IRS Guidance on CARES Act Retirement Plans Distribution and Loan Relief

On June 19, 2020, through IRS Notice 2020-50, the Internal Revenue Service (IRS) issued guidance on the CARES Act's retirement plan distribution and loan relief. The IRS previewed this guidance through a set of FAQs published on the IRS website on May 4, 2020. Consistent with those previously released FAQs, Notice 2020-50 closely resembles IRS Notice 2005-92, which provided guidance on similar distribution and loan relief passed by Congress in response to Hurricane Katrina. The **key takeaways** from Notice 2020-50 are summarized below, thanks to Adam McMahon of Davis & Harman, LLP.

As with the FAQs, Notice 2020-50 focuses solely on the provisions of the CARES Act related to loan relief and coronavirus-related distributions (CRDs). The Notice does not address the 2020 RMD relief (except as noted below regarding permitting 2020 amounts that would otherwise be treated as RMDs to be treated as CRDs if they otherwise qualify as such).

General Guidance

- **Distribution and loan relief is optional.** Consistent with prior guidance from the IRS, Notice 2020-50 again confirms that it is optional for employers to adopt the CARES Act's distribution and loan relief, including the loan repayment delay. Accordingly, plans sponsors can offer some, all, or none of the CARES Act's distribution and loan relief. The Notice makes clear that plan sponsors are permitted to choose whether, and to what extent, they wish to make available the CARES Act's distribution and loan relief.
- **Expansion of qualified individuals.** The CARES Act's distribution and loan relief is only available to certain "qualified individuals" who have been affected by COVID-19. For example, by statute, "qualified individuals" include individuals who have been diagnosed with COVID-19 and individuals who have experienced "adverse financial consequences" as a result of certain circumstance caused by the virus. It was widely recognized that there were a number of situations that were appropriate for relief, although they were not expressly covered by the list of "covered individuals" in the CARES Act. Pursuant to the CARES Act provision authorizing IRS to do so, Notice 2020-50 describes additional factors that will make someone a "qualified individual."

Thus, under the Notice, a "qualified individual" now includes an individual who experiences adverse financial consequences as a result of:

  - the individual 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 (as defined below) being quarantined, being furloughed or laid off, or having work hours reduced due to COVID-19, being unable to work due to lack of childcare due to COVID-19, 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; or
  - closing or reducing hours of a business owned or operated by the individual's spouse or a member of the individual's household due to COVID-19.

In this context, a "member of the individual's household" is someone who shares the individual's principal residence.

- **Self-certification.** Consistent with prior IRS guidance, in determining whether an individual is a "qualified individual," the administrator of an eligible retirement plan may rely on an individual's certification, unless the administrator has actual knowledge to the contrary. Notice 2020-50 confirms that this type of self-certification can be used for purposes of determining whether an individual is eligible to receive a CRD and for purposes of determining whether an individual qualifies for the CARES Act's loan relief. (The CARES Act had not specifically authorized self-certification with respect to loan relief, so section 303 of the HEROES Act did so. Now that the IRS has permitted such self-certification, the HEROES Act provision is no longer needed.)

  Notice 2020-50 also provides helpful guidance on two additional aspects of self-certification:

  - No inquiry necessary. First, Notice 2020-50 clarifies that the requirement for an administrator to not have "actual knowledge to the contrary" does not require an administrator to inquire into whether an individual

satisfies the conditions to be a qualified individual. Rather, in determining whether an administrator has "actual knowledge to the contrary," the administrator will only be judged on whether the administrator already possesses sufficiently accurate information to determine the veracity of the certification.

- Self-certification example. Second, Notice 2020-50 provides an example of an acceptable certification. This example does not require a plan participant to specifically identify the circumstances that make such participant a qualified individual. Rather, the certification only requires the participant to attest that he or she satisfies at least one of the factors listed in the CARES Act or Notice 2020-50.

- Effective dates for CRDs and increased loan limits. Consistent with the CARES Act, the Notice states that a CRD can be taken from an eligible retirement plan on or after January 1, 2020, and before December 31, 2020. The Notice does not permit a distribution taken *on* December 31, 2020 to be treated as a CRD.

  By statute, the CARES Act permits employers to increase the maximum loan amount available to qualified individuals for loans made "during the 180-day period beginning on the date of enactment [March 27, 2020]." There had been a question as to whether this 180-day period should count the day of enactment (in which case the period would end September 22, 2020) or the counting should begin the day after enactment (in which case the period would end September 23, 2020). Consistent with the previously released FAQs, the Notice states that the increased loan limits are available "before September 23," thereby indicating that September 22 is the last day that a loan can be distributed in accordance with the increased limits.

Coronavirus-Related Distributions

- Coronavirus-related distributions. Consistent with prior guidance, Notice 2020-50 indicates that an employer that offers CRDs "is permitted to develop any reasonable procedures for identifying which distributions are treated as coronavirus-related distributions under its retirement plans." However, the plan must be consistent in its treatment of similar distributions.

Notice 2020-50 also confirms that a qualified individual is permitted to designate a distribution as a CRD, even if the distributing plan chooses not to make available CRDs. In fact, the Notice repeatedly emphasizes that the plan's treatment of a distribution may be different than how the individual reports the distribution on his or her tax return.

Consistent with prior guidance, Notice 2020-50 states that amounts described in Q&A-4 of Treas. Reg. section 1.402(c)-2 are not permitted to be treated as CRDs. Thus, for example, corrective distributions of elective deferrals or employer contributions to comply with the 402(g) and 415 limits are not eligible to be treated as CRDs.

- Periodic payments and RMDs. Notice 2020-50 indicates that individuals can designate periodic payments and distributions that would have been required minimum distributions (RMDs) but for the CARES Act's 2020 RMD waiver as CRDs.

- Beneficiaries. Consistent with prior guidance, Notice 2020-50 confirms that a distribution received by a qualified individual as a beneficiary can be treated as a CRD. However, Notice 2020-50 explains that any CRD (whether from an employer retirement plan or an IRA) paid to a qualified individual as a beneficiary of an employee or IRA owner (other than the surviving spouse of the employee or IRA owner) cannot be recontributed.

- Loan offsets and deemed distributions. Notice 2020-50 confirms that a reduction or offset of a qualified individual's account balance in order to repay a loan can be treated as a CRD. By comparison, a plan loan treated as a deemed distribution cannot be treated as a CRD.

- Pension plans. Consistent with prior guidance, Notice 2020-50 confirms that pension plans, such as money purchase plans, are not permitted to make a distribution before an otherwise permitted distributable event merely because the distribution, if made, would qualify as a CRD. (The HEROES Act, passed by the House, would reverse this.) Further, a pension plan is not permitted to make a distribution under a distribution form that is not a qualified joint and survivor annuity without spousal consent merely because the distribution, if made, could be treated as a CRD.

- CRD amount. Notice 2020-50 confirms that CRDs, unlike hardship distributions, are not limited to the amount that is

necessary to satisfy a financial need arising from COVID-19. CRDs are, however, limited to an overall limit of $100,000 per person.

- Coronavirus-related distributions will not be treated as a change in substantially equal periodic payments. In the case of an individual receiving substantially equal periodic payments from an eligible retirement plan under the exception to the 10% early distribution tax, the receipt of a coronavirus-related distribution from that plan will not be treated as a change in substantially equal payments as described in § 72(t)(4) merely because of the coronavirus-related distribution.

- Repayments of CRDs. The CARES Act permits CRDs to be repaid to an eligible retirement plan within three years of the distribution. There have been questions about the extent to which retirement plans are required to accept recontributions of CRDs, especially when a plan otherwise accepts rollover contributions. Consistent with the IRS's earlier FAQs, Notice 2020-50 only partially addresses this issue.

Relevantly, Notice 2020-50 states, "In general, it is anticipated that eligible retirement plans will accept recontributions of coronavirus-related distributions, which are to be treated as rollover contributions. However, eligible retirement plans generally are not required to accept rollover contributions. For example, if a plan does not accept any rollover contributions, the plan is not required to change its terms or procedures to accept recontributions of coronavirus-related distributions."

Notice 2020-50 also reiterates that only CRDs that are eligible for tax-free rollover treatment under Code sections 402(c), 403(a)(4), 403(b)(8), 408(d)(3) or 457(e)(16) can be recontributed to an eligible retirement plan. However, notwithstanding this general rule, hardship distributions that otherwise qualify as a CRD can be repaid.

Notice 2020-50 also indicates that the relief described in Q&A-14 of 1.401(a)(31)-1 (regarding invalid rollover contributions) is available for repayments of CRDs if the plan administrator accepting the recontribution reasonably concludes that the recontribution is eligible for the CARES Act's repayment rules, as described in Notice 2020-50. For this purpose, a plan administrator can rely on an individual's self-certification for purposes of determining whether the individual is a qualified individual, unless the administrator has actual knowledge to the contrary.

- Tax reporting. Consistent with prior guidance, Notice 2020-50 confirms that CRDs should be reported on Form 1099-R, even if repaid in the same year. Additionally, Notice 2020-50 confirms that payors are permitted to report CRDs using distribution code 2 (early distribution, exception applies) or code 1 (early distribution, no known exception) in box 7 of Form 1099-R.

CARES Act Loan Relief

- One-year delay of loan repayments. There has been considerable confusion about how to apply the loan repayment delay permitted by the CARES Act. Specifically, the CARES Act permits plans to delay, for a period of up to one year, retirement plan loan repayments otherwise due for qualified individuals on or after March 27, 2020 and before January 1, 2021.

Similar to Notice 2005-92, Notice 2020-50 cuts through the issue to some extent by offering a safe harbor method to comply with the loan repayment delay. But the Notice also describes other ways for plans to implement the CARES Act's loan repayment delay. We read the Notice as offering at least three ways to administer the loan repayment relief. Notice 2020-50 also expressly recognizes that there may be additional reasonable ways to administer the loan repayment relief.

  - Safe Harbor Method. Under the safe harbor method, a plan can suspend a qualified individual's obligation to make loan repayments for any period beginning not earlier than March 27, 2020, and ending not later than December 31, 2020 (suspension period). The loan repayments must resume after the end of the suspension period, and the term of the loan may be extended by up to 1 year from the date the loan was originally due to be repaid. If a qualified employer plan suspends loan repayments during the suspension period, the suspension will not cause the loan to be deemed distributed even if, due solely to the suspension, the term of the loan is extended beyond 5 years. Interest accruing during the suspension period must be added to the remaining principal of the loan. A plan satisfies these rules if the loan is reamortized and repaid in substantially level installments over the remaining period of the loan (that is, 5 years from the date of the loan,

assuming that the loan is not a principal residence loan, plus up to 1 year from the date the loan was originally due to be repaid). If an employer, under its plan, chooses to permit a suspension period that is less than the maximum suspension period described above, the employer is permitted to extend the suspension period subsequently, but not beyond December 31, 2020. The Notice includes an example to illustrate the safe harbor method.

- Alternative 1. The Notice describes the CARES Act loan repayment delay as allowing the following. Under the first alternative method, "each repayment that becomes due from March 27, 2020 through December 31, 2020 may be delayed for up to 1 year and then reamortized (taking into account interest) over a period that is up to 1 year longer than the original term of the loan. Each reamortized repayment may then be added to other reamortized repayments and to non-reamortized repayments to construct an overall loan reamortization schedule." This method would appear to result in loan repayments in 2021 being uneven, which may be difficult to implement.
- Alternative 2. In addition, the Notice states that "there may be additional reasonable, if more complex, ways to administer section 2202(b) of the CARES Act" and then gives an example. Under the example, assuming that a plan has a suspension period beginning April 1, 2020, "each repayment that becomes due during the suspension period may be delayed to April 1, 2021 (the 1-year anniversary of the beginning of the suspension period). After originally scheduled repayments for January through March of 2021 are made, the outstanding balance of the loan on April 1, 2021, including the delayed repayments with interest, may be reamortized over a period that is up to 1 year longer than the original term of the loan."

Nonqualified deferred compensation

There has been an effort to get the IRS to provide relief for employees participating in nonqualified deferred compensation (NQDC) plans. Notice 2020-50 provides limited relief in this regard.

Generally, once an employee makes an election to defer compensation into a NQDC plan, that election must be irrevocable for the next year. Thus, an employee that elected to defer compensation into an NQDC plan for 2020 cannot easily cancel that election even if the employee needs the cash.

The current regulations already have an exception, allowing a NQDC plan to offer a cancellation of a deferral election if the employee has an unforeseeable emergency or hardship distribution from the employer's qualified plan. Notice 2020-50 states if an individual receives a CRD from the employer's plan, this will be treated as a hardship distribution, allowing the NQDC election to be cancelled (but not postponed or otherwise delayed).