



CARES ACT ADMINISTRATIVE Q&As

COVID-19 LOANS

A common question regarding the CARES Act loan provision is whether the loan provisions are optional or mandatory. Remember that, if allowed by the plan, a qualifying individual¹ may take a plan loan up to the lesser of \$100,000 or 100% of the participant's vested account balance. This only applies to loans made on or before September 22, 2020 (180 days following enactment of CARES).

Eligibility & Adoption

CL1: Are the COVID-19 loan provisions optional?

A: Yes, the loan provisions are optional according to IRS Notice 2020-50.

CL2: If a plan allows loans increased to \$100,000, is the employer responsible for determining if an employee meets the definition of a qualified individual?

A: The CARES Act and IRS Notice 2020-50 state that the administrator of an eligible retirement plan may rely on an employee's representation that the employee satisfies the conditions to be a qualified individual.

CL3: If one of the business owners is also a participant, are they still eligible for the new loan provision of up to \$100,000?

A: Yes, if they meet the definition of qualified individual, they are eligible for the increased loan amount.

CL4: Can a business owner (a dentist) that is laying people off qualify for the distribution or participant loan option under COVID-19? He's not closing his business but is definitely feeling the effects of this. Is this an obvious area I am overlooking?

A: It seems you are asking about whether the dentist would be considered a qualified individual. The answer is yes. One of the criteria to be an eligible individual is the individual experiences adverse financial consequences as a result of, among other items, "closing or reducing hours of business owned or operated by the individual."

CL5: Can a terminated employee take a COVID-19 loan when the plan only allows loans to active employees?

A: Yes. A plan can permit terminated employees to take COVID-19 loans. This will require a change to the plan's loan program to allow the loans to terminated employees. The loan program will also need to be modified if it only permits loan repayments by payroll deduction.

CL6: How do COVID-19 CARES Act loans from IRA based plans work? Are they all characterized as early distributions that are taxed, and then after money is put back into an IRA, is an amended tax return is filed? Is there a way to simply take a loan from SEP or SIMPLE IRA?

A: IRAs and IRA based plans (SEPs and SIMPLE IRAs) cannot offer loans. The individual would have to take a distribution (and if a COVID Qualified Individual and distribution could repay in 3 years).



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CL7: If a plan sponsor wants to use the CARES special loan provision, but does not offer loans now, does it need to amend the plan to add a regular loan provision?

A: The short answer is yes the plan must be amended - but it's not clear which issue you are raising, so here are answers to both possible issues.

First, can the loan provision be limited to just COVID-19 loans or you must you also allow broader loan provisions? The answer to that is you can limit loans to COVID 19 loans - although you would still need all the loan program items you identified.

Second, when must the amendment be adopted? Some would say it's a discretionary amendment and must be adopted by the last day of the plan year - or even sooner because of ERISA. There are good arguments to support the position that the addition of the broader loan rules is integrally related to the change in the law and is covered by the extended deadline in the CARES Act - the end of the 2022 PY (two years later for governmental plans).

CL8: If a qualified individual asked for the loan and said that it was going to be used for the of the purposes that allowed repayment over more than 5 years, would that be allowed?

A: The Act doesn't limit loans (or distributions) to need. So, it would be possible for a participant to use the higher COVID limits and get a loan to purchase a principal residence and have a repayment period longer than 5 years. A plan could, however, limit the terms of loans so you could provide that COVID loans are limited to 5 years.

Administration & Reporting

CL9: Does the extension of the loan repayments expire on 12/31/2020 so it's only really a year applied retroactively back to 1/1/2020?

A: The law provides that any loan repayments due between March 27, 2020, and December 31, 2020, can be delayed. Thus, for example, a loan repayment that would be due in December 2020 could be extended to December 2021.

CL10: Does the rule providing that the maximum dollar loan amount is reduced by the principal paid on any loans in the past 12 months (i.e., the difference between the highest outstanding balance and the current balance of a loan) apply?

A: Yes, that rule still applies. The CARES Act only increased the limit on participant loans for qualified individuals. It did not change the calculation of the maximum permissible loan under IRC §72(p) so the calculation would be \$100,00 minus the amount of principal repaid in the prior 12-month period. For example, suppose an employee took a \$40,000 loan in 2019 and repaid the entire loan in January 2020. The maximum the employee could borrow under the CARES Act would be \$60,000 (\$100,000 - \$40,000 principal repaid in the prior 12 months).



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CL11: If a plan does not already allow loans and the client wants to add loans temporarily due to COVID-19, do they have to amend the plan to allow loans, then amend to remove them? Or can they add them temporarily as part of the COVID-19 amendment?

A: This can be handled as part of the effective date of the amendment. For example, the amendment could provide: "For the 180 day-period beginning on March 27, 2020, the plan permits loans in accordance with the following provisions: ..."

CL12: If a plan only allows CARES Act loans, how do they establish the interest rate, etc., other provisions of the loan policy if the amendment is not required until 12/31/2022?

A: The law only extends the deadline to adopt a plan amendment. The plan would still need to establish the parameters of the loan program in order to operationally implement the program.

CL13: Can you confirm that if a plan only allows one outstanding loan at a time, then a participant won't be able to request a higher loan amount until the existing loan has been repaid?

A: Confirmed. The CARES Act increases the maximum loan, but it does not force a plan sponsor to change its existing loan program. Of course, the plan's loan program could be amended to allow for more than one loan at a time.

CL14: An employee is laid off 3/13/2020 with an outstanding loan. Loan repayments are via payroll deduction but there is no payroll. Under the CARES Act, the loan can be extended for one year from 3/27/2020. What do they do about repayments that could not be made between 3/13 and 3/27?

A: This is not extended by the CARES Act. It would need to be handled like any other non-repayment of a loan (i.e., if not repaid by the plan's grace period, then the loan would be a default). However, it is possible the extension provided by Notice 2020-23 would apply to this loan (and if so, the repayment is extended to July 15, 2020).

CL15: What do you recommend we tell clients asking the question, "What do we do about loan payments for employees that may come back to work?" Do they need to have the employee send checks for loan payments while there is no payroll, or, do you think it best to tell the client wait and see when we have more guidance and in a few months when you know the employees are coming back? I feel that it may be best to tell employers to take a pause and wait to see what happens since the loans would not default under current loan policy without relief until 7/1/2020, as that would be one full quarter with no loan payments.

A: We can't provide a definitive answer, but your suggested approach makes sense. The individuals are qualified individuals so the plan could use the CARES Act loan repayment delay. The plan could either: (1) apply the one-year delay from the outset; (2) accept checks for loan repayments; or (3) wait until 7/1/20 before deciding whether to use the CARES Act provision (or a combination of (2) and (3) could be used).



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CL16: Since interest continues to accrue on COVID-19 loan repayment suspensions, there is a mathematical need to either re-amortize payments or take more payments. Someone has to do the calculations. Someone is going to charge for these calculations. On large loans, no big deal maybe. On a \$2,000 loan, the re-amortization fee could be higher than the additional interest. Is there any relief where if the additional interest is less than \$100 or \$150 just take same number of payments and can disregard additional interest?

A: The CARES Act requires that the additional interest accrue during the period that payments are suspended. There is no de minimis amount in the law where this does not have to be done.

CL17: We envision some problems on COVID-19 loans due to market volatility. These issues exist already but the COVID-19 limit and market volatility make them more likely to be an issue. A participant has \$20,500 in their account on day 1, and they request a \$20,000 COVID-19 loan on day 1. On day 2 they sign a promissory note and amortization schedule for \$20,000 loan. On day 3, the recordkeeper goes to distribute the loan and there is only \$19,000. What do they do? Restart whole process? Or just redo the amortization schedule? This can be a really downward cycle. Recordkeepers can do these documents quickly, but not quickly enough to deal with 10% market swings.

A: The moving target associated with making loans on daily valued plans has always been challenging with a cyclical market. For that reason, some providers have procedures in place that limit the maximum loan to a slightly smaller percentage of the maximum than otherwise allowed by the law. This would leave a buffer for market fluctuations.



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Notices

CL18: Some recordkeepers are waiving some fees for COVID-19 distributions and/or loans. There is no practical way to update ERISA §404(a)(5) notices timely. Is there a requirement to do so?

A: Yes, if the fees that can be charged to a participant's account changes, then a new notice needs to be provided. There is not an exception in the CARES Act for this. Normally, the update must be provided at least 30 days before the change. However, DOL Reg. §1.404a-5 has an exception for "unforeseeable circumstances beyond the control of the plan administrator." In that case, the notice must be furnished as soon as reasonably practical.



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Repayment Extension

CL19: How will amortization schedules be revised? Is there a consensus regarding how this should be handled?

A: The IRS provided guidance on how to handle this in Notice 2020-50. The safe harbor method, which is not the only method, would require the loan to be re-amortized as of January 1, 2021.

CL20: If a participant has existing loans, are repayments of those loans delayed by one year?

A: Under Notice 2020-50, it is optional whether a plan will allow the delay.

CL21: If a participant obtains a \$100,000 loan and defers repayments for a year, will the accumulated interest cause the loan to violate the statutory limit?

A: No. The limit is applied at the time the loan is made.

CL22: Does the extension of the loan repayments expire on 12/31/2020 so it's only really a year applied retroactively back to 1/1/2020?

A: The law provides that any loan repayments due between March 27, 2020, and December 31, 2020, can be delayed. Thus, for example, a loan repayment that would be due in December 2020, could be extended to December 2021.



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