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EMPLOYEE BENEFITS AND EXECUTIVE COMPENSATION

HARDSHIP WITHDRAWAL REGULATIONS FINALIZED

The Internal Revenue Service has issued final regulations updating the rules for hardship withdrawals under Section 401(k) and 403(b) plans. The regulations are largely identical to the proposed regulations issued last November, and the IRS confirmed that plans which have complied with the proposed regulations also satisfied the final regulations.

Details about the changes made by the proposed regulations and reflected in the new final regulations are available in our November 2018 newsletter, “IRS Issues Hardship Withdrawal Changes” (<https://www.hsela.com/news-and-information/legalcurrents/1509-irs-issues-hardship-withdrawals-changes>). While the final regulations do not make any substantial changes to the proposed regulations, the IRS did provide a few clarifications:

- The language of the participant certification (mandatory in 2020) that he/she has insufficient cash or other liquid assets to satisfy the hardship need has been adjusted slightly to require the participant to certify that he/she has insufficient cash or other liquid assets *reasonably available* to satisfy the hardship need. The IRS explained that this was intended to address concerns that a participant may have cash on hand but need that cash for another purpose (e.g., payment of rent).
- In response to questions, the IRS confirmed that its new permanent hardship event for individuals living or working in natural disaster areas identified by FEMA as eligible for individual assistance was intentionally drafted to be narrower than special hardship access rights for particular disasters (such as Hurricanes Harvey, Irma, Maria, Michael and Florence) that the IRS had previously granted. The new permanent withdrawal event does not cover losses incurred by relatives living or working in those areas, and does not specifically excuse collection of supporting documentation. However, the IRS added that it expects employers to be flexible in their documentation requirements in the wake of a disaster.
- The IRS reaffirmed that 401(k), 403(b) and eligible governmental 457(b) plans will *not* be permitted to suspend contributions because someone has taken a hardship withdrawal. This requirement will take effect for hardship withdrawals on or after January 1, 2020, though plans are permitted to implement it earlier.
 - Other types of plans are not subject to this prohibition on future suspensions, so a nonqualified plan may retain or remove a suspension linked to 401(k) or 403(b) hardship withdrawals so long as any action it takes complies with Section 409A of the Internal Revenue Code.
 - Suspension provisions in a plan that are related to non-hardship withdrawals are not covered by the regulations.

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- The new regulations are effective for distributions made on or after January 1, 2020, but can be applied earlier. Early application is available for most provisions for hardship withdrawals made in plan years beginning after December 31, 2018. Elimination of the contribution suspension was permitted as early as January 1, 2019, even for 2018 withdrawals still in their suspension period on that date. The elimination of the natural disaster requirement for principal residence casualty loss withdrawals and the addition of the new withdrawal event for FEMA natural disasters could have taken effect during 2018.

As under the proposed regulations, individually designed plan documents must be amended to reflect the mandatory changes (removal of any contribution suspension provisions associated with hardship withdrawals and, if an amendment to the plan's language is necessary, the IRS' new certification requirement) by the end of the second calendar year after the regulations appear in the Required Amendments List (i.e., December 31, 2021, if the regulations are included in the 2019 list), and amendments relating to any optional hardship withdrawal changes that the employer has chosen to implement are also due by that date. Plans using IRS-pre-approved documents must complete interim amendments in accordance with the normal rules (generally, the later of the end of the plan year of implementation of the change or the deadline for the employer's tax return for the taxable year in which the change is implemented), but the IRS will measure the deadline for all the hardship changes from the deadline for the required changes, even if some of the changes are put into effect earlier. The deadline for Section 403(b) amendments currently is March 31, 2020, but the IRS is considering granting additional time.

Safe harbor plans should be sure to include any 2020 updates in their safe harbor notices for 2020. In the event that an employer decides to make changes during 2020 and did not include those changes in its notice, the plan will be subject to the normal requirements that an updated notice be provided and participants be allowed to change their deferral elections. Generally, the updated notice is due 30 days in advance of a change.

If you have any questions regarding this alert, please contact a member of the Employee Benefits and Executive Compensation Group at 585.232.6500, 716.853.1616, or visit www.hselaw.com.

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