IRS Issues Guidance Implementing Coronavirus-Related Retirement Plan Provisions Under the Cares Act

The IRS has issued IRS Notice 2020-50 (the Notice) providing guidance implementing the retirement plan provisions of the Coronavirus Aid, Relief, and Economic Security Act (the CARES Act) that was enacted on March 27, 2020. A summary of the key provisions of the CARES Act affecting qualified retirement plans and a summary of the guidance implemented by the Notice follows.

New 401(k), 403(b) and 457(b) Distributable Event

The CARES Act created a new distributable event for qualified retirement plans, such as 401(k), 403(b), and 457(b) plans to allow plan distributions to qualified individuals who: (i) are diagnosed with COVID-19, (ii) have a spouse or dependent who is diagnosed with COVID-19, or (iii) experiences adverse financial consequences as a result of being quarantined, furloughed, laid off, having work hours reduced, being unable to work due to lack of child care due to COVID-19, or closing or reducing hours of a business owned or operated by the individual due to COVID-19 (a qualified individual). Distributions made on account of these events can be up to $100,000, will not be subject to the 10 percent early withdrawal penalty, and will be subject to income tax, but, at the election of the participant, can be subject to tax over three years rather than the entire distribution being subject to tax in the year of the distribution (a coronavirus related distribution).

The Notice expands the definition of a qualified individual to include an individual who experiences adverse financial consequences as a result of: (i) the individual having a reduction in pay or has a job offer rescinded or start date for a job delayed due to COVID-19, or (ii) the individual's spouse or member of the individual's household experiencing one of the previously listed event events causing eligibility for a coronavirus related distribution.

The Notice clarifies that a participant or beneficiary may designate all or any portion distribution received from a qualified retirement plan between January 1, 2020, and December 31, 2020, as a coronavirus related distribution up to the $100,000 limit, even if the distribution was not recognized by the employer as a coronavirus related distribution or was taken prior to the enactment of the CARES Act. The Notice also adds that if a qualified individual dies before the full taxable amount of the coronavirus related distribution has been included in their gross income, then the remainder must be included in their gross income for the taxable year that includes the individual's death. Importantly, the Notice also indicates that employers sponsoring qualified retirement plans can rely on a participant's certification indicating that they are qualified individuals, alleviating the need for receiving evidence of an employee's financial circumstances.

Individuals who receive a coronavirus related distribution may also repay all or any part of the distribution to an eligible retirement plan within three years of the distribution via a rollover that would make the original distribution non-taxable. The Notice indicates that if a qualified individual includes a coronavirus related distribution in their gross income and then recontributes the distribution to an eligible retirement plan after they file their federal income tax return for the year of the distribution, the qualified individual will need to file an amended federal income tax return for the year of the distribution to recoup the taxes paid on the distribution.

Increased Loan Availability and Suspension of Existing Loan Repayments

The CARES Act raised the maximum loan amount that a qualified individual could receive from a qualified retirement plan from 50 percent of a participant's vested balance, up to $50,000, to 100 percent of a participant's vested balance, up to $100,000, for loans taken between March 27, 2020, and September 22, 2020. In addition, employers are permitted, but not required to delay all

Related Practice Areas

- Employee Benefits & Executive Compensation required repayments from qualified individuals to be made for one year following receipt of the loan. This permitted delay in requiring loan repayments includes loans that were issued prior to March 27, 2020, but were outstanding between March 27, 2020, and December 31, 2020. An employer who elects receiving loan repayments should then adjust all subsequent loan repayments to reflect the one year delay.

The Notice provides a safe harbor, under which a qualified retirement plan will be treated as satisfying the loan requirements of the Internal Revenue Code if a participant's obligation to repay a loan is suspended for any period that begins not earlier than March 27, 2020, and ends not later than December 31, 2020. Under the safe harbor, loan repayments must resume immediately after the suspension period, and the term of the loan may be extended by up to one year from the date the loan was originally due to be repaid. The safe harbor requires that interest accruing during the suspension period be added to the remaining principal of the loan and repaid according to the loan's amortization schedule following the end of the suspension period.

Cancellation of Deferral Election under Nonqualified Deferred Compensation Plans

The Notice indicates that a nonqualified deferred compensation plan that is subject to Section 409A of the Internal Revenue Code may allow service providers to cancel their deferral elections made under the plan if the service provider receives a coronavirus related distribution from a qualified retirement plan. Participants who elect to cancel their deferral election must cancel their election in full and cannot postpone or otherwise delay their deferrals into the plan. The deferral election must be cancelled, not only postponed or otherwise delayed.

Other CARES Act Retirement Plan Provisions Not Affected by the Notice

In addition to the provisions described above, the CARES Act waived all required minimum distributions from qualified retirement plans and individual retirement accounts (IRAs) for all purposes for calendar year 2020. The CARES Act also provided employers with single employer defined benefit pension plans with funding relief by indicating that no pension contributions must be made until January 1, 2021. The Notice did not provide guidance on the implementation of the delay in required minimum distributions or defined benefit funding changes under the CARES Act. We will have to wait and see if future IRS announcements provide separate guidance on those issues.