Best practices for plan sponsors

Pros and cons of taking coronavirus-related distributions from retirement savings

The COVID-19 pandemic has undoubtedly shaken our economy to the core. Many businesses have struggled to keep their doors open which has caused unemployment claims to soar. Record unemployment, coupled with a U.S. society that has an average household savings account of about $8,800[1], has many people looking to their retirement savings as a "piggy bank" for necessary funds to keep their heads above water.

Withdrawing retirement savings should be carefully considered, even in view of the loosening of restrictions around withdrawals as a result of the Coronavirus Aid, Relief, and Economic Security (CARES) Act because any withdrawal can have a multiplying impact on long-term retirement goals.

However, we are living in unknown times and if your participants need to access their retirement savings, the passage of the CARES Act makes it easier.

The CARES Act and new ways to access retirement savings

The CARES Act relaxed certain provisions around withdrawals and loans from 401(k) plans due to the economic severity brought on by the pandemic. Under the CARES Act, a person who meets certain criteria and has experienced hardship can qualify for a Coronavirus-Related Distribution (CRD) from their IRAs and eligible defined contribution retirement plans, such as 401(k).

If you are considering adding these provisions, remember that amending your plan is a fiduciary decision and **should be thoughtfully considered and your actions documented**. Keep in mind that to provide for these expanded distribution and loan options, the plan needs to be formally amended; and it's best to contact your plan administrator for the required steps.

From a high-level, CRDs from a qualified retirement plan:

- Are available to individuals who meet certain criteria.
- Withdrawals are not subject to the normal 10% early penalty up to $100,000 per person.
- Unlike regular hardship withdrawals, CRDs may be repaid into the plan, or another qualified plan, within three years to avoid incurring taxes. The repayment is not subject to annual retirement plan contribution limits.

- If the individual does not recontribute the distribution within the three-year time period, taxation on the distribution can be spread over a 3-year period.

With regard to loans from qualified plans:

- The limit on loans doubled from 50% of a participant's vested account balance (up to $50,000) to 100% of the participant's vested account balance (up to $100,000).
- The due date for any repayment by a qualified individual of a participant loan that would occur from the date of enactment through December 31, 2020, is delayed for up to one year.
- A qualified individual who could be eligible for these expanded loan limits and loan delays is one who could meet the same coronavirus-related criteria for withdrawals.
- The coronavirus loan provisions are temporary and are in effect for 180 days from the March 27, 2020 date of enactment.

If possible, seek other options

Although the CARES Act makes 401(k) withdrawals and loans easier to access, participants should understand how these actions could affect the future of their retirement savings.

As general guidance, participants should consider other financial reserves before removing funds from their retirement savings. These accounts could include emergency funds, refinancing current debt, HELOCs, CDs, brokerage accounts, cash value life insurance options, personal lines of credit or potentially a loan from a family member.

Importance of financial wellness

Many lessons will be learned from the COVID-19 crisis. One positive impact this pandemic may have within your workforce is the importance of financial wellness. A good program can help employees manage expenses, budget, set financial goals and priorities, while encouraging them to establish a 3 to 6-month emergency savings.

Due to COVID-19, the vast majority of the workforce has been significantly affected. With tangible experience, the silver lining is that it can lead to better budgeting, financial oversight, and hopefully inspire more people to focus on the importance of a long-term retirement savings plan.

[1] Garcia, Adrian. "This is the average amount in savings accounts — how does your cash stack up?" Dec 3,2018.