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BENEFITS BRIEF

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Budget Act Includes Hardship and Other Important Retirement Plan Relief

The Bipartisan Budget Act of 2018 (HR 1892, "Budget Act") includes three tax relief provisions that didn't make the final cut in the Tax Cut and Jobs Act of 2017 (H.R. 1): (1) expanding 401(k) and 403(b) plan hardship distributions, (2) permitting the return to a plan of an excess federal tax levy, and (3) adding additional disaster relief for the California wildfires. The Budget Act also establishes a special Congressional committee to address the major funding concerns for multiemployer plans, their participants and the PBGC. These provisions are briefly summarized below.

Hardship Withdrawals. In-service distributions from 401(k) and 403(b) plans before a participant reaches age 59-1/2 are strictly limited. However, there is an exception for certain hardship distributions, including a safe harbor that most plans use.

Current Law: A number of rules apply to hardship distributions, including the following:

- to meet the safe harbor requirement that the distribution is deemed necessary to satisfy an immediate and heavy financial need, the participant (1) 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 (2) 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 6 months after receipt of the hardship distribution.

- hardship distributions are not available from the following sources: (A) qualified nonelective contributions (QNECs), (B) qualified matching contributions (QMACs), (C) safe harbor plan contributions, and (D) post-12/31/1988 earnings, including on pre-tax contributions.

What Changed: First, the Budget Act eliminates the long-standing requirement that a participant must first request all available plan loans before taking a hardship withdrawal. Specifically, a hardship distribution will not fail to be a hardship distribution solely because the employee does not take any available loan under the plan (or presumably other plans of the same employer).

Second, the Budget Act directs the Treasury Secretary to amend its 401(k) regulations to eliminate the 6-month suspension period for making new pre-tax (or Roth) 401(k) and after-tax contributions following a safe harbor hardship distribution.

Third, it expands the types of funds that can be distributed in the event of a hardship withdrawal under Code section 401(k) to include QMACs, QNECs, 401(k) safe harbor plan contributions, and earnings (including post-1988 earnings on elective deferrals).

When: Plan years beginning after 2018.

Impacted Plans: 401(k) and 403(b) plans that permit hardship distributions

Next Steps: Once implemented, these changes will simplify hardship administration and give participants in need more access to their accounts, so plan sponsors and third party administrators should update their hardship procedures before the 2019 plan year. We anticipate that these changes will apply equally to 403(b) plans that incorporate the 401(k) regulations by reference, but IRS guidance would be helpful to clarify the scope of these changes – and the impact if a plan sponsor chooses to retain the current more restrictive hardship provisions (or elects to retain the existing provisions for pre-2019 hardship distributions) (e.g., possible loss of safe harbor hardship status and/or loss of safe harbor 401(k) or 401(m) plan status).

These changes will also require plan amendments. For pre-approved plans, we anticipate plan amendments by next year, but individually designed plans will have more time, as there is the 2-year remedial amendment period after the items are listed on the Required Amendment List.

California Wildfires Disaster Relief. Code section 7508A (and related IRS Announcements) provides IRS authority to issue relief for natural disasters, and Congress also, on occasion, provides additional disaster relief for qualified plans.

Current Law: Announcement 2017-15 provides some limited relief for hardship and loans for victims of the California wildfires.

What Changed: Recently, Congress provided relief for hurricanes Harvey, Irma, and Maria, including from the 10% early withdrawal tax under Code section 72(t), permissible in-service distributions up to $100,000 with special tax relief to spread the taxation over 3 years, and increase of the loan dollar limits to $100,000 and 100% of the participant's account balance. The Budget Act provides nearly identical relief for victims of the 2017 California wildfires (actually through January 18, 2018).

Specifically, the Budget Act provides the following:

- Relief from 10% additional tax under Section 72(t) for early withdrawals of a "qualified wildfire distribution;"
- Relief from mandatory 20% withholding and 402(f) notice as the qualified wildfire distribution is not treated as an eligible rollover distribution;
- Permissible in-service distribution for a qualified wildfire distribution;
- Qualified wildfire distribution taxed over a three-year period;
- Recontribution of withdrawals after March 31, 2017 and before January 15, 2018 for California home purchases through June 30, 2018;

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- Increase 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 with up to a one-year delay for certain loan repayments; and

- Recontribution of a “qualified wildfire distribution” to an eligible retirement plan within three years.

For this purpose, a “qualified wildfire distribution” is a distribution of up to $100,000 from a Code section 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.

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 get an additional 2 years).

When: Effective February 9, 2018.

Impacted Plans: 401(a), 401(k), 403(b), governmental 457(b), IRA

Next Steps: Plan sponsors and recordkeepers should review their procedures for California wildfire relief, consider offering this additional relief, update distribution and reporting and withholding procedures, and (in the future) adopt an amendment reflecting the changes.

Improper Federal Tax Levy.

Current Law: Retirement plans generally prohibit the assignment or transfer of pension benefits in accordance with the Code’s anti-alienation provision of Code section 401(a)(13). However, there is an exception for federal tax levies.

What Changed: The Budget Act provides special relief for a qualified plan or IRA distribution that was made to comply with a federal tax levy that subsequently turns out to have been wrongful. To avoid taxation of the distribution and retain the tax-deferred status of the funds, the Budget Act permits an individual to avoid taxation by rolling back the funds (plus interest thereon) into the plan (if the plan sponsor accepts the funds) or to an IRA by the tax filing deadline (excluding extensions) for the year of the refund. (We note that this does not permit a tax-free rollover of non-Roth funds to a Roth IRA or a designated Roth account.)

When: Effective January 1, 2018.

Impacted Plans: 401(a), 401(k), 403(b), governmental 457(b), IRA

Next Steps: Plan sponsors should consider permitting these indirect rollovers into the plan, which (depending on the plan language regarding rollover contributions) may require a plan amendment.

Multiemployer Pension Plan Relief.

Current Law: Multiemployer plans and the PBGC’s multiemployer insurance program face serious fiscal challenges.

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What Changed: Congress took important first steps to address solvency concerns for the multiemployer pension system by creating a bipartisan committee to improve the solvency of multiemployer pension plans and the PBGC. The new House and Senate Joint Select Committee on Solvency of Multiemployer Pension Plans (the "Committee") is tasked with the goal of providing recommendations and legislative language to improve the solvency of multiemployer plans and the PBGC. The structure of the Committee includes:

- ***Membership.*** The Committee will consist of 16 members: 8 Senators and 8 members of the House appointed by the party leaders, divided equally between Republicans and Democrats (*i.e.*, 4 Senate Republicans and 4 Senate Democrats; 4 House Republicans and 4 House Democrats).

- ***Co-Chairs.*** There are two co-chairs, one Republican appointed by the Speaker and Majority Leader and one Democrat appointed by the Minority Leaders. The co-chairs are Senator Hatch (R-UT) and Senator Brown (D-OH) respectively.

- ***Appointments.*** The Committee members and co-chairs were appointed late on February 27. The Committee must hold its first meeting within 30 days of enactment.

- ***Meetings.*** The Committee must hold at least 5 public meetings or public hearings, and at least 3 public hearings (which may include field hearings).

- ***Staffing and Funding.*** Congressional staff may by detailed to the Committee and the co-chairs will appoint a staff director. The agencies may provide technical assistance on written request. $500,000 is authorized to pay expenses.

- ***Report.*** Not later than November 30, 2018, the Committee must vote on a report containing detailed findings and recommendations and proposed legislative language. The report and language are only approved if a majority of the Republicans (5/8) and a majority of the Democrats (5/8) on the Committee vote in favor. Dissenting members can file minority views.

- ***Termination.*** The Committee terminates on December 31, 2018 (or 30 days from submission of its report and recommendations, if earlier).

Once the Committee approves the report, the process to Congressional consideration is as follows:

- Within 15 days after its approval, the report and legislative language must be submitted to the President, Vice President, Speaker, and Majority and Minority Leaders. It will then be introduced the next day the Senate is in session by the Majority Leader or his designee and will be jointly referred to the Finance and Health, Education, Labor, and Pension ("HELP") Committees.

- The Finance and HELP Committees must report the bill without revisions and with a favorable or unfavorable recommendation (or no recommendation) within 7 session days after bill introduction.

- Within 2 session days after the bill is reported by the Finance and HELP Committees, it will be in order for the Majority Leader to move to proceed for consideration of the bill.

- There is a limit of 10 hours (equally divided) of debate on the motion to proceed.

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- By the last day of the 115th Congress, the Senate must vote on a motion to proceed to consideration of the bill.

Notably, 60 votes are still required to pass the motion to proceed (but all points of order and motions to postpone are not in order/waived).

When: Effective immediately.

Impacted Plans: Multiemployer pension plans

Next Steps: Stakeholders in the multiemployer system may wish to submit their views about potential legislation to the Committee and participate in the upcoming hearings.

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