Employee Benefits Corner

The Budget Act Brings Much Needed Hardship Relief for Plan Participants

By Elizabeth Thomas Dold and David N. Levine

The Bipartisan Budget Act of 2018 (the "Budget Act") brings important relief for plan sponsors and recordkeepers for tax-qualified retirement plans. This relief includes (1) relaxed hardship withdrawal rules, (2) expanded rollover for improper federal tax levies, (3) California wildfire relief for plan distributions, and (4) a special Congressional committee to address the major funding concerns for multiemployer plans. These provisions are summarized below.

1. Relaxed Hardship Withdrawals

First, and likely most significant, is the changes made to hardship withdrawals for 401(k) and 403(b) plans. Historically, hardship withdrawals were rather restricted and a number of provisions had to be met, including the following:

- Hardship withdrawals were not available from qualified non-elective contributions (QNECs), qualified matching contributions (QMACs), safe harbor plan contributions, and post-12/31/1988 earnings, including on pre-tax contributions.
  - To meet the safe harbor requirement under the 401(k) regulations that the distribution is deemed necessary to satisfy an immediate and heavy financial need, the participant:
  - Must have obtained all other currently available distributions (including distribution of ESOP dividends, but not hardship distributions) and non-taxable (at the time of the loan) loans, under the plan and all other plans maintained by the employer and
  - Is prohibited, under the terms of the plan or an otherwise legally enforceable agreement, from making elective contributions and employee contributions to the plan and all other plans maintained by the employer for at least six months after receipt of the hardship distribution.

And as the 403(b) regulations incorporate the 401(k) regulations by reference for hardship distributions, these same rules outlined above extend to 403(b) plans.

Under the Budget Act, effective for plan years beginning after 2018 (*e.g.*, January 1, 2019, for a calendar year plan), the following changes have been made:

ELIZABETH THOMAS DOLD and **DAVID N. LEVINE** are Principals at Groom Law Group, Chartered in Washington, D.C.

- *Available Loans No Longer Relevant for Hardship Withdrawals*. A hardship withdrawal will not fail to be a hardship distribution solely because the employee does not take any available loan under the plan. We anticipate that the Internal Revenue Service ("IRS") will clarify that this change is also extended to loans of other plans of the same employer. Therefore, recordkeepers and plan sponsors will no longer have to concern themselves with whether or not the participant has the ability to take out a loan to address the hardship need. This will streamline the hardship process and likely expand the hardship withdrawals available to participants.

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- *Eliminates the Six-Month Suspension Period.* The Secretary of the Treasury is directed to amend the 401(k) regulations to eliminate the six-month suspension period for making employee contributions (pre-tax, Roth or after-tax) following a safe harbor hardship distribution. We anticipate IRS guidance regarding the implementation of this rule, similar to the guidance that was issued following EGTRRA in Notice 2001-56 and 2002-4 when Congress changed the 12-month suspension period to six months (and eliminated the post-hardship contribution limit). For example, we anticipate that the IRS will (1) provide transition relief to permit safe harbor hardship plans to eliminate the suspension period for only new loans on or after the effective date of the provision (*e.g.*, January 1, 2019, for a calendar year plan), (2) indicate whether a safe harbor 401(k) or 403(b) plan will be required to make these changes to maintain their safe harbor 401(k)/401(m) plan status, (3) indicate whether a non-safe harbor plan that wants to continue to use the safe harbor hardship distribution provisions needs to adopt this change, and (4) address the timing of any such plan amendments for pre-approved plans and individually designed plans. For example, individually designed plans have a Required Amendments List giving plan sponsors a two-year period once an amendment makes the list to adopt an amendment, provided these changes fall on this list and are not otherwise treated as discretionary amendments that would generally need to be adopted by the end of the 2019 Plan Year.
- *QNEC, QMACs, Safe Harbor Contributions, and Earnings Eligible for Hardship*. Lastly, the types of sources of contributions that are eligible for hardship distribution is now expanded to include: QNECs, QMACs, safe harbor plan contributions, and earnings of these accounts and on all pre-tax deferrals (including post-1988 earnings on elective deferrals). We anticipate recordkeepers and plan sponsors moving to include these additional contribution sources to facilitate a participant's need for a hardship withdrawal, which will likely eliminate the need to separately track the post-12/31/1988 earnings on deferrals.

For all these changes, we anticipate that these same changes will extend to 403(b) plans, but IRS guidance to that effect would be welcomed as we await updated regulations.

As we await additional guidance, plan sponsors should consider the impact of this relief and consider their appetite to make these changes, which will expand hardship withdrawal availability to participants in need. However, it will likely require updated hardship procedures, plan amendments, and changes to the Summary Plan Description to implement the changes, and with a 2019 Plan Year effective date there is not a lot of time.

2. Expanded Rollover Contribution for Improper Federal Tax Levies

Although qualified plans generally prohibit the assignment or transfer of pension benefits following the Code and ERISA anti-alienation provisions, there is an exception for federal tax levies. But when the IRS makes a mistake and the tax levy is improper, there is a process to return the funds to the taxpayer. However, it is not a process that would be completed within 60 days of the transfer to the government, and therefore, plan distributions paid to the federal government even if the return was a result of an error could not be re-contributed to the plan.

Well, the Budget Act provides a fix for this one. Effective January 1, 2018, plan distributions (including 401(a), 401(k), 403(b), governmental 457(b), and IRAs) made to comply with a federal tax levy that subsequently turns out to have been wrongful can be re-contributed to the plan (plus interest thereon), if the plan sponsor accepts the funds, or otherwise to an IRA by the tax filing deadline (excluding extensions) for the year of the refund. This returns the funds to the tax-favored solution and avoids current taxation. (Of course, it does not permit a tax-free rollover of non-Roth funds to a Roth IRA or a designated Roth account.)

If a plan sponsor is interested in facilitating this return of the funds, which is optional, the plan's rollover contribution procedures and plan document provisions should be reviewed and updated as necessary to accommodate any such requests.

3. California Wildfire Relief for Plan Distributions

Effective February 9, 2018, the Budget Act provides relief substantially similar to the Congressional relief provided to Hurricanes Henry, Irma, and Maria for plan distributions from October 8, 2017, and before January 1, 2019. This relief is in addition to the hardship and loan relief available under Announcement 2017-15.

The relief includes the following relief provisions for a "qualified wildfire distribution," which is a distribution of up to $100,000 from a Code Sec. 401(a), 403(b), IRA or governmental 457(b) plan on or after October 8, 2017, and before January 1, 2019, to an individual whose principal place of abode at any time during October 8–December 31, 2017, was in the California wildfire disaster area and who sustained an economic loss by reason of the wildfires:

- In-service distribution permitted;
- No 10% early withdrawal tax (under Code Sec. 72(t));
- No mandatory 20% federal income tax withholding;
- No 402(f) rollover notice as the distribution is not treated as rollover eligible; and
- Taxed over a three-year period and an option to rollover the amount to an eligible retirement plan within three years and avoid the taxation.

Participants who took a plan distribution after March 31, 2017, and before January 15, 2018, for a California home purchase through June 30, 2018, can return the funds to the plan as an eligible rollover contribution.

Lastly, the Budget Act increases the plan loan limit from $50,000 and 50% of vested account balance to $100,000 and 100% of vested account balance through December 31, 2018, and provides up to a one-year delay for certain loan repayments.

These provisions are optional, and if elected by the plan sponsor, should be reflected in a plan amendment by the end of the 2019 Plan Year (governmental plans receive an additional two-year period).

Therefore, plan sponsors and recordkeepers should review their current relief provided to impacted Californians and if additional relief if needed, consider providing some or all of the relief described above, and update procedures and plan documents accordingly.

4. House and Senate Joint Select Committee on Solvency of Multiemployer Pension Plans

It is no secret that multiemployer plans and the Pension Benefit Guaranty Corporation's ("PBGC") multiemployer insurance program face serious fiscal challenges. So as a first step towards a solution, the Budget Act creates a bipartisan committee to improve the solvency of multiemployer pension plans and the PBGC, called the House and Senate Joint Select Committee on Solvency of Multiemployer Pension Plans (the "Committee"). The Committee is charged with providing recommendations and legislative language to improve the solvency of multiemployer plans and the PBGC. Specifically, by no later than November 30, 2018, the Committee must vote on a report containing detailed findings and recommendations and proposed legislative language, which is only approved if a majority of the Republicans (5/8) and a majority of the Democrats (5/8) on the Committee vote in its favor. Once the report is approved, it will have a fast track process to facilitate it becoming law. So stakeholders in the multiemployer system may wish to submit their views about potential legislation to the Committee and participate in the process.

As we await additional guidance, plan sponsors should consider the impact of this relief and consider their appetite to make these changes, which will expand hardship withdrawal availability to participants in need.

