

Final Hardship Regulations Revealed! Questions and Answers

1. Regarding the casualty loss change: if a plan is amended to ignore Section 165(h), will it still be within SH hardship rules? and, with respect to Disaster loss: Is a federally declared disaster as defined under Section 165(h) and an area designated by FEMA to receive assistance related to the disaster one and the same? Are these 2 conditions interchangeable? Meaning, if you have one condition, could a participant technically qualify for both types of withdrawals?

A: Yes, that is the essence of the change. The intent is that the hardship safe harbor rules will permit a distribution to cover home casualty losses, even if it is not a federally declared disaster.

The portion of the 401(k) regulations relating to casualty losses (Treas. Reg. 1.401(k)-1(d)(3)(ii)(B)(6) permits a hardship to cover expenses that re deductible under Code Section 165, determined without regard to Section 165(h)(5). Section 165(h)(5) requires that deductible casualty losses be due to a "Federally declared disaster," which is defined in Section 165(i)(5) to be "any disaster subsequently determined by the President of the United States to warrant assistance by the Federal Government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act."

The new FEMA-related hardship event is in Treas. Reg. 1.401(k)-1(d)(3)(ii)(B)(7), which relates to expenses and losses "on account of a disaster declared by the Federal Emergency Management Agency (FEMA) under the Robert T. Stafford Disaster Relief and Emergency Assistance Act ..."

So, clearly, the events constituting a "Federally declared disaster" are the same. And so, there is overlap between the two. The disaster provisions cover residential losses and other expenses in the event of a disaster. The casualty provisions are limited to residential losses, but are no longer limited to federal disasters.

2. Will an applicant still need to provide documentation supporting the amount of hardship being requested?

A: The short answer to this is "yes." How that is provided depends on whether the Plan Administrator requires actual proof or is using the substantiation guidelines pursuant to the 3/7/19 memorandum from Tom Petit to EP Examinations employees (which, by the way, is available on ERISApedia in the "Miscellaneous" section of the IRS "Other" category. It has also been added to the Internal Revenue Manual at § 4.72.2.7.4.1.

If the former, then full documentation must be provided. If the latter, the plan administrator must provide certain information to the participant, the participant must provide certain summary information to the plan administrator and promise to retain the source documents.

3. If an employer provides medical insurance, and hardship withdrawal is requested for medical expenses, must that insurance be taken into account in determining whether an employee has "insufficient cash or other liquid assets reasonably available to satisfy the need"?

A: The regulations provide that the employee's attestation is only effective to the extent that the employer does not have contrary knowledge. I would think that, to the extent that the company provides the medical insurance, then the employer's knowledge of what is covered by the insurance could affect whether the attestation is to be believed. Having said that, however, it is possible that the ability to access care may be dependent on the employee pre-paying the medical provider, whereas the insurance commonly pays only after the expense is incurred. In that situation, I could see a good argument that the existence of insurance does not satisfy the need.

4. If a participant has unreimbursed medical expenses that they have paid - from saving or other means. Can the participant still use those expenses to obtain a hardship from the plan?

A: I would think it would be hard to claim that you don't have other liquid resources when the expenses are already paid. But, continuing the example in the prior answer, you could have a situation where the employee prepaid expenses out of the rent money, and still needed a hardship distribution to replenish the account.

5. What documentation would you need to provide to substantiate under new casualty loss rules?

A: The IRS substantiation guidelines note that the Plan Administrator must confirm the following items:

Repairs for Damage to Principal Residence • Is this the participant's principal residence? • Address of the residence that sustained damage • Briefly describe the cause of the casualty loss (fire, flooding, type of weather-related damage, etc.), including the date of the casualty loss • Briefly describe the repairs, including the date(s) of repair (in process or completed)

In addition, the Plan Administrator would need to get information as to the cost of the repairs at issue. If the substantiation guidelines are not being used, then, the Plan Administrator would need receipts and the like to show that the repairs were actually done to the property at issue and for the purposes claimed, or at the very least, a contractor's estimate.

6. Please go over federal disaster rules again - Do you need a federally declared disaster?

A: If you want to take a hardship due to casualty losses on your home, all you need is the casualty loss to occur (no federally declared disaster). If you want to take a hardship to cover other losses related to a disaster (such as lost wages or loss of personal property), then it needs to be a FEMA-declared disaster.

7. If loans are permitted for hardship necessity only - will be use these new rules for loans as well?

A: This type of limitation is one imposed by the plan. Therefore, the plan document language (or the language of the loan policy) will control. But, it makes sense that the definition of "hardship" used for the plan would suffice for that purpose, if that is what the employer desires.

8. The regulation indicates that an employee must have "obtained all other currently available distributions (including distributions of ESOP dividends under section 404(k), but not hardship distributions) under the plan and all other plans of deferred compensation, whether qualified or

nonqualified, maintained by the employer." Do most practitioners require employees to take a qualified reservist or uniform services withdrawal before taking a hardship withdrawal if he/she is otherwise eligible for such withdrawal? A technical reading indicates that an employee would be required to take such withdrawal.

A: I think the concept is that, if the person is eligible to get any other kind of distribution, he or she should do so. So, yes, I believe those withdrawals should be taken first.

9. Can the employer rely on the participant's self-certification of the amount needed for the hardship instead of submitting documentation?

A: only if the IRS's substantiation guidelines are used, and then the participant is not simply self-certifying, but providing a summary of the expenses.

10. How will documentation/certification requirements for the federal disaster safe harbor be determined?

A: See #5 above re casualty losses. For the other losses, there is no current IRS guidance, but logic would indicate that you would (a) proof or a representation of a residence or business in the disaster area; (b) documentation to indicate the amount of the losses (e.g., if the person's pay was docked due to absence related to the disaster, perhaps a comparison of the paycheck prior to the disaster and the paycheck during the disaster period; repair bills or replacement receipts for the related losses). If the substantiation guidelines are used, then the receipts would not need to be provided (just retained by the participant), but the expenses would need to be summarized. The preamble to the final regulations note, "it is expected that plan administrators will be flexible in interpreting plan terms requiring documentation relating to the hardship when processing hardship distribution requests during the difficult circumstances following a disaster." As a practical matter, the employer will often know, based on payroll records, the participant's residence, and may very well have first-hand experience as to whether there was a federally declared disaster.

11. What is reasonable for the amount of taxes when you are including taxes in the hardship distribution?

A: There's no specific guidance. You could reasonably use the tax bracket related to the person's income or ask them to represent their bracket. Perhaps you could make use of their withholding certificate to estimate the taxes, adjusting for the 10% premature distribution penalty as appropriate.

12. Must 'need' be totally satisfied or can it be partially satisfied?

A: if what you are asking is whether, if the person has the wherewithal to cover some but not all of the expenses related to the need, it makes sense that the hardship withdrawal would be available to cover what the person couldn't afford with other resources.

13. If the plan sponsor decides to adopt an amendment to ignore the "federally disaster area" limitation, are they still allowed to approve hardship for losses outside of the residential damage? Is that 2 separate options or do they go together?

A: These are two different hardship causes. So, if your house is damaged, all you need is the casualty loss to qualify (if the plan is amended to use the newly permitted definition in that regard). If you are trying to get reimbursement for other than casualty losses to the home, you need the new FEMA-related hardship event. See Q#1 above for how these two hardship events interrelate when there is a FEMA-declared disaster.

14. After 12/31/19 can the plan administrator continue to obtain actual documentation vs. relying on participant representation?

A: Yes.

15. Can you confirm on the suspension elimination effective 1/1/2020, would that apply to a hardship taken in 2019 that the participant is on a suspension on 1/1/2020, should the suspension be removed effective 1/1/2020?

A: You can apply the rule either way. So, you can eliminate the deferral suspension requirement only with regard to distributions occurring on or after 1/1/20 (or such earlier date on which you decide to eliminate the rule), or you can eliminate the suspension requirement for anyone who is currently being suspended.

16. So, is the suspension rule tied to the other necessity rule changes, as far as amendment timing? If a plan has already waived the suspension rule (beginning 1/1/2019) then are they required to abide by (and amend for) the other necessity rules for 2019.

A: You can amend each part of the new rules separately. So, you can eliminate the suspension rule for 2019, but not permit casualty loss distributions unless there is a FEMA event until 2020 (or forever, if desired).

17. On the effective date of 1/1/2020, is it 1/1/2020 for all plan years or is it based on your first plan year in 2020? For example if you have a 4/1 plan year, does the rule still go back to 1/1/2020 or 4/1/2020?

A: The suspension rules may not apply to any distribution on or after 1/1/20, regardless of the plan year.

18. You will likely cover this but in case you don't - is there a Sponsor Level Amendment to make these changes across all of our plans? Using Sungard documents (PPA PPD prototype) - I see a plan level amendment checklist was sent but it mentions Sponsor-Level amendment in the "note" of this checklist.

A: It is reasonable to assume that preapproved document sponsors, such as FIS, will provide amendments to be used. FIS will provide both individual and sponsor level amendments. Other providers may make different choices. Whether they will be sponsor-level or plan-level amendments will depend on whether the sponsor is willing to make all discretionary decisions on

behalf of the adopting employers. Because of the variations in the provisions that are available, it is more likely that you will want to have the individual employers adopt their own amendments.

19. What about Davis-Bacon contributions? Will those be allowed effective 1/1/2020 for hardship distribution?

A: I do not believe that any limitations on distribution are required by Davis-Bacon rules; I believe that all limitations on distributions were caused by the fact that 401(k) plans and QNECs are commonly used to provide Davis-Bacon required contributions. Therefore, barring anything else in the plan, Davis-Bacon contributions should be available for hardship distributions under the new rules.

20. What if a hardship was requested and approved on 12/28/2019, can the 6-month of suspension still apply (given it is prior to 1/1/2020)?

A: Yes, so long as it is distributed prior to 1/1/20 and the plan so provides.

21. Can any Safe Harbor Account be used for a hardship distribution?

A: Yes.

22. In regard to safe harbor contributions, you indicated ADP Safe Harbor contributions. For clarification, does this include the employer safe harbor match and/or safe harbor non-elective contributions?

A: Yes. The final regulations clarified that it also includes QACA contributions.

23. What about amendments to 457(b) plans?

A: 457(b) plans do not permit hardship distributions. They do permit distributions for unforeseeable emergencies. The regulations do not include safe harbors or restrictions on funds sources, and so there is no need for amendments to 457(b) plans. Please see ¶8.2 of the 457 Plan eSource for an in-depth discussion of the unforeseeable emergency rules

- 24. DERRIN – Participant shared - Slide has typo that effective 01/01/2000 rather than 01/01/2020**

A: Thank you. We have corrected it for the next program.

25. Assuming a Plan does nothing to eliminate suspension for 2019... What about suspensions that have recently started - are they lifted 1/1/20 or do they last the full 6 months?

A: Whatever the plan sponsor wants to do and the ultimate amendment provides.

26. Under prior rules, the maximum available hardship calculation had to take into account prior distributions from deferrals. Does that still apply with the new rules?

A: as the amount available for distribution due to hardship is not limited to deferrals, there is no need to do this calculation anymore.

27. What about safe harbor notices?

A: If your safe harbor notice discusses distributions (and it should), you will need to give notice of the change in the hardship rules within 30 days after adopting the amendment, per Notice 2016-16. Derrin recommended on the webcast that you do a joint safe harbor-SMM notice to kill two birds with one stone.

28. If a prototype k plan did not make any of the available changes in 2019 but will as of 1/1/2020 what will be the due date for the amendment?

A: The tax return due date (including extensions that are actually taken) of the employer that covers January 1, 2020.

29. Please give deadline examples for off-calendar plan years.

A: In these examples, assume that the employer is a C Corporation filing form 1120, and that it does not file an extension request. The due date of the tax return is 3 ½ months after the end of the tax year. The plan is a preapproved 401(k) plan.

Example 1: Suppose the plan year and the tax year end June 30. The employer amends the plan effective July 1, 2019. The amendment deadline is October 15, 2020, the due date of the tax return for the tax year ending June 30, 2020.

Example 2: Suppose the plan uses a calendar year, but the corporation has a June 30 tax year. The employer amends the plan effective January 1, 2019. The amendment deadline is the later of October 15, 2019, the due date of the tax return for the tax year ending June 30, 2019, or the last day of the plan year, December 31, 2019.

Again, we hope the IRS will provide further, and more generous guidance.

30. The tax return deadline referred to - the 5500 return deadline or the employer's tax return (1020 etc.) deadline?

The employer's deadline

31. The extended due date is regardless if the company actually extends?

A: No. The employer must file an extension request to obtain the benefit of the extended date.

32. If the business does not extend, then the amendment is due on March 15/April 15?

A: Yes, or other appropriate tax filing deadline depending on the tax year.

33. Dispute your calendar year plan with May tax year example. Don't you have until the later of tax year filing deadline of end of plan year?

A: Thank you. Yes. See Example 2 in Question 29.

34. Do plans that are terminating need to adopt a hardship amendment as long as the plan assets are all distributed before the deadline to adopt the amendment?

A: Yes, they must adopt. Plan termination cuts off the period to adopt needed amendments. If the plan has implemented any of the provisions of the new rules, they should adopt the amendment as part of the termination process.

35. Our document provider is telling us if we did not implement all the changes in 2019, so maybe did not implement the change to include earnings, we have until the tax filing deadline for 2020 return - so 9/15/2021. Did you see anything like this?

A; There are a lot of interpretations out there. We gave the most conservative interpretation. Frankly, given a strict reading of the preamble and the underlying revenue procedures, I think that approach is unwarranted. But reasonable minds can differ.

36. So if you don't adopt early when is the required amendment needed?

A: Suppose a preapproved 401(k) plan adopts the changes effective January 1, 2020. The plan year and the tax year are both the calendar year. The deadline is the extended due date of the 2020 return.

37. Can 403(b) plans use the remedial amendment period to correct through 3-31-2020?

A: Yes. In fact, based on Rev. Proc. 2019-39, they likely have until December 31, 2020 to adopt the hardship amendment if the changes were implemented in 2019.

38. Has the restatement date for 403(b) plans changed from 3/31/2020 to 12/31/2020?

A: No. The restatement deadline remains 3/31/2020. The only thing that has changed is the deadline to adopt hardship provisions or certain other amendments, but the end of the remedial amendment period for 403(b) plans remains 3/31/2020.

39. We (TPA firm) are finding that a lot of investment institutions are choosing and implementing the hardship changes for their plan sponsors without regards to whether or not the plan document has been amended yet. Every institution is different, but in general they seem to be notifying the client "we are making the following changes unless you tell us otherwise". Some did it for 2019 and some are doing it for 2020. In general, what impact does this have? (Financial institution operating differently than plan document)

A: Can you say operational failure? As we do the amendments, we need to discover what practices the employer has been following and craft the amendment to those practices. In some cases, this may mean learning what the record-keeper has been doing. If the practices and the amendment provisions don't match, then the plan will have an operational failure.

40. If the participant paid an eligible hardship expense with their credit card, but they do not have the means to pay the bill on their credit card, is that eligible for a hardship distribution?

A: I think the analysis in questions 3 and 4 applies here.

41. Does the plan have to allow substantiation - can the plan sponsor require the participant provide proof?

A: Absolutely, yes. They can also wear a heavy sweater outside on a warm day. But we don't recommend it.

42. Disaster Relief Area - how long after the disaster do you have to file the request?

A: There is not a specific time limit, any more than there is a time limit to requesting a hardship distribution for a funeral expense. However, the longer we go after the event, the more questionable it becomes.

43. How do deadlines for amendment work with the mandatory restatement for the 6yr cycle for pre-approved plans? Sounds like we will need snap on amendment for the interim.

A: There is no question at all we will need a snap-on amendment. The hardship rules came out after the 2017 Cumulative List, and therefore will not appear in the Cycle 3 documents the IRS is currently reviewing. This amendment should survive the Cycle 3 restatement and will not appear in a preapproved document until the Cycle 4 restatement, more than 6 years from now.

44. If amendment adopted for 2019 by 3-15-20, how does that effect 2019 SH notice; by then 2020 is latest SH notice?

A: Notice 2016-16 applies even to retroactive amendments. You give an updated safe harbor notice (the 2020 notice, obviously) and allow people to change deferral elections. In my view, however, if the employer shifted from safe harbor to ADP-tested for 2020, you would not provide an updated notice; there would be no point.

45. What is the amendment due date if the sponsor tax return is April 15, 2020 but they filed the return in Feb 2020?

A: April 15, 2020.

46. Some of the material I read said hardships would be extended to the primary beneficiary. I am assuming that did not happen. Is that correct?

A: That happened in 2006 with PPA, but it hasn't been incorporated into the final regulations until now. What the final regulations clarified is that the employer has the option or not to expand hardships for funeral, education, and medical expenses to include expenses of the participant's primary beneficiary. The final regulations also provide a definition of primary beneficiary as "an individual who is named as a beneficiary under the plan and has an unconditional right, upon the death of the employee, to all or a portion of the employee's account balance under the plan"

47. SH notices are going out now, the amendment doesn't need to be adopted for another year and a half, but the plan cannot allow the 6 month suspension starting on 1/1/20. So our SH notice will be incorrect.

A: Ideally, since we KNOW (and have known for over a year), that suspensions would not be allowed beginning January 1, 2020, the notices would correctly reflect that. However, you can use Notice 2016-16 to issue an updated notice to correct the prior notice once you amend the plan.

48. If we follow the substantiation guideline, and the plan gets audited, but the participant has left employment by that time, what happens then?

A: The IRS was well aware of this issue when they provided the guideline. The instructions to auditors in situations covered by the guidelines is that they are not to request the underlying documentation except in unusual circumstances, and then only with manager approval.

49. You mentioned a plan sponsor can amend to ignore the new casualty code; do you then lose the expansion for hardship on expenses & losses related to federal disaster area. is it an all or nothing?

A: You can change the casualty definition or not. You can adopt the disaster provision or not. Those are independent choices.

50. Sorry I'm a chimp. I'm a financial advisor. Is this something that the record keeper or TPA will have to do or do I need to follow up with them to make sure that they are on top of these changes?

A: Do you have a service agreement with your client? Does it say you are reasonable for this? If it doesn't, then I wouldn't expect this to be an area the financial advisor would handle. But relationships vary.

51. Do you expect them to extend the amendment adoption date of a pre-approved plan document before company tax returns are due so know if they have to file an extension for provisions made effective of 2019?

A: I long ago learned the follow of expecting anything from the government on issues such as this. If we get it, I'm grateful. And in the meantime I'm acting as though what we've got is what we're going to get.

52. What are the BRF rules for if a plan implemented the new hardship rules effective 1/1/19, but there was no SMM that went out yet to explain the new rules. If the sponsor operates the hardship non-discriminately to all participants, are we ok? Maybe effective availability would be an issue? But if the hardship application was reflective of the new rules, would that cover effective availability?

A: I don't see that there will be questions on effective availability, so long as the employer treated all hardship requests the same. If, for example, beginning in 2019 the plan stopped

making 6 month suspensions and demanding participants take loans first, then the absence of advance notice should not have been an issue. Remember, in normal situations (unrelated to safe harbor plans), the SMM is due 210 days after the end of the plan year.