Rael & Letson

SUMMARY OF THE CORONAVIRUS AID, RELIEF

AND ECONOMIC SECURITY ACT ("CARES ACT")

On March 27, 2020, the President signed the Coronavirus Aid, Relief and Economic Security Act ("CARES Act") into law. The new law is intended to provide broad relief to address the impact of COVID-19. While the CARES Act impacts many parts of the economy, there are three key provisions that target retirement plans and IRAs. Following is a high-level summary of these key retirement provisions from the CARES Act along with our observations and conclusions.

Coronavirus-Related Distribution ("CRD")

A CRD is an elected plan distribution designation created under the CARES Act to provide the possibility of temporary financial relief from COVID-19 to individuals with retirement funds through *additional fund access* and *favorable tax treatment*. A CRD can be designated within any eligible retirement plan (generally any qualified DC plan, qualified DB plan, or IRA) that allows this type of distribution.

Rael & Letson Observation: Your plan will need to recognize CRDs in order for participants to gain relief.

What distributions can be designated as CRDs?

- CRDs are only those paid to "affected individuals". An "affected individual" is someone who:
    - Is diagnosed with COVID-19,
    - Has a spouse or dependent who is diagnosed with COVID-19, or
    - As a result of COVID-19, experiences adverse financial consequences due to quarantine, being furloughed or laid-off, inability to work due to lack of childcare, reduced working hours, business closure, or other factors as determined by the Secretary of the Treasury.

- The distribution must be made on or after January 1, 2020 and before December 31, 2020.

- The distribution can be any amount up to the lesser of $100,000 or the account balance.

- The maximum distribution of $100,000 is aggregated across all retirement plans and IRAs.

- Only those distributions that are eligible for rollover.

Rael & Letson Observations: Really only applies to DC plans and IRAs since annuity payments cannot be rolled over. Since the plan administrator may rely on the employee's certification as an "affected individual", it is likely that most all DC plans would allow participants to self-certify. Also, qualified plans can limit CRDs to less $100,000, if plan sponsors want to impose stricter limits on access to retirement funds.

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What additional access to retirement funds can be provided?

- In-service distributions in certain defined contribution plans— Qualified Plans other than Pension Plans can be amended to allow CRDs without a termination of employment during 2020.

- Earlier access from certain defined contribution plans while not working—Plans typically require termination of employment with no or low hours for an extended period of time before funds are available. In recognition that furloughs and reduced hours can create a need for temporary fund access, any qualified DC plan can temporarily loosen distribution eligibility requirements. For example, making CRDs available after any month in 2020 in which no hours are worked.

Rael & Letson Observations: Temporary in-service relief does not currently apply to Money Purchase funds. As a result, Money Purchase Plans (including Money Purchase funds within Profit-Sharing Plans) may need to rely on other ways to provide needed short-term relief to participants. Allowing CRDs is optional, thus some Plan Sponsors may not want to provide in-service relief to limit retirement savings leakage.

What is the favorable tax treatment?

- CRDs are **not subject to the 10% early distribution** penalty normally assessed on distributions before age 59 ½. They are, however, subject to 10% Federal tax withholding and any State tax withholding unless waived by the participant.

- Unless the participant elects to have the distribution included as gross income for such taxable year, **taxes** associated with the distribution will be **spread ratably over a 3-year period** beginning with such taxable year.

- **CRDs can be repaid** in one or more contributions to an eligible retirement plan within three years of taking the distribution. CRDs that are repaid within three years will be treated as a rollover contribution to such eligible retirement plan.

Rael & Letson Observation: Because of the repayment options, administration effects are not yet clear. To avoid complication, it may be best to only allow CRDs on pre-tax funds (401(k) deferrals and employer contributions). There should be ample time to address repayment administration.

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Plan Loans

Defined Contribution plans **can** provide loans to affected individuals up to the lesser of $100,000 or their vested account balance between March 27, 2020 and September 23, 2020 (180-day period). This provision temporarily increases the limit on plan loans from $50,000 to $100,000.

- Eligibility criteria for an "affected individual" is the same criteria used for CRDs.

- Affected individuals with existing loans from a qualified plan can delay any repayments of such loans that are due between March 27, 2020 and December 31, 2020 by one year of such due date. The delayed payment period is disregarded for calculating the loan repayment period, which is generally five years unless the loan was used to acquire the participant's principal residence.

Rael & Letson Observation: For plans that currently provide loans, this provision can be used to give participants with outstanding loans short-term payment relief, and/or temporarily increase the available amount under their existing loan provisions. This may also provide an opportunity for plans without loan provisions to permanently introduce loans.

Required Minimum Distributions ("RMDs")

RMDs for 2020 are waived for all defined contribution plans. Waiver does not apply to defined benefit plans.

Rael & Letson Observation: There was a waiver in 2009 with similar timing. The most common response was to continue scheduled distributions to retirees through year end unless the participant elected otherwise. This approach may again be best practice. We understand that those who have already taken first time DC plan RMDs may roll over their distribution to an IRA within 60 days to avoid having it treated as a taxable distribution. It is not clear whether plans can allow participants to return RMDs received in 2020.

Concluding Remarks: These are Rael & Letson's preliminary interpretations of the CARES Act. IRS regulation is pending that will provide clarification on final rules for application of this law. These regulations are expected in the next few weeks. That said, time to act is now. Because relief needs are over the very short term, it is recommended that sponsors discuss potential needs and parameters around those needs. That way, approval can be swift once regulations are available. If action is taken, communication will need to be responsive. Sponsors, however, have until the end of the first plan year beginning on or after January 1, 2022 to amend their plans.