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Suspension of Loan Payments to a 401(k) Plan

As job losses mount in response to the COVID-19 outbreak, plan sponsors looking to mitigate the impact on employees facing termination or reduction in hours and who have outstanding loans from their 401(k) plans, have some tools which could provide some needed relief. Under existing guidance, 401(k) loan payments can be suspended for up to one year due to a leave of absence. Under the loan suspension rules, participants must be on leave without pay or the rate of pay (after income and employment tax withholding) during the leave period must be less than the amount of the installment payments required under the terms of the loan.

After the leave ends, the loan (including interest that accrues during the leave of absence) must be repaid by the latest permissible term of the loan (i.e., 5 years from the date of the original loan, unless the loan is a home loan) and the amount of the installments due after the leave ends must not be less than the amount required under the terms of the original loan. If the original length of the loan was less than the maximum period for a loan (i.e., 5 years for non-residential loans) the loan period can be extended to the maximum permissible period.

When payments resume following the leave, the installment payments may be adjusted for the remaining term to cover the missed payments, or the same payment amount may resume. If the same payment amount resumes, then a balloon payment might be due at the end of the term.

If the plan, loan policy and procedure or the loan itself does not contemplate loan suspensions, the applicable document can be amended to include the loan suspension rule.

An additional advantage to placing employees on leaves of absence or furlough, is that in many states, zero or reduced-hour employees remain eligible for unemployment benefits.

If you have questions, please contact Bodman attorney **Dave Walters** at (248) 743-6052 or dwalters@bodmanlaw.com