

IRS Issues Additional Guidance on Coronavirus-Related Distributions and Plan Loans under CARES Act

Alert

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On Friday, June 19, 2020, the Internal Revenue Service (IRS) released Notice 2020-50 which provides additional guidance regarding the coronavirus-related distributions (CRDs) and coronavirus-related loans and loan repayment delays (CR Loan Relief) made available to certain retirement plan participants affected by COVID-19 under § 2202 of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act). The notice expands, and in some cases modifies, previous guidance issued by the IRS regarding CRDs and CRD Loan Relief discussed in [our recent blog](#). Discussion of the material information contained in the notice is provided below.

Expanded Definition of "Qualified Individual" Eligible for CRDs and CR Loan Relief

Under authority granted to the IRS under § 2202(a)(4)(A)(ii)(III) of the CARES Act, Notice 2020-50 expands the definition of "qualified individual" (an individual eligible for CRDs or CR Loan Relief) to take into account additional factors such as reductions in pay, rescissions of job offers, and delayed start dates with respect to an individual, as well as adverse financial consequences to an individual arising from the impact of COVID-19 on the individual's spouse or household member.

Prior to the issuance of Notice 2020-50, a "qualified individual" was limited to an individual:

- Diagnosed with the virus SARS-CoV-2 or with coronavirus disease 2019 (collectively, "COVID-19") by a test approved by the Centers for Disease Control and Prevention (CDC) (including a test authorized under the Federal Food, Drug and Cosmetic Act)

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- Whose spouse or dependent (as defined in section 152 of the Internal Revenue Code) is diagnosed with COVID-19 by a test approved by the CDC (including a test authorized under the Federal Food, Drug and Cosmetic Act (FFDCA))
- Who experienced adverse financial consequences as a result of being quarantined, furloughed, laid off, having work hours reduced or being unable to work due to lack of childcare due to COVID-19, or having to close or reduce hours of a business owned or operated by the individual due to COVID-19

Under the expanded definition provided under Notice 2020-50, "qualified individual" is now defined as an individual who:

- Is diagnosed, or whose spouse or dependent is diagnosed with COVID-19 by a test approved by the CDC (including a test authorized under the FFDCA)
- Experiences adverse financial consequences as a result of the individual, the individual's spouse or a member of the individual's household (that is, someone who shares the individual's principal residence):
 - Being quarantined, 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
 - Closing or reducing hours of a business that they own or operate due to COVID-19
 - Having pay or self-employment income reduced due to COVID-19
 - Having a job offer rescinded or start date for a job delayed due to COVID-19

The notice clarifies that plan administrators can rely on an individual's certification that the individual is a qualified individual (unless the plan administrator has actual knowledge to the contrary), but also notes that an individual must actually be a qualified individual in order to obtain favorable tax treatment with respect to a CRD. Section 2.E of the notice provides a sample certification that may be used by an individual to certify that they satisfy the conditions to be a qualified individual.

Distributions that May be Treated as CRDs

In Notice 2020-50, the IRS confirms that, in general, a qualified individual is permitted to designate a distribution satisfying the applicable CARES Act requirements as a CRD without regard to whether the plan treats the distribution as a CRD. The notice provides examples of amounts that may be treated as CRDs including periodic payments and distributions that would have been required minimum distributions but for CARES Act § 2203, distributions 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. The notice also provides,

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however, that any amount described in Q&A-4 of Reg. § 1.402(c)-2 (for example, a loan treated as a deemed distribution or a corrective distribution of an excess contribution) is not permitted to be treated as a CRD.

Notice 2020-50 further clarifies that the amount of a CRD is not limited to amounts withdrawn solely to meet a need arising from COVID-19. Thus, an individual who is a qualified individual is permitted to take CRDs up to the \$100,000 limit regardless of the individual's need for the funds.

Direct Rollover, Notice and Withholding Requirements Not Applicable to CRDs

Notice 2020-50 and prior guidance provide that an employer retirement plan is permitted, but not required, to treat a plan distribution meeting the applicable requirements as a CRD. The notice clarifies that if a plan elects to treat a distribution as a CRD, the rules for eligible rollover distributions under Code § 401(a)(31), 402(f), and 3405 do not apply and the plan is not required to offer the individual a direct rollover with respect to the distribution and the plan administrator is not required to provide the individual with a 402(f) notice. In addition, the CRD is not subject to the 20% withholding requirement normally applicable under Code § 3405(c)(1), but the voluntary withholding requirements of Code § 3405(b) continue to apply.

Safe Harbor for Suspension of Loan Repayments

Under CARES Act § 2202(b)(2), a qualified employer plan may permit a delay in certain loan repayments (generally, loan repayments with a due date between March 27, 2020 and December 31, 2020) without causing the loan to be treated as a deemed distribution under Code § 72(p). For plans providing qualified individuals with this repayment relief, Notice 2020-50 provides a safe harbor under which suspensions of loan repayments will be treated as satisfying § 2202(b)(2) of the CARES Act and, by extension, Code § 72(p).

Under the safe harbor, a qualified individual will be treated as satisfying the requirements of § 72(p) pursuant to § 2202(b)(2) of the CARES Act if the suspension of loan repayments is conducted in accordance with the following:

- The obligation to repay a plan loan is suspended under the plan for any period beginning not earlier than March 27, 2020, and ending not later than December 31, 2020 (the suspension period).
- Loan repayments 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 is added to the remaining principal on the loan.
- The loan is reamortized and repaid in substantially level installments over the remaining period of the loan.

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Use of the safe harbor is not required and the IRS has acknowledged that there may be additional reasonable methods for administering the suspension of loan repayments.

Plans Accepting Recontribution of CRDs

Under the CARES Act § 2202(a)(3), a qualified individual who receives a CRD that is eligible for tax-free rollover treatment is generally permitted to recontribute, at any time within the three-year period beginning on the day after the date on which the distribution is received, any portion of the CRD (but not in an amount in excess of the amount of the distribution) to an eligible retirement plan that accepts eligible rollover contributions. A valid recontribution of a CRD will generally be treated as having been made in a trustee-to-trustee transfer to the recipient plan; however, the recontribution will not be treated as a rollover contribution for purposes of the one-rollover-per-year limitation under Code § 408(d)(3)(B).

Notice 2020-50 provides that the relief in Q&A-14 of Reg. § 1.401(a)(31)-1 (relating to the acceptance of invalid rollover contributions) applies to an employer retirement plan accepting recontributions of CRDs so long as the plan administrator accepting the recontribution reasonably concludes that the recontribution is eligible for direct rollover treatment, that the recontribution is made within the applicable three-year period, and that the recontribution does not exceed the amount of the CRD.

As is the case with issuing CRDs to qualified individuals, a plan administrator accepting a recontribution of a CRD may rely on an individual's certification that the individual is a qualified individual in determining whether the recontributed amount was a CRD, unless the administrator has actual knowledge to the contrary.

Tax Reporting of CRDs by Eligible Retirement Plans

Notice 2020-50 details the reporting procedures for eligible retirement plans that issue CRDs. If an eligible retirement plan makes a CRD the plan must report the distribution on Form 1099-R even if the individual recontributes the CRD to the same plan in the same year. If no other appropriate code applies to the distribution, the plan is permitted to use distribution code 2 (early distribution, exception applies) or distribution code 1 (early distribution, no known exception) in box 7 of Form 1099-R.

Tax Reporting of CRDs by Qualified Individuals

Notice 2020-50 provides a detailed discussion of the reporting requirements and tax consequences applicable to qualified individuals that receive CRDs. In general, a qualified individual is permitted to designate any distribution satisfying the applicable requirements as a CRD (without regard to whether the plan treated the distribution as a CRD) by reporting the distribution on the individual's federal income tax return and on Form 8915-E (Qualified 2020 Disaster Retirement Plan Distributions and Repayments).

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Qualified individuals designating amounts as CRDs have two options for including the taxable portion of the CRD in their income: (1) include the taxable portion of the distribution in income ratably over a three-year period; or (2) elect out of the three-year ratable income inclusion and include the entire amount of the taxable portion of the CRD in the year of distribution. An individual election cannot be made or changed after the timely filing of the individual's federal income tax return (including extensions) for the year of distribution and all CRDs received in a taxable year must be treated consistently (either all distributions must be including in income over a three-year period or all distributions must be included in income in the current year).

If a qualified individual elects to recontribute any portion of the CRD during the three-year period beginning on the day after the date the CRD is received, the reporting requirements and applicable tax consequences vary depending on whether the individual uses the one-year or three-year inclusion method with respect to the CRD and whether the recontribution is made before or after the individual files their federal income tax return for the applicable tax-year. Special rules also apply for qualified individuals who use the three-year income inclusion method with respect to a CRD if the individual dies before the full taxable amount of the CRD has been included in the individual's gross income.

Nonqualified Deferred Compensation Plans - Permitted Cancellation of Service Provider Deferral Elections

Under Reg. § 1.409A-3(j)(4)(viii), a nonqualified deferred compensation plan subject to Code § 409A may provide for a cancellation of a service provider's deferral election, or such cancellation may be made, due to an unforeseeable emergency or a hardship distribution, under Reg. § 1.401(k)-1(d)(3).

Notice 2020-50 provides that if a service provider receives a CRD from an eligible retirement plan, the CRD will be considered a hardship distribution under Reg. § 1.401(k)-1(d)(3) for purposes of Reg. § 1.409A-3(j)(4)(viii). As a result, if a nonqualified deferred compensation plan provides that a deferral election is canceled for an employee who receives a hardship distribution under a qualified retirement plan, deferrals under the nonqualified deferred compensation plan will be canceled for an employee who receives a CRD from the qualified plan.

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