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# Delving into CARES Act relief for retirement plan participants

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The Coronavirus Aid, Relief, and Economic Security (CARES) Act ([Pub. L. No. 116-136](#)) makes it easier for retirement plan participants affected by the pandemic to use their savings to regain their financial footing. For affected participants, the act lets defined contribution (DC) plans offer special in-service “coronavirus-related distributions,” doubles the maximum loan amount plans can make and allows suspension of loan repayments for the remainder of 2020. IRS has yet to issue any guidance on the CARES Act’s retirement provisions. However, IRS [Notice 2020-92](#) provides guidance on essentially identical relief under the Katrina Emergency Tax Relief Act (KETRA) of 2005 ([Pub. L. No. 109-73](#)). Absent any later guidance to the contrary, employers may look to that notice for direction. The CARES Act also waives all required minimum distributions from DC plans in 2020 (see [SECURE, CARES acts change rules on required minimum distributions](#) (April 7, 2020)).

## Participants eligible for relief

The CARES Act’s retirement plan relief is available to a “qualified individual,” defined as a participant who meets any of the following:

- Is diagnosed with SARS-CoV-2 or COVID-19 with a test approved by the Centers for Disease Control and Prevention
- Has a spouse or dependent diagnosed with SARS-CoV-2 or COVID-19

- Experiences adverse financial consequences from being quarantined, furloughed or laid off; having work hours reduced; being unable to work due to lack of child care; closing or reducing the hours of a business owned or operated by the individual; or from other factors, as determined by the Treasury secretary

Self-certification allowed. The act makes clear that plan administrators can rely on a participant's self-certification of eligibility for relief (although administrators shouldn't rely on a participant's self-certification if they have knowledge to the contrary). The act doesn't require written certification, so participants apparently can certify their eligibility over the phone. Employers still might consider requiring written confirmation of the participant's eligibility (for example, with completed distribution forms), even after a participant has provided oral certification.

Financial consequences for spouses. The act does not state that an employee is a qualified individual if the employee's spouse experiences any of the adverse financial consequences listed above. Whether Congress intended this omission is unclear. Even if an employee isn't furloughed or laid off, the loss of a spouse's income can put significant financial strain on a family. Guidance from the Treasury Department or IRS could expand the financial criteria to include adverse financial consequences due to changes in a spouse's work. However, in the absence of any guidance, employers should consult with legal counsel before providing relief to a participant solely because the participant's spouse experiences adverse financial consequences but does not have a SARS-CoV-2 or COVID-19 diagnosis.

## Coronavirus-related distributions

The CARES Act allows a qualified individual to treat up to \$100,000 in distributions received from an eligible retirement plan anytime in 2020 as a "coronavirus-related distribution." An "eligible retirement plan" has the same meaning that applies for plan rollovers and includes 401(a) qualified plans, 403(a) annuity plans, 403(b) plans and governmental 457(b) plans, as well as IRAs.

### In-service distributions allowed

The CARES Act allows — but does not require — employers to offer special in-service coronavirus-related distributions to qualified individuals until Dec. 31, 2020. The distributions can be made from most sources in a participant's account. Ordinarily, 401(k), 403(b) and 457(b) plans can distribute elective deferrals only after certain events — for example, termination of employment, death or disability. Coronavirus-related distributions are deemed to satisfy these requirements, which allows plans to distribute deferrals to qualified individuals who haven't had any of the usual distribution events.

## Favorable tax treatment

A coronavirus-related distribution is taxable to the participant, but on more favorable terms than the requirements that ordinarily apply to retirement plan distributions:

- The 10% penalty on distributions before age 59-1/2 doesn't apply.
- Distributions are taxed ratably over three years, unless participant elects full taxation in 2020.
- The mandatory 20% withholding on eligible rollover distributions doesn't apply. Instead, the withholding rules for other distributions apply, unless the participant elects no withholding.
- Employers don't have to provide a 402(f) rollover notice.

Distributions from Roth accounts. Distributions from designated Roth accounts after a participant attains age 59-1/2, dies or becomes disabled are tax-free if made more than five years after the participant's first contribution to the Roth account. If a distribution occurs before the participant satisfies these requirements, the participant must pay tax on the earnings portion of the distribution. The CARES Act does not make an exception for coronavirus-related distributions from Roth accounts. This presumably means that a qualified individual who takes a coronavirus-related distribution from a Roth account before satisfying the tax-free distribution requirements will owe taxes on the earnings — but under the more-favorable rules for coronavirus-related distributions.

## \$100,000 cap

The \$100,000 cap on coronavirus-related distributions applies to all eligible retirement plans — including employer plans and IRAs — in which the qualified individual has an account.

Example. Tom is a participant in his employer's 401(k) plan and also has an IRA. Tom tests positive for COVID-19. He can take coronavirus-related distributions until Dec. 31, 2020, from both his 401(k) plan account and his IRA. However, his total of 401(k) and IRA distributions cannot exceed \$100,000.

An employer is responsible for ensuring that a qualified individual takes no more than \$100,000 in coronavirus-related distributions from all plans in the employer's controlled group. However, employers do not have to determine whether a qualified individual has taken distributions from an IRA or a plan outside the controlled group that count toward the \$100,000 cap.

## Repayment allowed

The act allows — but doesn't require — a qualified individual to repay all or part of a coronavirus-related distribution. Repayments are treated as rollover contributions (the usual 60-day rollover deadline is deemed to be satisfied), so qualified individuals can repay their distributions to any employer-sponsored

plan that accepts rollovers or to an IRA. If a qualified individual takes an in-service coronavirus-related distribution and then terminates employment, the individual can repay the distribution to the employer's 401(k) plan if it accepts rollovers from former employees. If not, the individual can roll the distribution over to an IRA.

The total amount repaid cannot exceed the amount of the distribution (meaning the distributions can't be repaid with interest). Qualified individuals have three years from the day after receiving a coronavirus-related distribution to repay it. If a qualified individual takes more than one coronavirus-related distribution, then each distribution has its own three-year repayment period.

Example. Rita contracts COVID-19 from her husband, Tom. She takes a \$50,000 coronavirus-related distribution from her 401(k) plan on May 1, 2020. Rita has until May 2, 2023, to repay the distribution. She takes another \$50,000 coronavirus-related distribution from the 401(k) plan on July 1, 2020. Rita has until July 2, 2023, to repay the second distribution.

### Other distributions can be treated as coronavirus-related

The CARES Act allows treating virtually any 2020 plan distribution as coronavirus-related. For example, if an employer has layoffs this year, distributions under the plan's regular distribution provisions for terminated employees can be coronavirus-related.

Plan loan offsets. A plan loan offset occurs when a participant has a loan outstanding at the time of a distribution. The plan offsets the participant's account by the remaining loan balance to satisfy the participant's repayment obligation. The offset amount is a taxable distribution to the participant and an eligible rollover distribution subject to the usual 60-day rollover period. However, if the distribution is made upon the participant's termination of employment, the participant has until the tax filing deadline for the year in which the offset occurred to roll over the offset amount.

In the past, IRS has allowed plan loan offsets to be treated as qualified disaster distributions (under Notice 2005-92 and the instructions to the [2018 Form 8915B](#) for qualified disaster distributions). So loan offsets made this year to qualified individuals should be treated as coronavirus-related distributions. This would give qualified individuals three years to roll over offsets occurring this year.

Defined benefit (DB) plans. DB plans can distribute benefits after a participant's employment has ended. In-service distributions are also allowed, but only to participants who have reached age 59-1/2. The CARES Act does not make an exception to these requirements for coronavirus-related distributions. For past disasters, IRS has said DB plans cannot allow in-service distributions to disaster victims merely because the distribution, if made, would qualify as a disaster distribution. The same restriction continues to apply to coronavirus-related distributions.

However, if a participant has a permissible distribution event in 2020, then the participant can treat payments received this year as coronavirus-related. For example, if a DB plan allows in-service distributions at age 59-1/2, the plan can allow a qualified individual who is least that age to take a distribution and treat it as coronavirus-related. A terminated employee likewise can take a lump sum distribution in 2020 and treat up to \$100,000 as coronavirus-related (with excess amounts subject to mandatory 20% withholding and full taxation).

Limits on repayment. Although most 2020 distributions can be coronavirus-related, repayment is allowed only for distributions that would be eligible rollover distributions regardless of the relief. For example, a qualified individual can treat periodic annuity payments in 2020 as coronavirus-related distributions, but the individual can't repay those amounts since periodic payments aren't eligible rollover distributions. Notice 2005-92 and the instructions to 2018 Form 8915B confirm this treatment for periodic payments.

Distributions that can't be coronavirus-related. Notice 2005-92 states that certain distributions can't be treated as disaster distributions, including:

- Deemed distributions of plan loans that violate Internal Revenue Code Section [72\(p\)](#)
- Distributions of excess contributions under Section [415](#)
- Distributions of excess elective deferrals under Section [402\(g\)](#)
- Distributions to correct ADP and ACP nondiscrimination testing failures
- Dividends paid on employer securities
- Costs of current life insurance protection

These payments should also be ineligible for coronavirus-related distribution treatment.

### Hardship distributions distinguished

Coronavirus-related distributions aren't subject to the rules for hardship distributions. So employers offering in-service coronavirus-related distributions don't have to require that qualified individuals show they have an immediate and heavy financial need and are requesting only the amount necessary to meet that financial need.

Nonetheless, employers that want to discourage unnecessary withdrawal of retirement savings can choose to offer coronavirus-related distributions under a plan's hardship distribution provisions. In this case, employees would have to show that they are qualified individuals, have an immediate and heavy financial need, and are limiting the distribution request to the amount necessary to meet that need. If an

employee satisfies these requirements, then the hardship distribution would receive the favorable tax treatment that applies to coronavirus-related distributions.

Even though hardship distributions aren't usually eligible rollover distributions, an employee should be able to repay a coronavirus-related hardship distribution. Notice 2005-92 allowed Hurricane Katrina victims to repay hardship distributions treated as qualified hurricane distributions, specifically noting that the prohibition on rolling over hardship distributions didn't apply. IRS presumably will take the same position on coronavirus-related hardship distributions.

## Increased plan loan limit

The CARES Act allows — but does not require — plans to make loans to qualified individuals up to the lesser of \$100,000 or the individual's entire vested benefit (instead of the usual cap equal to the lesser of \$50,000 or 50% of the vested benefit). This increased loan cap is available until Sept. 22, 2020. Other rules for plan loans are unchanged. For example, a qualified individual who takes a loan at the higher limit is still subject to the maximum five-year repayment period and substantially equal payment requirements.

ERISA Title I requirements. ERISA requires plan loans to be available on a reasonably equivalent basis to all participants and adequately secured. Under Department of Labor (DOL) rules, the prohibited-transaction exemption for plan loans states that to ensure adequate security, plans cannot use more than 50% of the present value of a participant's vested accrued benefit to secure all outstanding plan loans made to the participant.

The CARES Act does not provide any relief from these requirements, and DOL hasn't issued any guidance for loans made under the CARES Act. However, after Hurricane Katrina, DOL said in a [press release](#) that the agency will not find plans in violation of ERISA Title I, "including the requirements that plan loans be available on a reasonably equivalent basis and be adequately secured, solely because they made a plan loan to a qualified individual in compliance with the provisions of KETRA."

## Suspension of loan repayments

The CARES Act allows qualified individuals to suspend all plan loan repayments until Dec. 31, 2020. The suspension is available for both new loans and loans taken before the act became law.

Safe harbor method. Notice 2005-92 provided a safe harbor method for implementing KETRA's loan suspension for Hurricane Katrina victims. In the absence of IRS guidance on the CARES Act, employers should be able to rely on this safe harbor.

Under the safe harbor, a plan is treated as complying with the loan suspension if a qualified individual's obligation to repay a plan loan is suspended any time between March 27 and Dec. 31, 2020. Repayments must resume in January 2021, and the plan may extend the term of the loan by the duration of the

suspension period. The loan balance and future payments must be adjusted for interest during the delay. The delay will not cause a loan to violate the maximum five-year repayment period or substantially equal payment requirements for plan loans.

Is delay mandatory or optional? The CARES Act states that due dates for all plan loan repayments during the remainder of 2020 “shall be delayed” for qualified individuals. This language suggests employers must make the relief available to qualified individuals (i.e., the individual can decide whether to continue making payments).

However, prior IRS guidance suggests the agency views this type of relief as optional. KETRA similarly provided that loan repayments due from Aug. 25, 2005, through Dec. 31, 2006, “shall be delayed” for eligible participants. But Notice 2005-92 stated “an employer is permitted to choose to allow this delay in loan repayments,” which appears to conflict with the statutory text. Employers considering not making the loan suspension available should seek the advice of legal counsel.

## Employer considerations for offering relief

As explained above, the suspension of plan loan repayments appears to be mandatory for plans. However, the other relief provisions are optional. Plans may — but don’t have to — offer coronavirus-related distributions and plan loans at the increased cap. Some employers might prefer to make all of the relief available to give participants the greatest flexibility. Different employers may prefer one option over the other. The decision will depend on a host of employer-specific factors, including the pandemic’s anticipated impact on the employer’s workforce.

For example, employers that expect to lay off workers might decide only to offer coronavirus-related distributions, since repayment would be optional for affected workers. However, an employer not expecting a workforce reduction might prefer to offer only loans to ensure employees will return the funds to their retirement accounts.

Other employers might feel their plans’ loan and hardship provisions already provide relief to their employees, especially if any distribution can be treated as coronavirus-related. However, these employers still might consider notifying their employees that the relief is available and allowing qualified individuals to claim the favorable tax treatment (e.g., no 20% withholding) on their plan distributions.

## Plan amendment deadlines

Nongovernmental employers have until the end of the first plan year beginning on or after Jan. 1, 2022, to amend their plans for the relief (although IRS could extend the deadline). Governmental employers have an additional two years. All amendments will be retroactive to March 27, 2020 — the date of the legislation’s enactment — or if later, the effective date of the amendment.

## Related resources

### Non-Mercer resources

- [Pub. L. No. 116-136, Coronavirus Aid, Relief, and Economic Security Act](#) (Congress, March 27, 2020)
- [Instructions to 2018 Form 8915B](#) (IRS, Feb. 14, 2019)
- [Notice 2005-92](#) (IRS, Nov. 30, 2005)
- [Press release, US Labor Department acts to improve access of hurricane victims to 401\(k\) loans and withdrawals](#) (DOL, Nov. 30, 2005)
- [Pub. L. No. 109-73, Katrina Emergency Tax Relief \(KETRA\) Act](#) (Congress, Sept. 23, 2005)

### Mercer Law & Policy resources

- [SECURE, CARES acts change rules on required minimum distributions](#) (April 7, 2020)
- [Stimulus bill gives 2020 DB funding relief, access to DC savings](#) (March 26, 2020)

### Other Mercer resources

- [Stay informed on the coronavirus](#) (regularly updated)

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