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An Update From Bodman PLC

Bodman PLC | COVID-19 Response Team Website

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Participant Access to 401(k) Retirement Accounts

As the COVID-19 pandemic continues, sponsors of 401(k) plans should anticipate that financially distressed participants will want to access their accounts as a means to replace lost income. Sponsors should review their plan documents to familiarize themselves with the options that are available under their plans. While each 401(k) plan is different, many plan designs include the following features which may allow participants to access their accounts.

In-service withdrawals. Generally, in-service withdrawals are limited for participants who continue to be employed. If the plan includes in-service withdrawal provisions, withdrawals are typically limited to certain accounts and satisfaction of conditions (e.g., withdraw employer contributions that have been in the plan for at least 2 years, or after the individual has been a participant for a predetermined number of years). Plans can be amended to add in-service withdrawals but care should be exercised, given in-service withdrawals are protected benefits which can only be eliminated with respect to future benefit accruals.

Hardship Withdrawals. Most 401(k) plans that permit hardship withdrawals follow the IRS safe harbor guidelines. One of the safe harbor reasons includes a distribution to a participant eligible for FEMA "disaster" relief. FEMA has yet to declare a COVID-19 "disaster." Accordingly, COVID-19 disaster requests may be outside of the safe harbor and not available at this time. A request based on one of the other safe harbors may still be available. Congress is considering relief which may make hardship withdrawals more readily available. Alternatively, sponsors could amend their plans to apply a facts and circumstances test to allow for withdrawals due to COVID-19 that result in an immediate and heavy financial need.

Loans. Many 401(k) plans permit participants to access their accounts via a loan. The plan rules regarding eligibility should be confirmed. The maximum amount that a participant may borrow may not exceed the lesser of $50,000 or 50% of the participant's vested plan account. Importantly, in view of the significant investment losses experienced by many 401(k) plan participants, the 50% requirement need only be satisfied at the time the loan is made and need not be periodically reevaluated. Additionally, the loan must be repaid over 5 years with level amortization. Sponsors may want to reconsider limitations imposed on the number of loans that might be available to participants.

Distributions. If the employee has been terminated (voluntary or involuntary) they would generally be eligible to receive a distribution of the amount credited to their account. A distribution which is not rolled over would be subject to withholding.

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