FAQs for retirement plan professionals

How the CARES Act affects retirement plans

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security (CARES) Act was passed by Congress and signed into law by the President. The CARES Act is the latest round of federal government support relating to the coronavirus public health crisis and associated economic turmoil. It contains some significant retirement plan provisions.

The following is a detailed look at the CARES Act's retirement provisions and related legislation, provided in a FAQ format for easy reference.

Contents:

Details on coronavirus-related distributions under the CARES Act

Did the CARES Act provide for a new type of plan withdrawal?

Yes, a coronavirus-related distribution (also referred to as a CRD, COVID-19 withdrawal, or CARES Act withdrawal) is a new type of distribution available under a plan to participants still employed by the plan sponsor.

Is this provision mandatory or optional?

A CRD is an optional provision. If you choose to offer this distribution, you'll need to amend your plan. Note that the deadline to amend a calendar year plan is December 31, 2022.

What types of plans can offer a CRD?

Profit-sharing, 401(k), 403(b), and governmental 457(b) plans, as well as IRAs, can offer CRDs. The provision doesn't apply to nonqualified plans, including 457(b) plans sponsored by tax-exempt entities. A defined benefit (DB) plan or money purchase pension plan can only make the CRD available for participants age 59½ or older.

Who can request a CRD?

A CRD may be made to a "qualified individual." Participants must certify that they're qualified individuals, and a plan administrator can rely solely on that certification.

A qualified individual is a participant, their spouse, or a dependent who's been diagnosed with the virus SARS-CoV-2 or with coronavirus disease 2019 (COVID-19) by a Centers for Disease Control and Prevention (CDC)-approved test. In addition, a qualified individual is also a participant who, due to such virus or disease, suffers adverse financial consequences resulting from:

- Being quarantined, furloughed, laid off, or having their work hours reduced
- Being unable to work due to lack of childcare or, if the individual owns or operates a business, as a result of a closure or reduction in operating hours
- Other factors, as determined by the Secretary of the Treasury (or the Secretary's delegate)

When can a participant request a CRD?

The CARES Act permits withdrawals made since January 1, 2020, and before December 31, 2020, to be considered CRDs. Therefore, the CRD must be made no later than December 30, 2020.

What if someone took a distribution before the law was passed?

John Hancock is waiting to see if the IRS will provide additional guidance on how distributions after January 1, 2020, and prior to March 27, 2020 (the date the CARES Act was enacted), should be reclassified; however, it appears that such distributions may be treated as CRDs, provided the individual otherwise qualifies.

How much can be withdrawn in a CRD?

The maximum amount, which can be distributed across all plans of the controlled group, is $100,000. The withdrawal can be in one lump sum or in multiple payments, but must be made in 2020 and, as previously mentioned, no later than December 30th.

What limits apply when making a CRD?

A CRD isn't subject to current restrictions on distributions from 401(k), profit-sharing, or 403(b) plans (e.g., elective deferrals available only due to hardship or reaching age 59½), or from an IRA; however, a DB or money purchase pension plan still isn't permitted to make an in-service distribution prior to the date the participant reaches age 59½. Guidance on this issue may be forthcoming.

How is a CRD different from other plan distributions?

Unlike other types of distributions, with a CRD:

- There's no requirement to provide the special tax notice (e.g., 402(f) notice).
- There's no requirement to withhold 20%, because a CRD isn't an "eligible rollover distribution."
- The withdrawal can't be directly rolled over to another plan or IRA.
- The 10% penalty for distributions prior to age 59½ (i.e., the early withdrawal penalty tax) doesn't apply.

John Hancock comment: This new distribution is separate from the new safe harbor event in the final hardship regulations that addresses participant expenses and losses (including loss of income) incurred due to federally declared disasters. Although the COVID-19-related disaster declaration currently only extends to certain states, the Federal Emergency Management Agency (FEMA) is continuously updating the states subject to similar declarations of "major disasters."

John Hancock comment: Since CRDs aren't eligible rollover distributions, notice must be provided to participants that they're permitted to elect out of withholding. The penalties for not providing the notice were increased to $100 per participant under the SECURE Act, with a maximum of $50,000.

Can a participant repay a CRD?

Yes, a CRD can be repaid within three years. The three-year period begins on the date after which the CRD is received. Only the amount received (no earnings) can be paid back. The distribution amount can be repaid in one lump sum or in multiple payments to an "eligible plan" in which the participant is a "beneficiary" and which accepts rollovers. Repayments to plans (versus IRAs) are treated as timely rollovers. On the other hand, repayments to IRAs are treated as trustee-to-trustee transfers, so they don't count toward the 1-per-12-month limit applicable to IRA distributions rolled over to IRAs.

Are repayments considered after tax or pretax?

John Hancock is waiting to see if the IRS will provide additional guidance on how repayments are classified.

John Hancock comment: We believe a repayment will be considered after tax or pretax depending on your CRD. For example, if the CRD was taken from all pretax sources, any repayment will be considered pretax. Alternatively, if the distribution was taken from all designated Roth accounts, any repayment will be considered Roth.

Will income tax be due on the full amount of a CRD when 2020 taxes are paid in 2021?

No, participants may spread payment of CRD-incurred income taxes they owe over three years (to the extent not repaid), unless they elect otherwise.

John Hancock comment: We anticipate the IRS will provide additional guidance on how to treat income taxes due and payable prior to the date a participant may choose to repay the CRD.

Details on loan provisions under the CARES Act

How does the CARES Act affect loans?

The CARES Act affects loans by increasing loan limits and suspending repayments, but only for qualified individuals.

How have the loan limits been increased under the CARES Act?

The CARES Act increases the current limits for loans from $50,000 to $100,000, and the 50% of vested account limit to 100%, but only for "qualified individuals" and only for a limited period.

Is a plan required to use the increased loan limits?

This provision appears to be optional for plan sponsors. In determining the maximum dollar loan limit, the limit is still reduced if the qualified individual has other loans in the last 12 months under the existing loan rules. In addition, plan administrators may want to consider decreasing the "100% of participants' account balance" to a lower percentage to account for changes in a participant's vested account, from the date on which the loan is requested to the date it's processed.

Who's a "qualified individual" for purposes of the increased loan limits?

The qualification criteria is the same as that for the CRD described above.

John Hancock comment: While the CARES Act specifically provides that a plan administrator can rely on a participant's certification that they're a qualified individual for purposes of a CRD, this language isn't specifically included in the increased loan limit provision. It appears that this is a technical oversight.

When can the increased loan limits be used?

There's a limited window to use the new increased loan limits. These limits apply to loans taken on or after March 27, 2020 (i.e., date of enactment of the CARES Act), and no later than September 22, 2020 (180 days following the date of enactment).

Can loan repayments be delayed?

For a qualified individual, loan repayments due on or after March 27, 2020, through December 31, 2020, can be delayed for one year from their original due date (delay period). This applies to existing loans in good order on March 27, 2020, and to loans taken after that date in 2020 and with payment due dates in 2020.

John Hancock comment: It's unclear if the delay period applies to a loan during its cure period, provided a loan cure period is permitted under the plan. Plan sponsors should confirm with their service providers and outside ERISA counsel.

Does the delay also apply if the qualified individual has terminated employment?

This is unclear. Absent guidance, it appears reasonable to permit the suspension of loan repayments until the earlier of the end of the one-year delay period and date on which the participant requests distribution (which would trigger a loan default).

Does interest continue to accrue during the delay period?

Yes, interest continues to accrue during the delay period and will be added to the outstanding loan.

John Hancock comment: Although it's unclear how recordkeepers will treat the accrued interest, we believe most will add the accrued interest to the principal and re-amortize the loan in substantially level amounts over the remainder of the loan (as extended for the one-year delay period).

Does the delay period extend the term of the loan (five years or plan period for residential loans)?

Yes, the delay period is added to the expiration of the loan note.

Must plans permit qualified individuals to delay repayment of loans under the CARES Act?

Unclear. Absent guidance, it appears that plans are required to offer qualified individuals the right to delay repayment of loans, provided the loans are eligible, as described above.

John Hancock comment: We'll monitor this situation and notify you if guidance is issued indicating that the right to delay loan repayments is optional.

What's the due date for plan amendments to reflect these loan changes?

The deadline is the last day of the plan year beginning in 2022 (2024 for governmental plans).

Handling 2020 RMD waivers under the CARES Act

What changes did the CARES Act make with respect to RMDs?

The CARES Act waives the requirement that a participant receive an RMD in calendar year 2020. RMDs from defined contribution (DC) plans, such as 401(k), employee stock ownership plans, profit-sharing, money purchase, 403(b), and governmental 457(b) plans, as well as IRAs (including inherited IRAs), are waived; however, the waiver doesn't apply to RMDs from DB pension plans.

For purposes of distribution within five years of a participant's death, calendar year 2020 is disregarded. In other words, it's excluded when counting the number of years since the participant passed away, extending the deadline for receiving the RMDs by one year.

John Hancock comment: The CARES Act didn't make any changes with respect to the rules regarding the mandatory 10-year distribution period for an individual not considered a "designated beneficiary" pursuant to the new rules under the SECURE Act. We'll monitor this and notify you if changes are made.

John Hancock processed the remaining RMDs for participants who turned age 70½ in 2019 and were required to receive their first RMD by April 1, 2020 (absent the CARES Act). What happens if a participant in a plan that's subject to the waiver doesn't want to receive this RMD?

As with the RMD waiver provisions passed in 2009, we expect further guidance from the IRS to liberalize the rules for making indirect rollovers of amounts distributed as RMDs before the CARES Act was enacted, similar to the way waiver provisions were issued in 2009.

Will the plan automatically suspend RMD payments in 2020?

We'll notify plan sponsors and participants as soon as possible with respect to the implementation of the waiver for 2020 RMDs.

The impact of the CARES Act on DB plans

Does the CARES Act affect DB plans?

Yes, the CARES Act extends the time for making 2020 minimum required contributions to single-employer DB plans and permits the use of the prior year's adjusted funding target attainment percentage (AFTAP) for the 2020 plan year. In addition, it appears to permit such plans to add a COVID-19 withdrawal provision, at least for affected participants who've attained age 59½.

When must minimum required contributions for 2020 be made to single-employer DB plans?

The Act permits sponsors of such plans to delay, until January 1, 2021, minimum required contributions due in 2020 (e.g., 2020 quarterly contributions and contributions due in 2020 for the 2019 plan year). Delayed contributions, when made, must be made with interest. The interest rate is the plan's effective rate of interest (ERI) for the plan year, including the date of payment. For many plans with a calendar year plan year, the ERI for 2020 is currently between 5% and 6%.

John Hancock comment: While this provides some welcome relief to plan sponsors, it takes a "kick the can down the road" approach to meaningful funding relief. The expectation is that Congress will pass legislation later this year to reduce funding obligations, thereby decreasing the amount employers that delay contributions will eventually have to make. It's unclear whether such funding relief would also affect (i.e., increase) the ERI for delayed payments. In addition, although the CARES Act permitting the delay until January 1, 2021, is a practical matter since that date is a holiday, it appears the latest contribution date is December 31, 2020.

How does the CARES Act affect a DB plan's AFTAP?

The Act permits employers to use the DB plan's AFTAP (used to determine whether a plan must implement benefit restrictions) for the last plan year ending before 2020 as the **AFTAP for plan years that include calendar year 2020.**

John Hancock comment: DB plans with calendar year plan years are permitted to use the 2019 AFTAP for the 2020 plan year. For DB plans with non-calendar-year plan years, the effect of this provision is less clear. For example, in the case of a DB plan with a July 1 to June 30 plan year, can the plan use the AFTAP for the plan year ending June 30, 2018, for both a plan year beginning July 1, 2019, and a plan year beginning July 1, 2020?

Can a DB plan offer a CRD?

It appears the answer is yes; however, any such withdrawal will be unavailable to an active participant before age 59½.

John Hancock comment: The CARES Act doesn't restrict CRDs to DC plans, but it does limit the waiver of currently applicable distribution timing restrictions for only DC plans. It's unclear whether this distribution type is intended to apply to DB plans as well. Since more guidance is needed on this issue, employers should consider refraining from adding this withdrawal type to their DB plans.

The effects of the Families First Coronavirus Response Act on retirement plans

Is there other legislation that we should know about that may affect retirement plans?

Yes, the Families First Coronavirus Response Act (FFCRA) became law on March 18, 2020. Although the provisions of the FFCRA don't directly apply to retirement plans, there are two provisions within it that may affect the amount withheld from compensation for qualified plan purposes by plan sponsors. The provisions are effective as of April 1, 2020, and expire on December 31, 2020.

What are the two provisions in the FFCRA that may affect my retirement plan?

The Emergency Paid Sick Leave Act and Emergency Family and Medical Leave Expansion Act provisions of the FFCRA may affect plan compensation for qualified plan purposes. Amounts that must be paid to employees by the employer as paid sick leave, as well as payments for absences under the Family Medical Leave Act (FMLA) of 1993 due to the public health emergency resulting from COVID-19, should be included when determining compensation under a plan, unless the plan's provisions specifically exclude this compensation from the definition.

John Hancock comment: The U.S. Department of Labor (DOL) has provided a detailed explanation of this matter on its website.

Does the FFCRA apply to all plan sponsors?

No, the FFCRA will be applied as follows:

- The FFCRA will apply to private employers with fewer than 500 employees, as well as certain public employers (e.g., federal, state, and local public agencies).
- If the employer's business is closed as a result of the public health emergency related to COVID-19 (or an employee is laid off or furloughed), these provisions don't apply (although an individual may be eligible for unemployment benefits).
- Any amounts paid on or prior to the effective date (i.e., March 31, 2020) should be excluded when determining amounts due pursuant to the FFCRA.
- Employers will be reimbursed for the amounts they expend through "refundable tax credits." They'll be able to retain an amount of the payroll taxes (federal income tax, as well as the employer and employee share of Social Security and Medicare taxes) equal to the amount of qualifying sick/childcare leave they pay, instead of depositing it with the IRS. If payroll taxes are insufficient, employers may apply for an advance from the IRS, which will provide the necessary forms, instructions, documentation, and procedures for this purpose.

With respect to the new sick pay and paid FMLA mandated under the FFCRA, should these forms of compensation be eligible amounts included as deferrals and loan repayments in our DC plan?

Generally, the answer is yes; however, you should check your plan's definition of compensation. Any 401(k) deferrals should be withheld from pay related to sick or family and medical leave under the FFCRA, unless the plan specifically provides otherwise (e.g., a specific exclusion of compensation related to sick leave and/or family and medical leave). This compensation would also include amounts for outstanding loan repayments, which should be remitted to the plan. These forms of compensation will also be eligible for employer contributions (i.e., matching and profit-sharing contributions), unless otherwise excluded in the plan's definition of compensation.

John Hancock comment: As a rule, these forms of compensation are included in any basic definition of plan compensation, which is subject to 401(k) withholding. Amounts are paid by the employer and taxable to the employee, although the employer may claim a dollar-for-dollar tax credit.

John Hancock comment: Under applicable Treasury Regulations, this form of compensation doesn't appear to be considered an excluded form of compensation for plan purposes. Additionally, per DOL regulations, this form of compensation doesn't appear to be a "welfare benefit" since the compensation is included in payroll practices.

How do the FFCRA's Emergency Paid Sick Leave Act and Emergency Family and Medical Leave Expansion Act provisions apply to full-time employees?

There are specific requirements set forth in the FFCRA as it relates to the eligibility for paid sick time, if the effects of COVID-19 leave an employee unable to work (including working remotely), an employee is eligible to be paid for an additional 10 weeks of pay, or an employee can't work because a child's school is closed or due to a lack of available childcare as a result of COVID-19. Full-time employees are eligible for 80 hours of paid sick leave.

In total, a full-time employee could be eligible for up to 12 weeks of paid leave (2 weeks under the paid sick leave provisions and an additional 10 weeks under the expanded FMLA provisions), and a part-time employee would be eligible to be paid for the number of hours they'd normally work during that period.

John Hancock comment: Employees are required to provide documentation substantiating the need. Keep in mind that, while the FFCRA adds this new reason for FMLA purposes, if an individual would otherwise be eligible for FMLA purposes due to the impact of COVID-19, then the existing FMLA certifications must continue to be provided. As a result, it remains important to collect and retain any documentation for audit purposes.

How do I determine how much compensation part-time employees are eligible for under the Emergency Paid Sick Leave Act and Emergency Family and Medical Leave Expansion Act?

First, check the terms and conditions of the plan to see if only certain employees are eligible for the plan. The IRS precludes a plan sponsor from expressly excluding part-time employees from the plan if they'd otherwise satisfy the plan's age and service requirements (maximum age of 21 and attainment of 1 year and 1,000 hours of service, respectively) for eligibility purposes.

In determining paid sick time under the FFCRA, part-time employees are eligible to be paid for the number of hours they'd typically work, on average, over a two-week period. The same number of daily hours would be used to determine the employee's eligible pay under the Expanded Family Medical Leave Act.

The applicable rate of pay effectively depends on why the part-time employee isn't working, and compensation is classified by the FFCRA in one of two ways. One determination is based on a "regular rate of pay." The second determination is made based on "two-thirds of the employee's regular rate of pay," as a result of how the employee has been affected by COVID-19.

John Hancock comment: The DOL provides FAQs on its website, so employers have guidance on how to calculate the amount of leave.

MGTS-PS42002-GE 04/20 42002 MGR0401201137582 | 19882