

IRS NOTICE 2020-50 – This notice provides guidance regarding provisions of the CARES Act permitting qualified individuals to take penalty-free distributions from eligible retirement plans.

Exception for Coronavirus Distributions from Early Distribution Penalties.

The starting point for any discussion is the general rule that there is a 10 percent early distribution penalty for a distribution from a retirement plan before the account owner reaches age 59 ½ (unless there is an exception) and a 25 percent penalty if the early distribution is from a SIMPLE IRA that has not had a contribution in at least two years. There are exceptions to those penalties, and a “coronavirus related distribution” was added under the CARES Act. This penalty-free exception is capped at \$100,000 per person.

Two other aspects differentiate a coronavirus-related distribution from the treatment of an otherwise early distribution.

- Three years to include the distribution in income. As a general rule, a distribution from a retirement account is includible in income for the year in which the amount is distributed. A coronavirus-related distribution provides another exception to a general rule allowing the account to be included in income ratably over three years starting in 2020. If the account owner desires, an election can be made to include all the distribution as income in 2020.
- Three years to rollover. As a general rule, an account owner who wants to exclude a distribution from income may return it to the eligible account by “rolling over” the amount back to the account within 60 days of receiving the distribution. The 60-day requirement is waived under certain circumstances; and for coronavirus related distributions, the rollover may be within three years of receipt.

A “coronavirus-related distribution” must meet three key requirements: (1) the distribution must be made any time between January 1, 2020, and December 31, 2020; (2) it must be from an eligible retirement plan, and; (3) it must be made by a “qualified individual.”

Under the specifics of the CARES Act, a “qualified individual” is someone (1) who was diagnosed with SARS or COVID-19; (2) whose spouse or dependent was diagnosed with COVID-19; or, (3) who experienced an adverse financial impact as a result of (a) being quarantined, furloughed or laid off, or having work hours reduced due to COVID-19; (b) being unable to work due to lack of childcare due to COVID-19; or (c) closed or reduced hours of a business owned or operated by the individual due to COVID-19.

IRS Notice 2020-50 takes the definition of a “qualified individual” to an expanded level definition. Under the IRS notice, a qualified individual would be eligible for the penalty-free benefit,

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income spread of three years, and the three-year rollover if the individual's spouse or member of their household (must share the principal residence) faces an adverse financial consequence of COVID-19. An adverse financial consequence would include being the result of a reduction in pay (or self-employment income), rescission of a job offer, or delayed employment start to the individual, the spouse, or member of the household.

There are a number of other aspects of IRS Notice 2020-50 that should be considered along with the individual's financial and/or tax advisor.

A "Qualified Individual" Does Not Have to Have a Need to Take a Coronavirus Distribution.

If an individual is a "qualified individual," a distribution may be taken with the penalty-free benefit and roll-over benefit regardless of any showing of a financial need as a result of COVID-19. In other words, the distribution can be taken; and the IRS will not require that the individual prove there was an actual financial hardship to justify the distribution. Whether or not this is a wise decision for an individual can only be decided on that individual's circumstances.

The IRS notice makes clear that a qualified individual may take a coronavirus-related distribution from a beneficiary account under an employer-sponsored retirement plan or beneficiary IRA. The income is eligible to be spread ratably over three years.

Regarding distributions from any "inherited" retirement account, the IRS notice makes it clear that rollover provisions for a coronavirus-related distribution will apply only if the beneficiary is the surviving spouse of a deceased account holder and not to any other beneficiary of an inherited IRA. Related to this concept is that a distribution that is not eligible as a rollover cannot qualify as a coronavirus-related distribution. There is an exception to a hardship distribution, if it would otherwise meet the requirements of a hardship distribution; and under that exception, the coronavirus-related distribution rules may apply and be rollover eligible.

Finally, IRS Notice 2020-50 confirms that "required minimum distributions" (RMDs) from qualified plans do not have to be taken in 2020; and any distribution which would have been an RMD (except for the CARES Act) is eligible for the rollover distribution and eligible for the distribution benefits if taken by a "qualified individual." This does not apply to RMDs from defined benefit plans.

MendenFreiman cannot provide any universal advice regarding taking or not taking coronavirus related distributions, and nothing in this article should be viewed or relied upon as legal or financial advice to anyone reading or reviewing this article. Each individual and their family members will face different decisions as a result of COVID-19, and their specific income circumstances and any action taken should only be done after consultation and review with one of our attorneys.