

## Labor and Employment Alert: CARES Act and Retirement Plan Changes

Among the many changes made by the CARES Act, there are a few that can be expected to have a significant impact on participants in tax-qualified retirement plans, such as 401(k) plans, 403(b) tax-deferred annuity plans, profit sharing and pension plans, and the employers that sponsor such plans, as well as individual retirement accounts (IRAs). Qualified retirement plans provide benefits to employees that are generally paid after they terminate employment. Distributions to participants while they are working are generally prohibited, except, if the plan so provides, in the event of a participant's hardship or attainment of age 59  $\frac{1}{2}$ .

The CARES Act, in light of the significant adverse health and financial impact caused by the COVID-19 virus, seeks to liberalize certain plan and IRA distribution rules to provide participants and IRA owners greater access and control over their accounts under such plans and IRAs. To the extent the following CARES Act changes are implemented, appropriate plan amendments will need to be timely adopted. We expect interpretive guidance to be issued by the IRS in the near future concerning these CARES Act changes.

### **Pension Plan Funding**

In an effort to help tax-qualified pension plans and their employer plan sponsors, the CARES Act provides that any minimum required contribution which would be due during 2020 shall instead be delayed until January 1, 2021. However, the amount of any such deferred pension contribution will be increased by interest (at the plan's effective interest rate for the plan year that includes January 1, 2021) for the period between the original contribution due date and the payment date.

Further, defined benefit pension plans are subject to benefit payment restrictions if the plan is not adequately funded in accordance with certain IRS guidelines. Under the CARES Act, in calculating the plan's funded percentage for 2020, a plan sponsor may elect to use the plan's funded percentage for 2019, in lieu of using the plan's 2020 funded percentage, for purposes of applying the benefit payment restrictions for 2020. In light of the downturn in the financial markets in 2020 due to the COVID-19 virus, using a plan's 2019 funded percentage, instead of the 2020 funded percentage, should help minimize the impact of the funding-based benefit restrictions under defined benefit pension plans for 2020.

### **Expanded Distribution Rights**

Under the CARES Act, an eligible participant may, if the plan or IRA so provides, elect to receive a distribution from the plan or IRA during 2020, even if, in the case of an employer-provided qualified retirement plan, the participant is still working. An eligible participant (referred to as a "Qualified Individual") is an individual (i) who is diagnosed with the COVID-19 virus pursuant to an approved CDC test; (ii) whose spouse or dependent is diagnosed with the COVID-19 virus pursuant to an approved test; or (iii) who experiences adverse financial consequences as a result of being quarantined, being furloughed or laid off or having work hours reduced due to the COVID-19 virus, being unable to work due to a lack of child care due to the COVID-19 virus, closing or reducing hours of a business owned or operated by the individual due to the COVID-19 virus, or other factors as determined by the IRS.

The distribution is subject to special federal income tax rules. The distribution amount for any Qualified Individual from all retirement accounts may not exceed, in the aggregate, \$100,000. Unless the individual elects otherwise, the distribution shall be included in the individual's income ratably over three taxable years beginning with the 2020 taxable year. Thus, if, for example, a qualified individual receives a \$30,000 distribution in 2020, then \$10,000 will be included in the participant's income in each of the 2020, 2021, and 2022 taxable years, unless the individual elects to include the full distribution amount in income in 2020. Further, such distribution is not subject to the additional 10% early distribution tax that generally applies to plan or IRA distributions before age 59  $\frac{1}{2}$ .

In addition, a participant who receives a CARES Act qualifying distribution may repay all or any portion of the distribution during the three-year period beginning on the day after the date the distribution was received to a qualified retirement plan or IRA of which the individual is a beneficiary and to which a rollover contribution can be made. Future IRS guidance will be needed to determine the appropriate tax treatment for any such repayment amounts.

**Expanded Plan Loan Rights**

Loans from a participant's qualified plan account will be taxable to the participant unless certain tax law requirements are met, including a requirement that the amount of all outstanding plan loans not exceed the lesser of \$50,000 or 50% of the participant's vested account balance. The CARES Act liberalizes those plan loan limits during the 180-day period beginning on the date of enactment of the CARES Act (i.e., March 27, 2020) by increasing the plan loan amount limit, for a plan loan during such period to a Qualified Individual, to the lesser of \$100,000 or 100% of the participant's vested account balance. In addition, in the case of a plan loan outstanding for a Qualified Individual on or after March 27, 2020, if the due date for any payment under such loan occurs during the period March 27, 2020 through December 31, 2020, such due date is delayed for one year. In such case, subsequent loan payments shall be appropriately adjusted to reflect the payment due date deferral.

**Required Minimum Distribution Waiver**

Generally, benefits under a qualified retirement plan or IRA must commence to be paid after the participant or IRA owner attains a certain age (generally age 70 ½, which has recently been increased to age 72). Failure to make these required minimum distributions (RMD) will subject the participant or IRA owner to substantial tax penalties. Under the CARES Act, the RMD requirements are waived for calendar year 2020 with respect to qualified defined contribution plans (such as 401(k), 403(b), and governmental 457(b) plans), and IRAs. This RMD waiver applies to, among others, those participants whose required beginning date occurred in 2020 (i.e., attained age 70 ½ in 2019), but who did not receive the RMD with respect to such required beginning date in 2019. This RMD waiver for 2020 should be helpful to plan participants and IRA owners in that it offers them the ability to not have to liquidate their account balances to pay the RMD at a time when financial markets are experiencing substantial losses in value.

We are here for you. If you have any questions about this alert, or any other labor and employment issue, please contact:

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