Damitz Brooks Nightingale Turner Morrisset

Benefits in Brief

News and Insights for HR Executives, CFOs and Professional Administrators

Summer 2020

COVID-19 and Retirement Plans

How the CARES Act Affects Your Retirement Plan

The Coronavirus Aid, Relief, and Economic Security (CARES) Act that was signed into law in late March is a massive piece of legislation that's more than 880 pages long and carries a price tag of at least $2 trillion.

The Act contains a number of provisions that affect pensions and qualified retirement plans. Following is an overview of the CARES Act provisions you should be aware of as a retirement plan sponsor.

Penalty-Free Retirement Plan Distributions

Qualified individuals who have been affected by COVID-19 are exempted from the normal 10 percent penalty that applies to early withdrawals from their retirement account. This exemption applies to withdrawals of up to $100,000 made during the 2020 calendar year.

Plan participants will qualify for one of these coronavirus-related distributions if at least one of the following conditions applies:

- The individual, or his or her spouse or dependent, tested positive for COVID-19.
- The individual is experiencing adverse financial consequences due to being quarantined, furloughed, laid off, or otherwise unable to work due to COVID-19.
- The individual is unable to work due to childcare issues related to COVID-19.
- The individual owns a business that has been forced to close or reduce its hours due to COVID-19.

Note that adoption of this provision is optional for plan sponsors. You can rely on the plan participant's certification as proof that he or she qualifies for a coronavirus-related distribution due to one of these factors.

Participants can re-contribute funds to their plan (or another retirement plan) within three years of taking the distribution without regard to annual plan contribution limits. If they don't recontribute funds within this time, they can spread out the payment of taxes on the distribution (without penalty) over three years.

Increased Plan Loan Limits

The CARES Act doubles the amount of money that qualified plan participants can borrow from their retirement plan from $50,000 to $100,000, assuming their plan allows loans. This provision applies for loans taken out during the 180-day period after March 27, 2020.

Participants can delay repayment of plan loans that are due through the end of this year for up to one year. Later repayments will also be adjusted as appropriate to reflect the prior delayed due date plus any interest that accrues during the delay. Adoption of this provision is also optional.

Continued on page 3

The Coronavirus Crisis

What's Your Fiduciary Duty During the Crisis?

Employee benefit plan sponsors are facing many questions due to the coronavirus pandemic. One of the most important is simple: What is your fiduciary duty during this crisis?

Given the depth of the crisis and the financial impact it's having on many plan participants, it's critical for plan sponsors to seriously consider this question. In particular, sponsors should be providing participants with proper guidance and tools when it comes to managing their retirement plan during times of heightened volatility and uncertainty.

Now more than ever, participants need help in making the best decisions regarding their retirement plan investments. This includes information and guidance to help them avoid making emotional investing decisions that could derail their long-term retirement strategies.

Your employee education and financial literacy efforts can be divided into three parts: risk, timing, and opportunity. Following is a closer look at each.

Going Beyond Risk Tolerance

Risk tolerance questionnaires are often used to gauge the level of risk that participants are willing to take with their retirement investments. However, this approach to gauging risk may not only be unsuitable but also harmful for some plan participants.

A better approach for participants might be to gauge their risk according to three key dimensions:

1. How much risk do they *want* to take?
2. How much risk are they taking *now*?
3. How much risk is *necessary* to reach their financial goals for retirement?

By viewing risk through this lens, participants may be more prepared emotionally when markets experience corrections … or worse. As a plan sponsor, you can better fulfill your fiduciary duty by providing tools that help participants better match their portfolio's asset allocation with their true risk tolerance.

Maintaining a Long-Term Perspective

One of the biggest challenges that many plan participants face is keeping a long-term perspective with their retirement savings. This is especially true during times of crisis and extreme volatility.

Nobody enjoys watching their retirement portfolio sink by 20 percent or more during a bear market. However, many participants could be reminded that short-term stock market drops will likely be little more than a blip on the radar when they begin withdrawing retirement funds decades later.

Even recent history is replete with examples of major crises and stock market plunges that were followed relatively quickly by rebounds and new market highs—from the 9/11 terrorist attacks to the 2008-2009 financial crisis. Reminding participants of this history can go a long way toward fulfilling your fiduciary duty.

Capitalizing on Opportunity

When stock markets fall by 20 to 30 percent or more, it can be hard to see the silver lining in the clouds. But market drops like this can present an opportunity for retirement investors who maintain a long-term perspective.

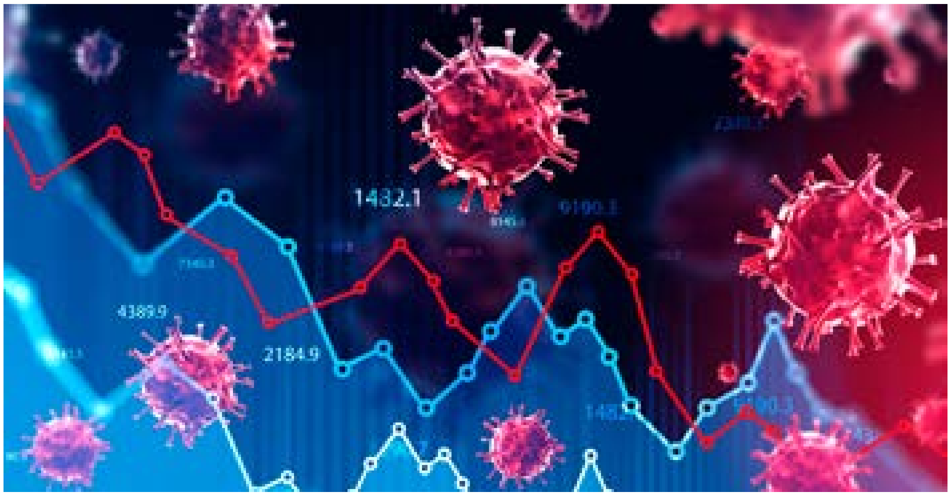
For example, U.S. recessions accompanying stock market drops that averaged 34 percent were associated with pullbacks that lasted an average of 15 months. On average, it takes 23 months for investors in these markets to get back to where they were before the pullback started.

In other words, investors who experience a 34 percent market drop recoup their losses in a little less than two years on average. The opportunity comes from continuing to make contributions to their retirement accounts during this time—because these contributions are purchasing securities at heavily discounted prices.

You can fulfill your fiduciary duty during the coronavirus crisis by educating participants about these kinds of opportunities, as well as offering default investment options like target date funds that make it easier for participants to take advantage of these opportunities.

Reassess Your Fiduciary Duty

Now is the time to reassess your fiduciary duty given the challenges of the coronavirus crisis—especially when it comes to participant education, communication, and guidance. Doing so could help you avoid problems down the road.



Key CARES Act Provisions

Continued from page 1

Suspension of RMDs for 2020

The SECURE Act legislation signed late last year raised the age for taking required minimum distributions (RMDs) from traditional IRAs and 401(k)s from 70.5 to 72. The CARES Act has taken this further by suspending all RMDs for 2020, including from inherited accounts.

As a result, account owners who normally would have been required to take RMDs this year will no longer have to do so. This could benefit participants whose retirement investments have lost value due to the stock market correction as it will allow their portfolios to potentially recover if markets rebound later this year.

The suspension of RMDs applies to owners of the following types of retirement accounts:

- Profit sharing and money purchase pension plans
- Traditional 401(k) plans
- 403(a), 403(b), and 457(b) plans
- Traditional IRAs

If participants have already taken an RMD for this year, they can generally roll these funds back into their account or another retirement account and eliminate the tax bill. While this is technically allowed for RMDs taken between January 1 and April 1 of this year, the 60-day deadline for rolling over assets after their distribution effectively limits it to RMDs taken after January 31.

Delay of Contributions for Defined Benefit Plans

If you sponsor a single employer pension plan, you would normally be required to make quarterly contributions to the plan. However, the CARES Act allows you to defer these contributions with interest until January 1, 2021.

Note: You can use the funding percentage for the 2019 plan year instead of the 2020 plan year to help avoid benefit restrictions.

Steps to Consider

Now is a good time to review your plan's procedures to determine if any changes are required to implement these provisions. Pay especially close attention to the following areas:

- You will need to create a new distributive event that's not subject to the 10 percent early distribution penalty or mandatory 20 percent withholding for participants to make penalty-free retirement plan distributions. Also, if you offer multiple plans, you should ensure that the aggregate amount of distributions taken by any one participant doesn't exceed $100,000.
- If participants are going to repay penalty-free distributions to their accounts, you should treat these repayments as rollover contributions.
- You must allow for the increased plan loan limits if you intend to allow this.
- Delayed loan payments should be properly documented so they aren't treated as being in default.
- Consider whether now is a good time to allow plan loans if your plan currently doesn't permit them.
- If your plan does permit loans, update loan procedures and amortization schedules to reflect changes in the loans.

In addition, you should prepare and distribute communication materials to inform participants about any plan operational changes resulting from the CARES Act. These materials should also let participants know about any additional steps required to benefit from these changes.

Have more questions about how the CARES Act could affect your retirement plan? Give us a call to schedule a meeting soon.

Form 5500 Filing Deadline Extended

The IRS has extended the deadline for filing Form 5500 due to the coronavirus crisis. Sponsors of retirement plans with original or extended due dates falling between April 1 and July 15, 2020 now have until July 15, 2020 to file their form.

If you need more time, you can request an additional extension by filing Form 5558 by July 15, 2020. However, the extended due date will not be later than what it would have been without relief. The filing deadline extension also applies to Form 990.

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200 East Carrillo, Suite 303
Santa Barbara, CA 93101
805-963-1837 Fax 805-564-2150

Fiduciary Focus: Target Date Funds

Target date funds (TDFs) have become an increasingly popular investment choice for many retirement plan participants. According to a recent estimate by Bloomberg Law, participants currently hold about $1.4 trillion in TDFs.

The coronavirus crisis is putting TDFs in a new light for plan sponsors due to the potential for fiduciary breach lawsuits. During the 2008-2009 financial crisis, TDFs lost an average of 67 percent of their value. It remains to be seen what kind of damage this crisis will inflict on TDFs, but it's possible that we could see more lawsuits later this year.

Now is a good time to ensure you're fulfilling your fiduciary duties when it comes to your plan's TDF offerings. Not all TDFs are the same. While the DOL has designated TDFs as a qualified default investment alternative (QDIA), the fiduciary safe harbor does not relieve you of the responsibility to prudently select and monitor your TDFs and ensure that fees are reasonable.

You might consider hiring a professional fiduciary, such as a 3(21) investment advisor, to help you review your TDFs and assume co-fiduciary responsibility. You should also plan to review and consult with your advisors on a regular basis given the fluidity of the pandemic situation and economic developments.

Review your process for TDF selection and oversight to ensure it covers all your fiduciary responsibilities. Also consider establishing and documenting a formal procedure for TDF selection and oversight if you don't currently have one, as well as maintaining thorough recordkeeping of all decisions you make.

Contact our office if you have more questions about your fiduciary duties as they relate to target date funds.

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