

CARES Act: Retirement Plan Changes

In response to the economic trauma of COVID-19, Congress made it easier for taxpayers to access retirement funds

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) was signed into law on March 27, 2020. This wide-ranging effort to combat the economic upheaval created by the COVID-19 outbreak gives individuals options to utilize retirement plans and Individual Retirement Accounts (IRAs) to help deal with the economic impact of the pandemic. It also waives required minimum distributions in 2020 so taxpayers are not forced to take distributions when account values have declined.

Early Withdrawal Penalties

Distributions from qualified retirement plans and IRAs made before the plan participant turns 59½ are generally subject to a 10% penalty unless the participant meets an exception such as death, disability, or a series of substantial equal periodic payments over the life of the taxpayer (other exceptions may also be available).

The exceptions to the 10% penalty are expanded to include “coronavirus-related distributions,” which is one made:

- Up to an aggregate of \$100,000;
- During calendar year 2020;
- From an IRA (including SEPs and SIMPLEs), qualified retirement plan such as a 401(k), a 457(b) plan maintained by a governmental entity, or a 403(b) plan; and
- To a qualified individual, which is defined as someone:
 - Who is diagnosed with the virus SARS-CoV-2 or its related disease, COVID-19;
 - Whose spouse or dependent is diagnosed with such virus or disease; or
 - Who experiences adverse financial consequences as a result of being quarantined, furloughed or laid off, or having work hours reduced due to such disease, being unable to work due to lack of child care, or the closing or reduction in hours of a business owned by the individual.

Repayment Option

Coronavirus-related distributions may be recontributed within a 3 year period, beginning the day after the date of the distribution, without regard to plan contribution limits.

CARES ACT: RETIREMENT PLAN CHANGES

Taxation

Most qualified plan distributions are subject to ordinary income tax. Taxation of a coronavirus-related distribution can be avoided completely by repaying the distribution within three years. To the extent the distribution is not repaid, the taxpayer can elect to spread out the taxation ratably over three tax years (2020, 2021, and 2022).

Qualified Plan Loans

The amount that a “qualified individual” (defined above) can borrow from a qualified plan which has a loan provision is increased from \$50,000 to \$100,000, but only for loans taken out between March 27, 2020 and September 22, 2020. The percentage that can be borrowed is also increased from 50% to 100% of the present value of the vested amount (capped at \$100,000).

For both new and existing loans, repayment dates between March 27, 2020 and December 31, 2020 are delayed for one year. Subsequent payments and interest accrual will be adjusted to reflect the delay.

Required Minimum Distributions

Required minimum distribution (RMD) rules are waived in calendar year 2020 for IRAs (traditional, SIMPLE and SEP) and certain defined contribution plans, including 401(k), 403(b), 457(b) plans administered by a governmental entity, Roth 401(k), and Roth 403(b) accounts. The RMD rules for non-governmental 457(b) plans, defined benefit plans, and nonqualified annuities have not changed.

Eligibility

Unlike the 10% penalty and policy loan provisions, the waiver of RMDs is *not* limited to qualified individuals. Rather, it is available to all taxpayers who have an RMD in 2020.

- Those who turned 70½ in 2018 or earlier do not have an RMD in 2020.
- Those who turned 70½ in 2019 and took their 2019 RMD in 2019 have no 2020 RMD. Those who turned 70½ in 2019 and take the 2019 RMD on or before April 1, 2020 have no RMD for either 2019 or 2020.
- Those turning 70½ in 2020 would not have an RMD this year anyway since the Required Beginning Date was changed to age 72 by the SECURE Act.

Required Minimum Distributions Already Taken in 2020

If the account owner already received his 2020 RMD, the distribution might be able to be placed back into the account or rolled into an IRA. Since RMDs are waived for 2020, the amount taken out is not considered an RMD, but rather as a normal distribution.

- If the account owner qualifies for “coronavirus-related” relief, then it can be repaid within a three year period beginning the day after the date of distribution.
- However, if the account owner does not qualify for such relief, the distribution must be rolled over within 60 days and the owner is still subject to the one rollover per year rule.

CARES ACT: RETIREMENT PLAN CHANGES

Inherited Accounts

The waiver of RMDs for 2020 includes inherited IRAs and qualified plans if the beneficiary was taking advantage of the RMD rule which permits annual distributions over the beneficiary's life.

If the account owner died before 2020 and the beneficiary was under the general RMD rule requiring that the entire account be distributed by the end of the 5th year following death, 2020 is not counted towards this 5-year period.

If distributions are governed by the new SECURE Act 10-year payout to designated beneficiaries, 2020 is not counted when determining the 10-year period.

A non-spouse beneficiary who has already taken a 2020 RMD cannot roll the distribution into an IRA.

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