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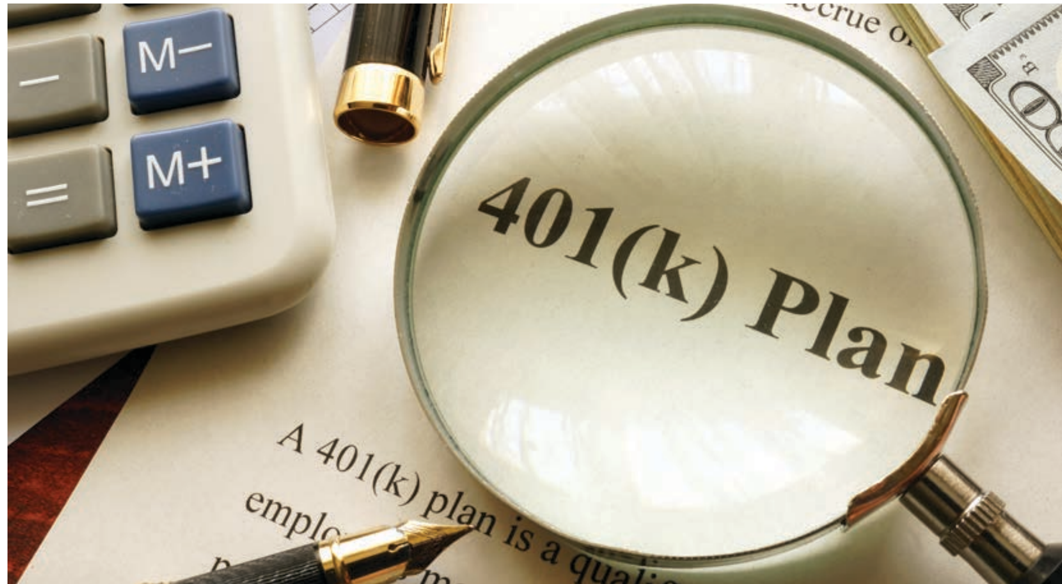
Proposed IRS Regulations For Hardship Distrubutions Offer Welcome Guidance



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Included in the February 2018 Bipartisan Budget Act were important changes to the hardship withdrawal rules for defined contribution plans (401(k) and 403(b) plans) and a directive ordering the Treasury Department to modify its related regulations. On November 14, the Treasury Department issued proposed regulations addressing these changes. These regulations would relax many of the existing rules governing hardship distributions.

While the regulations are in proposed form and plan amendments are not yet required, the regulations offer important guidance for plan sponsors. We recommend that plan sponsors discuss the new rules with their counsel and third-party administrators before the end of 2018.

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The proposed regulations:

- eliminate the requirement that employee contributions be suspended for six months following a hardship distribution

- eliminate the requirement that a participant take any available plan loans before taking a hardship distribution

- allow hardship distributions from qualified non-elective contributions (QNECs), qualified matching contributions (QMACs), employer safe harbor contributions and earnings on those contributions, as well as earnings on 401(k) contributions.

The proposed regulations generally apply the same rules to 403(b) plans, except that QNECs and QMACs held in a custodial account and earnings on 403(b) elective deferrals remain ineligible for hardship distributions.

The regulations would also modify the safe harbor list of expenses that are deemed to be a basis for a hardship distribution and add to that list expenses or losses incurred as a result of a federally declared disaster. For hardship distributions made on or after January 1, 2020, the proposed regulations further provide that a distribution is treated as necessary to meet a qualifying expense only if the employee first obtains all available distributions from qualified and nonqualified plans maintained by the employer and represents that he or she has insufficient cash or other liquid assets to satisfy the qualifying expense. Plan administrators may rely on these employee representations unless they have actual knowledge to the contrary.

These changes may generally be implemented for plan years beginning after 2018. While the expansion of available sources for hardship distributions and the elimination of the requirement that a participant first take a plan loan are voluntary changes, the proposed regulations *require* that, for any hardship distribution made on or after January 1, 2020, a plan may not impose the six-month suspension of employee contributions as a condition of obtaining the distribution.

We encourage plan sponsors to review their hardship distribution rules before the end of 2018, evaluate when and whether to make any of the permitted changes, plan to implement the required changes no later than January 1, 2020, and coordinate the necessary operational changes with their third-party administrators.