

IRS Issues Anticipated CARES Act Guidance On Plan Loans and Distributions

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On June 19, 2020, the Internal Revenue Service (“IRS”) issued Notice 2020-50, which provides clarity to plan administrators and participants on coronavirus-related loans and distributions following the passage of the [Coronavirus Aid, Relief, and Economic Security \(CARES\) Act](#) (Pub. L. 116-36). Notably, this guidance

- expands the reach of relief provisions by factoring in household — not just individual — financial impact due to COVID-19, and adding additional events that cause a financial impact.
- provides a safe harbor for employers electing to offer plan loan suspensions.
- includes a sample certification for participants to sign and explains the parameters of the “actual knowledge” exception to reliance on the certification for both loans and coronavirus-related distributions (CRDs).
- allows cancellation of irrevocable deferral elections under a nonqualified deferred compensation plan (NQDC plan) for participants who take a CRD.
- largely tracks Notice 2005-92 that was developed to provide relief after Hurricane Katrina, including details and examples of:
 - *Eligible Distributions*. Distributions eligible for CRD treatment includes loan offsets, as well as payments from pension plans and money purchase pension plans if there is otherwise a distributable event. CRDs excludes various corrective distributions that are not eligible rollover distributions.

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- Use of Funds. The amount of the CRD is not limited to the needs of the participant, and there is no requirement to be tied to the financial impact of COVID-19.
- Recontribution Right. The three-year recontribution right for otherwise eligible rollover distributions is available to an IRA or to an eligible employer plan (if the plan sponsor so allows), and the recontributed amount is treated as a rollover contribution.
- Rollover Notice. There is no 402(f) rollover notice requirement and there is no direct rollover right.
- Withholding and Reporting. The distribution is subject to 10% voluntary withholding and the entire amount is reported on 2020 Form 1099-R, using code 1 or 2 in box 7.
- Tax Treatment To Participants. The CRD is reported on Form 8915-E (still pending) to receive favorable tax treatment, including the recontribution rights. A participant or beneficiary that has a distributable event can take advantage of the favorable tax treatment on his tax return even if the plan sponsor does not offer CRDs. Moreover, a CRD will not be treated as a change in substantial equal periodic payments so there is no Code section 72(t) recapture tax.
- Timing of Plan Amendments. As set forth in the statute, plan sponsors have until the last day of the 2022 plan year (2024 plan year for governmental plans) to adopt plan amendments (unless these dates are extended).

Additional details on this guidance follow.

In General

In response to the pandemic, the CARES Act gave retirement plan participants greater access to their retirement savings by expanding plan loans and allowing for coronavirus-related hardship distributions. For “Qualified Individuals,” plan loan limits under the Code were increased from \$50,000 to \$100,000 (or 100% of vested account balance) through September 22, 2020, and certain plan loan payments due in 2020 could be suspended for up to a year. Also, a special distribution right was made available for up to \$100,000, at the plan sponsor’s election, for certain plans that provided favorable tax treatment for the distribution – including relief from the 10% additional tax under section 72(t), the ability to spread the taxes over three years, and right to recontribute the funds. The new guidance provides welcome relief in the following key areas.

Expanded Definition of “Qualified Individuals”

Notice 2020-50 expanded the definition of “Qualified Individuals” for the purpose of coronavirus-related distributions and loans to now include:

- Participants (and beneficiaries), their spouses or dependents diagnosed with COVID-19; or

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- Participants (or beneficiaries)—or their spouse or a member of their household (meaning a person who shares the principal residence) – who experiences adverse financial consequences as a result of the following due to COVID-19:
 - Quarantine
 - Furloughs
 - Lay offs
 - Rescinded or delayed job offers
 - Reduction in work hours or pay
 - Unable to work due to lack of childcare
 - Closing or reducing hours of a business owned or operated by such individual

A sample certification is also provided for use by plan administrators, who may rely on the certification, absent actual knowledge to the contrary. Notably, there is no duty to inquire whether an individual has satisfied the conditions.

Employer Safe Harbor for Plan Loans

The CARES Act permits a delay in certain plan loan repayments in light of COVID-19. Importantly, the Notice establishes the following safe harbor for employers who choose to offer coronavirus-related plan loan suspensions for Qualified Individuals:

- Loan from a qualified employer plan outstanding on or after March 27, 2020,
- The due date pursuant to Code section 72(p)(2)(B) or (C) for any repayment with respect to the loan occurs during the period beginning on March 27, 2020 and ending on December 31, 2020,
- The obligation to repay a plan loan is suspended under the plan for any period beginning not earlier than March 27, 2020, and ending not later than December 31, 2020 (suspension period),
- Loan repayments resume after the end of the suspension period (e.g., no later than January 1, 2021), and the term of the loan may be extended by up to 1 year from the date the loan was originally due to be repaid, and
- Interest accrued during the suspension period must be added to the remaining principal loan balance, which is satisfied if the loan is reamortized and repaid in substantially level installments over the remaining loan period (e.g., 5 years from the date of the loan, plus up to 1 year).

The IRS also recognized that other reasonable approaches may be used, and gave an example of another approach that delays reamortization (but not 2021 payments) beyond January 1, 2021.

Nonqualified Deferred Compensation Plan Relief

The Notice also provides important relief for participants with a deferral election under a NQDC plan. Specifically, it deems a CRD to be a hardship distribution for purposes of the 409A regulations rule (Treas. Reg. sec. 1.409A-3(j)(4)(viii)) that allows for the cancellation of an otherwise irrevocable deferral election under the NQDC plan if a participant receives a hardship distribution from the 401(k)

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plan. This cancellation results in the permissible accelerated payment of amounts that would have been deferred into the NQDC plan. The relief is available now, and does not require the higher level of scrutiny needed for an “unforeseeable emergency” distribution from such plan.

Next Steps

Plan sponsors and recordkeepers should review their existing policies and procedures (including distribution and loan forms) and update them accordingly in compliance with the Notice. A key takeaway is to update these materials for the expanded definition of Qualified Individual (and consider using the sample certification). If an existing loan suspension approach falls outside of the IRS safe harbor, a careful review of the approach is advisable. In addition, plan sponsors should review the terms of any NQDC plan to determine whether the cancellation of a deferral election is required upon a CRD. Of course, the Notice cannot, and does not, contemplate all possible situations (such as the interplay with Notice 2020-23 for loan suspensions), but it certainly provides a good starting point to address many issues.

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