Retirement Plan Relief in Consolidated Appropriations Act, 2021

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Signed by the President in December, the Consolidated Appropriations Act, 2021 (CAA) combines COVID-19 stimulus relief with a number of year-end appropriations bills, and it includes numerous provisions that will impact retirement plans. The retirement plan relief provisions in the CAA are divided between (1) qualified disaster relief (including actions Congress has historically taken to relax normal retirement plan distribution and withdrawal rules in light of a natural disaster) and (2) separate COVID-19 relief (including new rules for retirement plans in light of the ongoing COVID-19 pandemic).

These retirement plan provisions are permissive, meaning that a plan sponsor is not required to adopt the provision. However, if a plan sponsor does decide to adopt any of these provisions, it will need to work with its third-party administrator (TPA) to put procedures in place for proper plan administration. A plan sponsor also will have to provide notice of any new plan provisions to impacted eligible employees; however, the CAA allows additional time for plan sponsors to adopt formal amendments to their retirement plans.

Qualified Disaster-related Relief for Retirement Plans

The qualified disaster-related relief provisions in the CAA are similar to relief Congress has utilized in the past to respond to wildfires, hurricanes and other natural disasters. These CAA provisions are designed to address the natural disasters that occurred coincident with the COVID-19 pandemic by relaxing retirement plan distribution rules to give participants more access to their funds and to provide penalty relief for distributions taken during such a disaster.

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Qualified Disaster Distributions

The CAA provides relief in the form of a Qualified Disaster Distribution (QDD). Under this relief, a plan sponsor may amend its retirement plan to allow a "Qualified Individual" to take a QDD from his or her eligible retirement plan account (i.e., from a 401(k), 403(b), or governmental 457(b) plan) of up to $100,000, without penalty or withholding (similar to Coronavirus-Related Distributions under the Coronavirus Aid, Relief, and Economic Security Act ["CARES Act"]). To constitute a QDD, the distribution must be made to a Qualified Individual on or after the first day of the incident period of a "Qualified Disaster" and before June 25, 2021. Each QDD is taxed ratably over a 3-year period (unless the Qualified Individual elects otherwise) and may be recontributed in 3 years to an eligible retirement plan, with repayments receiving direct rollover treatment.

For these purposes, a Qualified Disaster includes any disaster that occurred between December 28, 2019 and December 27, 2020, and which was declared a disaster by the President under the Robert T. Strafford Disaster Relief and Emergency Assistance Act during the period beginning January 1, 2020 and ending February 25, 2021. Further, a Qualified Individual is someone: (1) whose principal place of abode is located in a "Qualified Disaster Area"; and (2) who suffered an economic loss as a result of the Qualified Disaster. A Qualified Disaster Area is any area in which a Qualified Disaster was declared, but does not include an area that is a disaster area solely due to the COVID-19 pandemic (relief for which was provided under the CARES Act).

Return of Withdrawals for Home Purchase/Construction

The CAA also allows plan sponsors to amend their plans to grant participants the special right to recontribute any hardship distributions initially taken to purchase or construct a principal residence in a Qualified Disaster Area, if those funds were not used for such purposes due to a Qualified Disaster. To qualify for this right: (1) the hardship distribution must have been received no more than 180 days before and within 30 days after the Qualified Disaster incident; and (2) the repayment must be made no later than June 25, 2021 to an eligible retirement plan in which the individual is a beneficiary and for which rollover contributions of such distributions are permitted.

Disaster-related Plan Loans

In addition, the CAA permits plan sponsors to increase their retirement plan's loan limits to allow Qualified Individuals to receive plan loans ("Disaster-related Plan Loan") in amounts up to $100,000 or 100% of the present value of his or her vested account balance, instead of the $50,000 and 50% vested account balance limits that normally apply under the law. Further, a plan may provide that repayments of a Disaster-related Plan Loan may be suspended for a period of up to one year or up to June 25, 2021, if longer, if repayment of such loan normally would be due during the period beginning on the first day of the disaster incident period and ending 180 days from the last day of such incident period. However, interest on the Disaster-related Plan Loan must continue to accrue during the applicable suspension period. This CAA loan relief is similar to the loan provisions provided in the CARES Act.

Plan Amendment Deadline

These Qualified Disaster–related relief rules are optional provisions under the CAA, and plan sponsors generally have until the last day of the plan year beginning on or after January 1, 2022 (i.e.,

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December 31, 2022, for calendar year plans) to amend their plans to provide for this relief. Plan sponsors of governmental plans have until the last day of the plan year beginning on or after January 1, 2024 to amend their plans to provide for this relief (i.e., until December 31, 2024 for calendar year governmental plans). (These are the same amendment deadlines that apply under the CARES Act.) If a plan sponsor decides to implement these provisions and make them operational before amending the retirement plan, it is important to keep track of these plan amendment deadlines so that the plan does not have an operational failure.

New COVID-19 Pandemic–Related Relief

The CAA also contains the following new relief provisions for plan sponsors whose participant base is directly impacted by the COVID-19 pandemic.

Partial Plan Termination Temporary Relief

The CAA provides temporary relief from the partial plan termination rules under section 411(d)(3) of the Internal Revenue Code of 1986, as amended ("Code"), for turnovers due to the COVID-19 pandemic period. As background, Code Section 411(d)(3) requires retirement plans to provide for 100% vesting upon full or partial termination of a retirement plan. The determination of whether a partial plan termination has occurred is based on facts and circumstances, but as a general rule, a reduction of more than 20% in the number of covered participants during a plan year has been considered a partial plan termination by the Internal Revenue Service (IRS).

The CAA provides brief relief from the partial plan termination rules (and therefore, 100% vesting) during any plan year that includes the period beginning March 13, 2020 and ending March 31, 2021. In order to be eligible for this relief, the number of active participants covered under the retirement plan on March 31, 2021 must be at least 80% of the number of active participants covered under the retirement plan on March 13, 2020. This percentage is based on the total number of active participants; however, the 80% does not have to be comprised of the same individuals who were active participants on March 13, 2020. As a result of this temporary relief, an employer who may have incurred layoffs and closings during the COVID-19 pandemic, but whose employment numbers, and ultimately plan participation numbers, rebound by March 31, 2021, will not be required to fully vest those who were terminated during such period.

We anticipate further guidance from the IRS, including guidance on any required plan amendments. Future guidance from the IRS is also expected to address the treatment of a prior determination of a partial plan termination during the COVID-19 pandemic which is subsequently determined to be eligible for this temporary relief, especially in cases where 100% vesting and termination distributions occurred before the relief was issued. We will update this article in the event such guidance is issued.

In-Service Distributions During Working Retirement

In addition, under the CAA, the in-service distribution age during working retirement applicable to pension plans Code Section 401(a)(36) has been lowered from age 59½ to age 55 for certain employees in the building and construction industry. As background, Code Section 401(a)(36) permits employers with pension plans to offer in-service distributions to employees who have

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attained at least age 62. The Setting Every Community Up for Retirement Enhancement Act of 2019 ("SECURE Act") later lowered this minimum age limit from age 62 to age 59½ for pension plans and governmental 457(b) plans. For certain multiemployer pension plans covering employees in the building and construction industry, the CAA now lowers this minimum age limit again to age 55 for individuals who were participants in the pension plan before April 30, 2013. To qualify under this provision: (1) the pension plan's trust must have been in existence as of January 1, 1970; and (2) the pension plan must have received at least one favorable determination letter from the IRS before December 31, 2011, affirming the age 55 in-service distribution during working retirement provision.

This provision is effective for distributions made before and after the enactment date of the CAA. This is very targeted relief which will only apply to a limited number of multiemployer plans that meet these conditions.

Temporary Reversal of Section 420 Transfers

Further, the CAA permits a plan sponsor who elected to transfer excess defined benefit plan assets, in order to prefund a retiree health benefits account or a retiree life insurance account, to terminate such election by December 31, 2021, with respect to any taxable year specified by the taxpayer that begins after the election. As background, Code Section 420 permits "qualified future transfers," under which up to ten years of retiree health and life costs may be transferred from an overfunded pension plan to a retiree health benefits account and/or a retiree life insurance account within the plan (a Code Section 401(h) account). Such transfer must meet several requirements, including the requirement that the plan is at least 120% funded at the outset and throughout the transfer period.

Due to economic volatility related to the COVID-19 pandemic, pension plans that have historically met the excess funding requirement have fallen below the 120% threshold, and as a result, those plan sponsors face an immediate need to restore such losses in order to return the plan to the 120% threshold. Under this temporary relief, plan sponsors are permitted to make a one-time election no later than December 31, 2021 to terminate any existing transfer period for any taxable year beginning after the date of election. Assets previously transferred that were not used as of the election effective date are required to be transferred back to the pension plan within a reasonable amount of time. Assets transferred back to the plan are treated as a taxable employer reversion, unless the amount is transferred back to the applicable Code Section 401(h) account before the end of the five-year period beginning after the original transfer.

If you are considering adding any of these optional qualified disaster-related relief provisions or are wondering if the new COVID-19 relief provisions impact your retirement plan — or if you would like to discuss any other factors specific to your retirement plan — please contact a Trucker Huss attorney.

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