AIG Retirement Services

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PLAN SPONSOR UPDATE: IRS CARES Act guidance impacts participant eligibility and rollovers

The IRS recently issued guidance (Notices 2020-50 and 2020-51) addressing the distribution, loan and required minimum distribution (RMD) waiver provisions of the Coronavirus Aid, Relief, and Economic Security (CARES) Act.

The Notices help retirement plan participants affected by the COVID-19 coronavirus take advantage of the CARES Act provisions providing enhanced access to plan distributions and plan loans and provide guidance on the waiver of RMDs for 2020 as part of the CARES Act and on certain similar issues under the Setting Every Community Up for Retirement Enhancement Act (SECURE Act) of 2019.

Most significantly, the IRS guidance expands the categories of individuals eligible for the CARES Act distribution and loan provisions and provides additional rollover relief with respect to waived RMDs and certain related payments.

Eligible individuals

As expanded, a "qualified individual" now includes an individual who experiences adverse financial consequences as a result of:

- the individual, the individual's spouse or a member of the individual's household's (defined as someone who shares the individual's principal residence) having a reduction in pay (or self-employment income) due to COVID-19 or having a job offer rescinded or start date for a job delayed due to COVID-19;
- the individual's spouse or a member of the individual's household's being quarantined, furloughed or laid off; having work hours reduced due to COVID-19 or being unable to work due to lack of childcare due to COVID-19; or
- the closing or reduction in hours of a business owned or operated by the individual's spouse or a member of the individual's household due to COVID-19.

Rollover relief

The guidance extends the 60-day rollover period for certain distributions from plans to August 31, 2020. The extended rollover period applies only with respect to distributions in 2020 that would have been RMDs in 2020 but for (1) the CARES Act waiver of 2020 RMDs, or (2) the SECURE Act extension of the required beginning date ("RBD") to age 72.

The guidance also confirms (or re-confirms in some cases) the following:

Effective dates

Coronavirus-related distributions (CRDs) can be made (or distributions can be treated as CRDs) from January 1, 2020, through December 30, 2020. Thus, a distribution taken on December 31, 2020 cannot be treated as a CRD. The guidance reaffirms the deadline of September 22, 2020, for a participant loan utilizing the increased loan limits.

CARES Act provisions optional

Employers can choose whether and to what extent to implement the CARES Act CRD and loan rules, and qualified individuals can claim the tax benefits of a CRD even if plan provisions are not changed.

Self-certification

The administrator of an eligible retirement plan may rely on an individual's certification that the individual satisfies the conditions to be a qualified individual in determining whether a distribution is a CRD, unless the administrator has actual knowledge to the contrary. The requirement that an administrator not have "actual knowledge" that is contrary to an individual's certification does not mean that the administrator has an obligation to inquire into whether an individual has satisfied one of the conditions to be a qualified individual. Rather, this requirement is limited to situations in which the administrator already possesses sufficiently accurate information to determine the veracity of a certification.

Distributions that can and cannot be treated as CRDs

A qualified individual is permitted to designate any distribution that would meet the requirements of a CRD as a CRD without regard to whether the plan treated the distribution as a CRD, including periodic payments and distributions that would have been required minimum distributions (RMDs) but for the CARES Act RMD waiver; any distribution received by a qualified individual as a beneficiary; and a reduction or offset of a qualified individual's account balance in order to repay a plan loan, including a qualified plan loan offset. However, the following cannot be treated as a CRD: defaulted loans that are treated as deemed distributions; corrective distributions of amounts exceeding contribution limits or due to nondiscrimination testing and distributions that are permissible withdrawals from an eligible automatic contribution arrangement.

CRD limit

The total amount of distributions treated by an employer as CRDs under all its retirement plans (including plans within an employer's control group) with respect to a qualified individual is not permitted to exceed $100,000; however, a plan will not fail to satisfy any Code requirement merely because a qualified individual's total CRDs exceed $100,000 taking into account distributions from IRAs or other eligible retirement plans maintained by unrelated employers.

Financial need

The definition of a CRD under the CARES Act does not limit these distributions to amounts withdrawn solely to meet a need arising from COVID-19. So, unlike hardship distributions, CRDs can be made regardless of an individual's need for funds.

Re-contribution of CRDs

If a CRD is eligible for tax-free rollover treatment, a qualified individual is permitted, at any time in the three-year period beginning the day after the date of a CRD, to recontribute any portion of the distribution, but not an amount in excess of the amount of the distribution, to an eligible retirement plan. As with any rollovers into an eligible retirement plan, the plan administrator accepting the re-contribution of a CRD must reasonably conclude that the re-contribution is eligible for direct rollover treatment under the CARES Act. For this purpose, the guidance provides that the administrator of an eligible retirement plan may rely on an individual's certification that the individual satisfies the conditions to be a qualified individual in determining whether a distribution is a coronavirus-related distribution, unless the administrator has actual knowledge to the contrary. Any CRD paid to a qualified individual as a beneficiary of an employee (other than the surviving spouse of the employee) cannot be recontributed.

Loan payment deferrals and re-amortization

Under the CARES Act, a qualified individual's obligation to repay a plan loan may be suspended under the plan for any period beginning not earlier than March 27, 2020, and ending not later than December 31, 2020 (suspension period); the guidance provides employers a safe harbor procedure for implementing this suspension of loan repayments otherwise due through the end of 2020, while recognizing there may be other reasonable ways to administer the loan re-amortization.

Under the safe harbor procedure, the loan repayments must resume after the end of 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. Interest accruing during the suspension period must be added to the remaining principal of the loan. The loan is re-amortized and repaid in substantially level installments over the remaining period of the loan (that is, five years from the date of the loan, assuming that the loan is not a principal residence loan, plus up to one year from the date the loan was originally due to be repaid).

Nonqualified deferred compensation

Generally, once a participant makes an election to defer compensation into a nonqualified deferred compensation plan that is subject to Code section 409A, that election must be irrevocable for the next year. However, a participant's deferral election may be cancelled due to an unforeseeable emergency or a hardship distribution. The guidance provides that if a participant receives a distribution from an eligible retirement plan that constitutes a CRD, that distribution will be considered a hardship distribution for this purpose and, as a result, the participant's deferral election may be cancelled (but not postponed or otherwise delayed).

Substantially equal periodic payments

Distributions from retirement plans that are part of a series of substantially equal periodic payments ("SEPPs") cannot be rolled over. The guidance, however, provides that SEPPs can be rolled over if they include 2020 RMDs. For this purpose, 2020 RMDs are either distributions paid in 2020 that would have been RMDs but for the CARES Act waiver or distributions paid in 2021 for the 2020 calendar year (addresses situations where an individual's required beginning date ("RBD") is April 1, 2021).

However, the RMD waiver for 2020 does not operate to permit the cessation for 2020 of distributions being made under the "RMD method" that are designed to satisfy the SEPP exception to the 10% penalty tax. So, while the guidance permits SEPPs to be rolled over, the rollover of payments that are being made to satisfy the SEPP exception to the 10% penalty tax will result in a modification that could trigger the recapture of the penalty tax.

Extension of deadlines

The deadline for electing whether to take post-death RMDs under the five-year rule or the life expectancy rule normally is now the end of the calendar year following the calendar year of the death of the participant. The guidance clarifies that if this deadline otherwise is the end of 2020, it is extended to the end of 2021.

Also, if a plan participant died in 2019, and the five-year rule applies to a benefit under the plan, the time prescribed for a non-spouse beneficiary to roll over the benefit tax-free directly to an inherited IRA and elect to take distributions under the life expectancy rule is extended from the end of the calendar year following the year of death (2020) to the end of 2021.

Deadlines not extended

These RMD-related deadlines are not extended: the five-year period or the 10-year period if a participant or beneficiary dies in 2020; the September 30 deadline relating to the determination of designated beneficiaries; the October 31 deadline relating to the date by which the trustee of a trust that is a plan's designated beneficiary must provide the plan administrator certain information, or the last-day-of-the-year deadline relating to the date by which separate accounts must be established.

Defined benefit plans

The RMD waiver does not apply to defined benefit plans, even if the plan is making a lump-sum distribution in 2020.