LEGALcurrents®

August 16, 2018

Harter Secrest & Emery LLP

ATTORNEYS AND COUNSELORS

EMPLOYEE BENEFITS AND EXECUTIVE COMPENSATION

RETIREMENT PLAN HARDSHIP WITHDRAWALS: NEW RULES FOR 2019

Author: Leslie E. DesMarteau

Changes to rules governing hardship withdrawals from qualified retirement plans will take effect for plan years beginning after December 31, 2018, pursuant to the Bipartisan Budget Act adopted in early 2018. Although some of the changes require further clarification from the IRS, plan sponsors should begin discussing the changes with their recordkeepers and determining what actions ought to be taken in advance of the new plan year.

Key Changes

- More types of contributions will be available for hardship withdrawal. At present, plans cannot allow hardship withdrawals from post-1988 earnings on elective deferrals, post-1988 qualified nonelective contributions ("QNECs") or post-1988 qualified matching contributions ("QMACs"), including QNECs and QMACs used as "safe harbor" contributions for plans exempt from ADP and/or ACP testing. The new legislation removes this prohibition.
- Employees who take a hardship withdrawal will no longer be required to suspend future contributions to the plan and most other employer plans for six months.
- Employees will no longer be required to obtain plan loans (if available) prior to taking a hardship withdrawal.

Open Questions

The IRS has yet to issue any guidance about the changes, and important open questions remain. However, here are our current thoughts on the open questions as we await further guidance:

- Are the changes mandatory or optional?
  - Since hardship withdrawals are an optional plan feature, we anticipate that employers should be able to decide whether or not they wish to expand the list of hardship-accessible accounts.
  - We believe it is probable that elimination of the six-month suspension on elective deferrals will be mandatory for plans using "safe harbor" designs that exempt them from ADP and/or ACP testing, consistent with the approach the IRS took when Congress reduced the suspension period from 12 months to six months in 2001.
  - We anticipate that the IRS may permit employers to decide whether employees will be required to take loans prior to taking hardship withdrawals, although it is possible that employers

Practice Group Leader
Paul W. Holloway

Retirement
Mark W. Wilson

Health and Welfare
Thomas J. Hurley

Executive Compensation
Christopher M. Potash

Counsel
Leslie E. DesMarteau
Lisa G. Pelta
Joseph E. Simpson

Senior Associate
John W. Brill

Associates
Amanda M. Karpovich
Crosby A. Sommers
Michael R. Staszkiw

Benefits Litigation Counsel
John P. Bringewatt
Megan K. Dorritie
Erika N. D. Stanat

seeking to use the IRS' pre-approved standards for determining whether an employee has a qualifying hardship will need to eliminate this requirement.

- Do all of the changes apply to 403(b) plans?
  - It is not clear whether 403(b) plans will be able to expand the list of hardship-accessible accounts to include earnings on elective deferrals, QNECs and QMACs.

Recommendations

We recommend that plan sponsors discuss the logistics of implementing one or more of these changes with their recordkeepers. Some recordkeepers may be planning to take a particular approach to these changes across their client bases, while others may be more willing to customize their systems. Once an employer understands its recordkeeper's capabilities, it can decide within those parameters what makes the most sense for its particular employee population (subject, of course, to final IRS guidance on any mandatory changes). With that in mind:

- In terms of whether hardship withdrawals should be available from QNECs and QMACs, most employers are likely to follow the approach they take for hardship access to other employer contributions. An employer that allows hardship access to all permissible funds in the plan likely will find it easiest to add these newly permissible accounts to the list of hardship-eligible funds. An employer that only allows hardship access to employee elective deferrals likely would want to simplify plan administration by allowing access to earnings on elective deferrals, but would be less likely to want to allow access to QNECs and QMACs.
- In most cases, eliminating the six-month suspension and eliminating the requirement for participants to take any available plan loans prior to making a hardship withdrawal should simplify plan administration while offering participants more flexibility. As discussed above, we think it is likely that "safe harbor" plans will be required to eliminate the six-month suspension, and it is possible the IRS will require all plans to do so. Also, the six-month suspension requires potentially complicated coordination across various plans of an employer, and thus creates the risk of errors that can be expensive to correct. The requirement that loans be taken out prior to hardship also can generate a great deal of complexity for employers with multiple 401(k) plans. As a result, these changes generally will be desirable, although some employers may be reluctant to increase employee access to hardship withdrawals out of concern that employees will draw down on funds better saved for retirement.

Any changes that the employer is required or chooses to adopt will necessitate a plan amendment. While in most cases, the amendments should be due no earlier than the end of the 2019 plan year, employers should discuss the amendment process and deadline with their plan recordkeepers. This is especially true for "safe harbor" plans, which will need to include any 2019 changes in their safe harbor notices (due by the beginning of December 2018 for calendar year plans).

A key point to keep in mind is that it is not too early to begin determining how to address the new hardship withdrawal rules, especially since recordkeeper involvement is needed and systems may need to be updated.

If you have any questions regarding this alert, please do not hesitate to contact any member of our firm's Employee Benefits and Executive Compensation Practice Area at 585.232.6500 or visit www.hselaw.com.

Leslie E. DesMarteau, 585.231.1273, ldesmarteau@hselaw.com

Attorney Advertising. Prior results do not guarantee a similar outcome. This publication is provided as a service to clients and friends of Harter Secrest & Emery LLP. It is intended for general information purposes only and should not be considered as legal advice. The contents are neither an exhaustive discussion nor do they purport to cover all developments in the area. The reader should consult with legal counsel to determine how applicable laws relate to specific situations. © 2018 Harter Secrest & Emery LLP