Welcome

CARES ACT RETIREMENT PLAN PROVISIONS AND RELIEF

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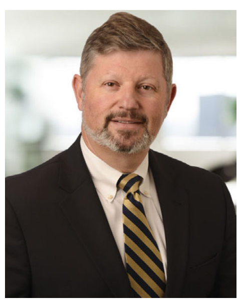

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CORONAVIRUS AID, RELIEF AND ECONOMIC SECURITY ACT (CARES ACT)

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The CARES Act Is Enacted Into Law

Coronavirus Aid, Relief and Economic Security Act (CARES Act)

Signed into law on March 27, 2020

Employers across the country are facing closures of offices, businesses resulting in required work from home arrangements as well as layoffs and furloughs

These business challenges have raised important questions around retirement plan administration and the right type of relief to be made available to plan participants

The CARES Act provides relief to retirement plan participants in a number of important areas that plan sponsors need to be aware of including:

- Distributions
- Loans
- Required minimum distributions
- Other provisions

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Coronavirus-Related Distributions

Retirement plans may now permit in-service coronavirus-related distributions from a participant's vested account balance without regard to normal withdrawal restrictions

This relief is offered through December 31, 2020

The amount of the distribution is limited to $100,000 per tax year – aggregated across all plans of the employer or controlled group

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Coronavirus-Related Distributions

These distributions are subject to the following requirements:

- They are not subject to the 20% mandatory withholding upon distribution
- They are exempt from the 10% early withdrawal penalty generally applied to distributions made to participants who are age 59 ½ or younger
- They are eligible to be indirectly rolled into an IRA or employer plan within three years from the date the distribution is taken
- Those amounts not indirectly rolled into an IRA or other employer plan will be included in gross taxable income, ratably, over three years unless the participant elects to include all amounts in a single year

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Coronavirus-Related Distributions

Coronavirus related distributions are available to eligible participants who meet these requirements:

- Are diagnosed with coronavirus illness or COVID-19
- Have a spouse or dependent diagnosed with the coronavirus illness
- Experience adverse financial consequences as a result of the quarantine, furlough, layoff, reduction in work hours, business closure, lack of childcare other factors determined by the IRS due to the coronavirus emergency

Interestingly, participants can <u>self certify</u> that they qualify for these distributions – a retirement plan administrator/plan sponsor may rely on participant certification that they in fact meet these qualifications

Best practice is to document self certification in writing

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Coronavirus-Related Loan Relief

Participants have been provided with two types of loan relief as well:

<u>Increased loan limits</u> – retirement plans may now allow eligible participants to take loans up to the lesser of $100,000 or 100% of the participants vested account balance

<u>Suspension of current loan payments</u> – upon request of an eligible participant, plan sponsors must suspend loan repayments due on outstanding loans are in good order for a period of up to 12 months

- This relief expires on December 31, 2020
- The suspension period is to be added to the original loan term when repayments, including accrued interest, resume, regardless of the length of loan's original term

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Qualification for Loan Relief

Coronavirus related Loan relief qualifications are identical to the requirements to qualify for coronavirus related distributions:

- Are diagnosed with coronavirus illness or COVID-19
- Have a spouse or dependent diagnosed with the coronavirus illness
- Experience adverse financial consequences as a result of the quarantine, furlough, layoff, reduction in work hours, business closure, lack of childcare other factors determined by the IRS due to the coronavirus emergency

Again, plan sponsors are relieved of the responsibility of verification as participants can simply sell certify that they meet these requirements

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Waiver of 2020 Required Minimum Distributions (RMDs)

Qualified 401(k), 403(b), governmental 457 plans and individual retirement accounts will not be required to make any RMD payments for 2020

Further, if the 2020 RMD has already been paid, it may be rolled over to an individual retirement account or an employer-sponsored retirement plan

Why is this important?

- If the required minimum distribution is calculated based on the values of accounts on December 31, 2019 and participant accounts are now down significantly, the date of this valuation could lead to a disproportionate RMD relative to today's account values forcing disproportionately larger taxable distributions
- So, for those taxpayers who don't need these RMDs to support their lifestyle, leaving it in the retirement plan is a good option

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Defined Benefit Plan Relief

Funding obligations for 2020 may be delayed – Under the CARES Act, all single-employer funding obligations due during 2020 are not required to be made until January 1, 2021, with interest for late payments

Of course, the delay of a contribution obligation to a defined benefit pension plan is not permanent relief from that obligation, but could be helpful in managing the business's cash flow in the current year

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Timing of Plan Amendments

The CARE Act includes a remedial amendment. Giving plan sponsors additional time to amend their plans for this relief

Consequently, plan sponsors can immediately provide coronavirus related distributions and enhanced loan provisions to their participants without having to first amend their plan which is very unusual in the qualified plan arena

Sponsors of non-governmental plans have until the last day of the plan year beginning in 2022 to amend their plans, (i.e., December 31, 2022 for a calendar year plan)

Sponsors of governmental plans have until the last day of the plan year beginning in 2024 to amend their plans

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Plan sponsors must make decisions

These coronavirus related distributions and loan limit increase provisions are optional – plan sponsor do not have to offer them

- Many of the record-keeping and administrative firms that HBKS works with to service our clients are moving to essentially a negative consent model where they will effectively add these revisions to your plan if you don't notify them otherwise prior to a certain date
- If you are unsure of how your administrative firm is handling these provisions, reach out to them directly or your HBKS plan advisor

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Plan sponsor options

Do nothing at this time – This may be a reasonable choice if you have not laid off team members or reduced hours for your employees. These provisions can be added later if the COVID-19 situation worsens

You can add increased loan limit provisions without offering the coronavirus related distribution provision – adding the loan provisions only will not create direct reduction of total plan assets. Additionally, because loan payments can be suspended for the rest of 2020, taking a loan will not create an immediate financial outlay for participants

- However, if a participant takes an expanded loan and is been terminated for any reason, if they are unable to repay the full amount, the outstanding loan balance would default and would be included in taxable income in that year – the three year ratable taxation which applies to coronavirus related distributions DOES NOT apply

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Plan sponsor options

Plan sponsors may add the coronavirus-related distributions provision without offering the increased loan limit provision– If you had expanded distribution options it will create possibly substantial reduction in total plan assets but ensures that effective participants can access their funds without risk of taxation due to a defaulted loan amount in a single plan year

- Again, amounts withdrawn may be repaid to the plan at a later date which might mitigate some of the overall leakage of assets from the plan and the tax burden if not repaid would be paid out over three years

Plan sponsors may add both the coronavirus-related distribution and increased loan limit provisions – Adding both provisions allows participants to have more choices and determine what is best for their particular situation

- This may be a good opportunity to educate participants on the importance of preserving their retirement savings to the extent they are able to and review the advantages of loans versus distributions or vice versa

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Responsive participant education will be critical

Regardless of which combination of coronavirus related/CARE Act is chosen by the plan sponsor, responsive education is critical

Your participant should be informed of potential tax consequences of both scenarios and encouraged to repay any amounts that they need to withdraw if at all affordable

Reach out to your HBKS plan advisor for assistance with participant education related to these options

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RETIREMENT PLAN SPONSOR CONSIDERATIONS DURING SIGNIFICANT BUSINESS DISRUPTION

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Sponsor Considerations During Business Disruption

Can I reduce, suspend or eliminate my *employer* contribution for the year?

It generally depends on whether your plan requires specific contributions or whether they are discretionary or not

For example, most plans do opt for both discretionary profit-sharing contributions and discretionary matching contributions, even if they may communicate a specific defined match to their participants

That being said, mandatory contributions such as safe harbor matching contributions and safe harbor nonelective contributions have special rules for stopping or suspending midyear

- Many of our clients have chosen to adopt safe harbor land designs because they allow the plan sponsor to be deemed to have passed nondiscrimination testing
- The safe harbor designs are popular as they allow highly compensated employees to make the maximum salary deferral

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Sponsor Considerations During Business Disruption

Can my *employees* suspend or reduce their deferral contributions for the year?

In most cases, yes, participants may reduce their salary deferral contributions

Most plan sponsors have published administrative procedures that define how frequently participants can change their deferral elections

Many plans also allow their participants to stop deferrals at any time

These administrative procedures can typically be modified without modifying the plan document

If you're going to modify your administrative procedures related to when participants can stop, start or increase or decrease their contributions, you should provide a notice to participants of this procedural change

It is of course a best practice to document your employees requested modification to their deferrals

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Sponsor Considerations During Business Disruption

Does the coronavirus business disruption impact my obligation with respect to employee deferrals and loan repayments?

The current crisis does NOT reduce the plan sponsor's fiduciary obligation related to depositing employee contributions in a timely manner

Plan sponsor should continue to make employee salary deferrals and loan repayments as soon as administratively possible – for companies with fewer than 100 participants employee deferrals and loan repayments should be made no later than seven business days after the payroll date

You should notify your record-keeping firm and your administrative firm immediately if there are any situations beyond your control to prevent you from making timely deposits

This is an issue that the regulators take very seriously and scrutinize closely if the plan is ever subject to an audit

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Sponsor Considerations During Business Disruption

How do layoffs impact the viability of my plan?

Generally, the layoff is considered a termination of employment and terminated employees have access to distributions from their retirement plan

- These distributions may be in the form of a rollover to another qualified plan or individual retirement account
- Individuals may also choose to have these distributions paid directly to them subject to income taxes

IMPORTANT – if you lay off more than 20% of your workforce a partial plan termination may occur

- If there is a partial plan termination, all affected participants must become 100% vested in their retirement accounts
- The 100% vesting provision for partial plan termination supplies to matching contributions and profit-sharing contributions that may be subject to a vesting schedule

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Sponsor Considerations During Business Disruption

What happens if I rehire back an employee I had to lay off?

If the eligible employee had already satisfied the eligibility requirements, the employee must re-enter the plan on the later of

- The entry date on which they would have entered the plan had there been no severance of employment or
- The date of their re-employment unless the break in service rules apply

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PAY ATTENTION TO TRADITIONAL PLAN SPONSOR FIDUCIARY BEST PRACTICES

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Plan Sponsor Best Practices

Traditional fiduciary best practices for plan sponsors matter even more

Financial markets have dropped precipitously during the first quarter of 2020

Participants may be scrutinizing decisions that plan sponsors have made more carefully after receiving their March 31st statements

Participants may also challenge investment –related decisions and service provider fees, even though these decisions may not have directly contributed to participant account performance

Consequently, plan sponsors should, despite other distractions related to the current business crisis, continue to focus on fiduciary best practices and document these processes

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Plan Sponsor Best Practices

Duty to monitor

Plan sponsors continue to have the duty to monitor the plan's investments and various service providers

We encourage plan sponsors to not table investment committee meetings to review designated investment alternatives or other scheduled meetings with record-keeping or administrative service providers

Remember that plan sponsors have a duty to monitor service provider fees and be able to justify that those fees are reasonable based on the services provided

- Monitoring fees and being able to document that you have a thoughtful process for confirming that those fees are reasonable may be even more important as participants scrutinize the plan service providers and any fees that you are passing on to them

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Plan Sponsor Best Practices

Monitoring plan investments

Plan sponsors continue to have a duty to monitor the plan's investments relative to a prudent, fiduciary standard of care

Plan sponsors should be able to document that they are following this prudent process

This is a good time to review your plans investment policy statement (IPS) and make sure that you are following the processes outlined in the IPS

If the plan's designated investment alternatives was well selected and monitored in the past it is likely that these investment options continued to be prudent even if they may have experienced significant loss due to the overall downturn in the market

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Plan Sponsor Best Practices

Best practice – scrutinize participant actions

Work with your service providers to examine the overall health of your plan

For example, are participants making material changes to their deferrals or significant changes to their investment allocations

Typically, market timing has not been a successful investment strategy, if it appears your participants are "going to cash" as an example, you may want to take that into consideration in your overall communication plan

We strongly suggest you reach out to your plan's advisors and inquire about educational tools or online training that they can make available to participants

Some record-keeping firms for example have built significant online libraries that participants can consult when considering investment changes during periods of extreme market volatility

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Plan Sponsor Best Practices

Best practice – challenge service providers

Ask your various service providers, investment advisor, recordkeeper, third-party administrator, etc. about their business continuity plans and their availability to your participants

Most national record-keeping providers are building informational and educational materials related to market volatility and coronavirus related matters

Confirm that all of the previously published call center information, staffing, etc. is still viable and in place

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