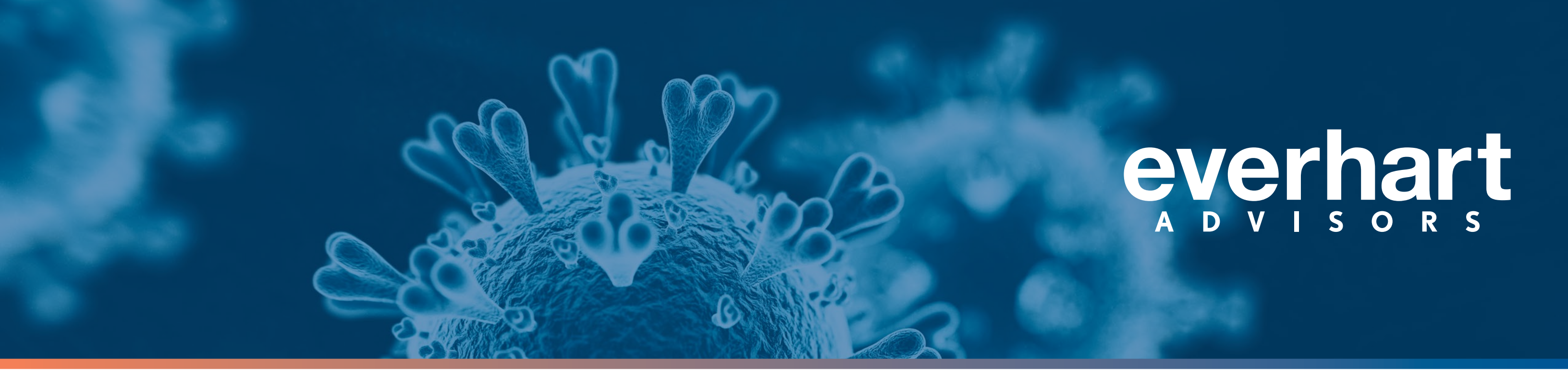

COVID-19 – 401(k) FAQs for Business Owners and Plan Participants

Without question, the COVID-19 pandemic has created a great deal of economic uncertainty. There are numerous crisis-related 401(k) questions that small business owners need answers to. In general, they want to know their options for cutting (or delaying) plan expenses and participant options for taking a 401(k) distribution and loan. This FAQ includes answers to many of the most common questions that have been asked.

Can I reduce or suspend the employer contributions I make to a safe harbor 401(k) plan?

Yes, it's possible to reduce or suspend either safe harbor matching or nonelective contributions (as applicable) mid-year. However, to do so, certain requirements must be met:

- Either:
  - Your business is operating at an economic loss, or
  - the safe harbor notice you distributed to plan participants before the start of the plan year included a statement that you may reduce or suspend contributions mid-year.
- A supplemental notice is distributed to plan participants at least 30 days before the effective date of the reduction or suspension.
- Plan participants are given a reasonable opportunity change their deferral election before the reduction or suspension occurs. A 30-day election period is deemed reasonable
- Your plan must be ADP/ACP tested for the full plan year in which the reduction or suspension occurs using the current year testing method.
- Your plan must meet top heavy minimum contribution requirements for the full plan year in which the reduction or suspension occurs.

Can I reduce or suspend the employer contributions I make to a non-safe harbor 401(k) plan?

Yes. In general, it's easier to reduce or suspend non-harbor contributions. However, the process for doing so will depend upon whether the employer contribution is discretionary or "fixed" (non-discretionary) in nature.

Discretionary matching and profit sharing contributions can be suspended at any time with no plan amendment required. Further, you have no legal obligation to notify your plan participants about this change – though we strongly recommend you do so.

Fixed matching and nonelective contributions can only be reduced or suspended by plan amendment. The effective date of the amendment cannot be retroactive and fixed contribution allocations must continue through the effective date of the amendment.

I have been paying my 401(k) fees from a corporate bank account. Can my plan pay them instead?

Very likely. The DOL divides 401(k) fees into two basic categories – administrative and settlor expenses. Administrative expenses can be paid from 401(k) plan assets, while settlor expenses cannot. In general, fees for 401(k) plan administration (i.e., asset custody, participant recordkeeping, third-party administration) and professional investment advice will qualify as administrative expenses.

Contact Everhart Advisors for a full understanding of your payment options. Changing your payment method could require an update to participant fee disclosures.

My company needs to lay people off. Could these layoffs affect our 401(k) plan?

Yes, if the number of layoffs triggers a partial plan termination. In general, a 401(k) plan is considered to have a partial plan termination when 20% or more of its participants are laid off in a year. If one occurs, you must 100% vest the affected participants. A partial plan termination can be triggered by a single group layoff or multiple group layoffs.

Have the funding deadlines for 401(k) contributions been affected by the COVID-19 crisis?

Not generally. While Notice 2020-18 extended the deadline for calendar-year sole proprietors or C-Corps to fund a 2019 tax-deductible employer contribution from April 15 to July 15 (assuming no filing extension), all other employee and employer contribution deadlines remain the same.

What are the 401(k) distribution and loan options I can offer plan participants?

It depends on the terms of your 401(k) plan. 401(k) plans are not obligated to offer participants access to loans or in-service distributions. When they do, they can offer dramatically different terms. Below are some basics.

- In-service (non-hardship) distributions – permit plan participants to receive a distribution of their account while still employed, subject to the following limitations:
  - Employee elective deferrals (including Roth), safe harbor contributions, QNECs and QMACs cannot be distributed until age 59.5
  - Non-safe harbor matching and profit sharing contributions can be distributed at any age.
  - Employee rollover and voluntary contributions can be distributed at any time.
- Hardship distributions – permit plan participants to receive an in-service distribution of their account if they have an "immediate and heavy financial need" and the distribution is "necessary to meet" the need. The following expenses are automatically considered an "immediate and heavy financial need":
  - Medical expenses not covered by insurance for the participant, his/her spouse, dependents, or beneficiaries.
  - Purchase of a primary residence.
  - Expenses to repair damage to a primary residence.
  - Expenses necessary to prevent eviction or foreclosure from a primary residence.
  - Post-secondary education expenses for the upcoming 12 months the participant, his/her spouse, dependents, or beneficiaries.
  - Funeral expenses for the participant, his/her spouse, dependents, or beneficiaries.
  - Expenses resulting from a federally declared disaster in an area designated by the Federal Emergency Management Agency (FEMA).
- Participant loans - permit plan participants to borrow from their account, subject to the following limitations:
  - The amount of the loan cannot exceed the lesser of: 1) $50,000, minus the participant's highest outstanding loan balance during the past 12 months, or 2) the greater of $10,000 or ½ of their current vested account balance
  - The term of the loan cannot exceed five (5) years. Your plan may allow a longer term for loans used to purchase a principal residence
  - The participant must agree to make substantially equal repayments that include principal and interest at least quarterly
  - The loan must be subject to a legally-enforceable agreement.

Has COVID-19 legislation made any 401(k) distribution and loan changes?

Yes. The Coronavirus, Aid, Relief and Economic Security (CARES) Act allows your 401(k) plan to temporarily loosen certain distribution and loan requirements for participants affected by COVID-19. You can adopt the Act's OPTIONAL provisions in operation immediately - even if your plan does not permit hardship distributions or loans today - provided you formally adopt them by plan amendment before the end of the 2022 plan year (or later if prescribed by the Treasury Secretary).

- Coronavirus-Related Distributions - the bill allows your 401(k) plan to offer a Coronavirus-Related Distribution (CRD) to participants during 2020 that meet one or more of the following conditions:
  - The participant is diagnosed with the virus SARS-CoV-2 or with coronavirus disease 2019 (COVID-19) by a test approved by the Centers for Disease Control and Prevention,
  - The participant's spouse or dependent is diagnosed with such virus or disease by such a test, or
  - The participant experiences adverse financial consequences as a result of being quarantined, being furloughed or laid off or having work hours reduced due to such virus or disease, being unable to work due to lack of child care due to such virus or disease, closing or reducing hours of a business owned or operated by the individual due to such virus or disease, or other factors as determined by the Secretary of the Treasury

You may rely upon the participant's certification that they qualify under one or more of these conditions. The maximum distribution amount eligible for CRD treatment is $100,000. CRDs are not subject to the 10% early withdrawal penalty or mandatory withholding. A recipient can pay the income taxes on a CRD ratably over three years. They can also repay a CRD by rollover over a three-year period.

- Participant Loans – the bill allows your 401(k) plan to offer special loan terms to participants that meet one of the CRD conditions.
  - For new loans requested between March 27, 2020 and September 23, 2020, an eligible participant can receive 100% of their vested account balance up to $100,000.
  - For existing loans, an eligible participant can delay repayments due between March 27, 2020 and December 31, 2020 for up to one year. Delayed payments will need to be re-amortized for accrued interest over the remaining loan term. The general 5-year loan repayment deadline can be extended by the length of the suspension.
- Required Minimum Distributions - the bill allows your 401(k) plan to offer any plan participant – regardless of whether they meet one of the CRD conditions or not – the option to waive their 2020 Required Minimum Distribution (RMD). If a participant has already taken a 2020 RMD, they can repay it by rollover within 60 days – assuming your plan accepts indirect rollovers and the participant is eligible to make a rollover contribution.

Don't lose sight of the future in these uncertain times

No doubt about it – COVID-19 has hit many small businesses hard. However, cutting back 401(k) plan expenses today can dramatically reduce the future value of participant accounts decades from now due to the power of compound interest. That said, if you're a business owner, you should carefully weigh your options before you act.

If you need help doing so – or help counseling your in-need plan participants - call us. We can guide you.

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