groom.com](mailto:dlevine@groom.com)

202-861-5436

**Louis T. Mazawey**[lmazawey@groom.com](mailto:lmazawey@groom.com)

202-861-6608

**Malcolm Slee**[mslee@groom.com](mailto:mslee@groom.com)

202-861-6337

**Seth Perretta**[sperretta@groom.com](mailto:sperretta@groom.com)

202-861-6335

**Allison Ullman**[aullman@groom.com](mailto:aullman@groom.com)

202-861-6336

**Brigen Winters**[bwinters@groom.com](mailto:bwinters@groom.com)

Effective March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") brings immediate changes and relief to 401(k) plans, similar to natural disaster relief issued in the past. The changes include:

- **Distribution Right.** Distribution right of \$100,000 from the plan (not to exceed the participant's account balance) through December 30, 2020 that is subject to special tax relief.
- **Loan Limit Increase.** Increase in the loan limit under Code section 72(p) from \$50,000 to \$100,000 (or 100% of the participant's account balance, if less) for loans made from March 27, 2020 through September 22, 2020.
- **Loan Suspension.** Suspension of loan payment due March 27, 2020 through December 31, 2020 for up to one year.
- **RMD Relief.** Suspension of 2020 required minimum distributions.

This relief follows the relief available for natural disasters in the past (and the 2009 WRERA relief following the 2008 economic downturn), and as such is generally viewed as available at the option of the plan sponsor.

Plan amendments are not required until the end of the 2022 plan year (2024 for governmental plans), provided that the plan is operated in accordance with the terms. Therefore, plan sponsors should work together with their recordkeepers to provide this valuable relief.

A brief summary of the relief is set forth below:

## Distribution Right

*For distributions from January 1, 2020 through December 30, 2020, a qualified individual can elect to treat a 401(k) plan distribution as a "Coronavirus-related distribution," which has the following benefits:*

- Not subject to the 10% early withdrawal tax for distributions prior to age 59-1/2
- Not subject to mandatory 20% withholding (rather 10% voluntary withholding applies)

- Not treated as an eligible rollover distribution (and therefore no 402(f) rollover notice)
- Taxed pro rata over a three year period (2020-2022), unless the individual elects otherwise
- Eligible for re-contribution back into a plan or IRA within three years from the date of distribution
- Up to \$100,000 can be taken by the individual (with the plan sponsor obligation to ensure that the \$100,000 distribution cap is not exceeded for plans within the employer's controlled group). The limit is a personal limit for each individual that includes both plan and IRA distributions.
- Unlike a hardship distribution, there is no requirement to show documentation of losses or expenses to justify the distribution.

A qualified individual is defined as an individual (1) who is diagnosed with SARS-CoV-2 or COVID-19 by a test approved by the CDC, (2) whose spouse or dependent is so diagnosed, or (3) who experiences adverse financial consequences as a result of being quarantined; being furloughed or laid off or having work hours reduced to such virus; being unable to work due to a lack of child care due to the virus; closing or reducing hours of a business owned or operated by the individual due to the virus; or such other factors determined by Treasury. No such other factors have been published by Treasury to date. Notably, an employee certification will be accepted for this purpose.

## Loan Limit Increase

Code section 72(p) is amended to replace \$50,000 and 50% account balance restrictions with \$100,000 and 100% of the participant's account balance for loans made from March 27, 2020 through September 22, 2020. This is still an aggregate limit taking into account other outstanding loan balances. A plan sponsor may want to expand the number of plan loans available to facilitate these loans.

## Loan Suspension

Loan payments due between March 27, 2020 through December 31, 2020 can be suspended for a year. Notice 2005-82 provides a safe harbor that results in a loan being re-amortized on January 1, 2021 including the suspension period and payment restarting on such date. Plan sponsors should discuss the suspension approach with their recordkeeper. (Note that Notice 2020-23 extending tax deadlines generally also provides a loan suspension period, for payments due April 1 through July 14, 2020, until July 15.)

## RMD Relief

Similar to the waiver approved in the wake of the 2008 economic downturn, the CARES Act provides for 2020 required minimum distributions ("RMD") to be waived for 401(k) plans due to the volatile financial markets.

This means that the following RMD payments do not need to be made from the plan:

- 2020 RMD payments for individuals who already are receiving them (e.g., attained 70-1/2 before 2019),
- 2020 RMD payments for individuals who turned age 70-1/2 or retired (if later) in 2019, along with the 2019 RMD payment to the extent it was not already made in 2019,
- 2020 RMD payments for individuals who have a required beginning date of April 1, 2021 as a result of their retirement in 2020

These amounts are eligible for indirect rollover within 60 days to a plan or IRA if the participant so elects. The 60-day period was extended for RMDs made between Feb. 1, 2020 and May 15, 2020 until July 15, 2020 following Notice 2020-23.

Absent guidance in short order, we recommend following Notice 2009-82, which provides for two different approaches (and sample amendments) for plan sponsors to choose between:

1. Default to Continue 2020 RMDs. This approach provides individuals an opportunity to elect to stop receiving such distributions.
2. Default to Discontinue 2020 RMDs. This approach provides individuals an opportunity to elect to continue receiving such distributions.

The plan sponsor can also elect to treat these 2020 RMD payments as eligible for direct rollover.

For post-death distributions, this one-year period (*i.e.*, 2020) is disregarded for purposes of the five-year payout period. It also provides a one-year extension for a spouse to elect to commence lifetime payments where that decision was otherwise due in 2020.

## Next Steps

Operations is the key focus. Plan amendments are not required until the end of the 2022 plan year (2024 for governmental plans), provided that the plan is operated in accordance with the terms. Therefore, plan sponsors should work together with their recordkeepers to provide this valuable relief.

As many participants are in need of funds, decisions may need to be made rather quickly by plan sponsors. Some recordkeepers are trying to facilitate participant needs with a type of negative election, so plan sponsors need to be on the look-out for these materials and understand their role in administering these provisions. And of course, to the extent the IRS issues guidance, which we understand informally that they are working on, we will need to adopt operations to comply.

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