Federated Hermes

Covid-19: The Latest for Plan Sponsors and Advisors

New IRS, DOL and SEC Guidance and Enforcement Policies Related to the Pandemic and the CARES Act

As of May 21, 2020

Key IRS CARES Act FAQs:

- If Coronavirus Related Distribution (CRD) rolled back into a plan or IRA before end of the third year, no Federal tax—amend prior returns to get back any tax already paid.
- Eligible individuals get CRD tax treatment on distributions, even if plan doesn't adopt CRD.
- CRD income can be divided equally over three years OR declared all in 2020.
- Defined benefit (DB) distribution rules not waived by CRD, distributable event and spousal consent apply.
- Until more guidance issued, see Hurricane Katrina Guidance in Notice 2005-92.

DOL Guidance and Enforcement

- Temporary non-enforcement policy for delinquent participant contributions and loan repayments if solely because of COVID.
- Disclosure relief: will not violate ERISA for failure to timely furnish notice, disclosure or document during COVID emergency if (1) act in good faith, and (2) provide as soon as administratively practicable. Applies to annual funding notices, summary plan descriptions (SPDs), summary of material modifications (SMM), qualified default investment alternative (QDIA) notices, summary annual reports (SAR), 404(a)(5) disclosures, etc.
- Can use electronic and website disclosure as part of good faith effort.
- Clarifies that CARES Act loans do not violate ERISA's adequate security and reasonably equivalent basis requirements.

SEC/FINRA Guidance & Enforcement

- Regulation Best Interest and Form CRS not delayed—go into effect on June 30.
- Registered investment advisors (RIA) "may" need to disclose Paycheck Protection Program (PPP) on Form ADV if it is "material fact" relating to the advisory relationship with client.
- BDs don't have to disclose PPP loans on Form U-4 unless they are not forgiven.
- SEC opening "voluntary" PPP enforcement sweep gathering information on PPP loans.

Not surprisingly for a law written in just a few days, the CARES Act relief package wasn't perfect, and plans and their service providers have been burning some midnight oil as a result. The retirement provisions raised a lot of real-world implementation issues for which there were often not clear answers. The Paycheck Protection Program (PPP) offered employers forgivable loans if they kept their employees on the payroll, but a flood of applicants, vague standards, and controversy over which types of businesses received loans before the money ran out is leading to investigations from a wide array of Federal agencies, including the SEC. Finally, the pandemic is making it hard to carry out many of the "normal" administrative duties involved in running plans. To address all of these issues, plans and service providers looked to the regulators for new rules, guidance, and enforcement relief. IRS, DOL and SEC are starting to respond, and Congress is considering another round of relief as well.

Will Congress Make more Retirement Changes in the Next Stimulus Bill?

Probably, but it is not yet clear when a new stimulus package might be coming or what will be in it. The Democrat-controlled House passed a new $3 trillion relief bill called the HEROES Act on May 15, but the Republican-controlled Senate is unlikely to allow it to move forward without major revisions and negotiations.

While there was wide bipartisan agreement on the CARES Act, it will take much longer to work out a compromise on the HEROES Act due to the price tag and the underlying policy differences.

The House HEROES Act does have some significant retirement provisions—it would expand the waiver of required minimum distribution (RMD) provisions to include 2019 as well as 2020, and it would reduce defined benefit plan funding requirements. It would also provide some welcome technical corrections to the CARES Act, such as clarifying that employers may deduct wage and benefit costs for workers paid for by a PPP loan, and that plans can rely on participant self-certification of eligibility for Coronavirus related loans, not just for Coronavirus Related Distributions (CRD). It is likely that Congress will make a deal and pass another stimulus bill, and it likely will have some new retirement provisions in it, but the legislative process may take some time.

President Trump Issues New "Deregulatory" Executive Order

While Congress debates the HEROES Act, President Trump issued a new "Executive Order on Regulatory Relief to Support Economic Recovery" on May 19. The new Executive Order calls on Federal agencies to review actions already taken in response to the pandemic and to identify new "deregulatory" activities to pursue that will assist the county in recovering from the economic effects of the pandemic. The guidance discussed below predates this new Executive Order—it remains to be seen how aggressive agencies will be in changing rules in response to this new directive.

IRS Issues Some Guidance—FAQs on the CARES Act

On May 4th, the IRS posted 14 questions and answers on Section 2022 of the CARES Act. While this guidance answered a few significant issues, it did not address all of the important questions on which the regulated community has requested guidance. In question #2, the IRS noted that further guidance was coming, but it went on to suggest that until this guidance is available, taxpayers should refer to the Hurricane Katrina relief guidance. Specifically, the IRS wrote, "The Treasury Department and the IRS anticipate that the guidance on the CARES Act will apply the principles of Notice 2005-92 [the Katrina Guidance] to the extent the provisions of section 2202 of the CARES Act are substantially similar to the provisions of KETRA (Katrina Emergency Tax Relief Act of 2005) that are addressed in that notice."

FAQ Guidance For Plans

Plan Choice: The guidance reiterates that retirement plans are not required to adopt the CARES Act provisions (CRDs, loans and required minimum distribution (RMD) waivers), but may choose to do so. It also notes that plans are not required to accept rollover contributions, but states that the IRS "anticipates" that plans will do so to allow CRD proceeds to be returned.

Loan Payment Deferrals: Question #8 indicates that the plan "may" delay loan payments due between March 27 and December 31, 2020 "for up to one year." This seems to confirm that the CARES Act does not require plans to delay payments due on existing loans, and that this is a plan choice. Whether the CARES Act mandated this deferral on existing loans has been a key question facing record-keepers and plans.

CRD Doesn't Waive Pension Distribution Rules: The guidance clarifies that the CARES Act CRD provisions do not otherwise waive normal pension plan rules. For example, there must be a distributable event for a Money Purchase Pension Plan participant to receive a distribution, and the spousal consent rules still apply.

CRD Participant Self-Certification: The guidance clarifies that the plan may rely on the participant's self-certification of eligibility for CRDs "unless the administrator has actual knowledge to the contrary." (As a practical matter, a self-certification process asking the participant to state that he or she meets "one or more" of the criteria reduces the likelihood that this "actual knowledge" standard would be applicable.)

FAQ Guidance for Individuals

Eligibility: The guidance states that the Treasury Department is considering expanded eligibility criteria, but reiterates that a taxpayer must actually be eligible to receive favorable tax treatment.

Favorable Tax Treatment Even if Plan Doesn't Adopt CRD: The guidance clarifies that even if the taxpayer's plan has not adopted the CRD provisions, any distribution the taxpayer does receive is treated as a CRD for tax purposes as long as the taxpayer is eligible. In other words, the 10% early withdrawal penalty waiver and the three-year income realization would apply to an individual who took a "traditional" distribution where the plan did not adopt the special CRD provisions itself.

Rollover of CRD Proceeds: The guidance clarifies that the individual may rollover some or all of the CRD proceeds into a plan or an IRA. The distribution would then be treated as though it were repaid in a direct, trustee-to-trustee transfer as long as the rollover takes place within three years of the distribution. The IRS further clarified that any taxes already paid in years one or two can be refunded by amending the prior year returns for amounts rolled over in year three.

CRD Income Year: The guidance clarifies that the taxpayer can either realize all of the CRD proceeds in 2020, or spread it out ratably (in other words, in thirds) over 2020, 2021, and 2022. This timing flexibility may matter to taxpayers who anticipate lower incomes in 2020 due to the pandemic, making it advantageous to realize the whole amount in 2020 relative to future years in which they may have higher taxable incomes.

DOL Enforcement Policies and COVID-19 Disclosure, Reporting and Document Relief

On April 28, 2020, DOL issued Disaster Relief Notice 2020-01 which provided deadline relief and enforcement policy guidance for a variety of ERISA-related deadlines and requirements. Further, on May 4, 2020, DOL and IRS jointly issued a final regulation extending time frames for certain ERISA deadlines. In general, the period from March 1, 2020 until 60 days after the declaration of the end of the COVID-19 National Emergency ("the Outbreak Period") is disregarded for these deadlines.

DOL Disaster Relief for Furnishing Notices, Disclosures and Documents

For retirement plans, the DOL Disaster Relief Notice explains that it will not be a violation of ERISA to fail to timely furnish a notice, disclosure, or document that is required to be furnished during the Outbreak Period if the plan and responsible fiduciary:

1. act in good faith, and
2. provide the information "as soon as administratively practicable under the circumstances."

The types of documents to which this applies include annual plan funding notices, Summary Plan Descriptions, Summaries of Material Modifications, QDIA notices, Summary Annual Reports, participant fee disclosures, and certain loan-related disclosures.

This relief does not mean than plans can ignore the requirements during the Outbreak Period. DOL explains this by suggesting the type of actions that would constitute good faith alternatives to full compliance. For example, DOL would expect to see the "use of electronic alternative means of communicating with plan participants and beneficiaries who the plan fiduciary reasonably believes have effective access to electronic means of communication, including email, text messages, and continuous access websites."

The Disaster Relief Notice also provides clarification for "blackout" notices. These are required to be provided to individual account plan participants 30 days in advance of any temporary suspension, limitation, or restriction of participant rights, such as the ability to direct investments. The new relief explains that the exception to the advance blackout notice requirement in the existing blackout notice regulations—which apply when a plan administrator is unable to provide advance notice of a blackout period due to events beyond the plan administrator's reasonable control—is applicable here because "pandemics are by definition beyond a plan administrator's control."

DOL Delinquent Contributions Non-Enforcement Policy

The single most common violation DOL finds in its plan investigations is delinquent contributions—a failure to deposit timely participant contributions or loan repayments withheld from pay into the plan trust in accordance with DOL regulations. Recognizing that the disruption caused by the pandemic may make these payroll processing issues more difficult, DOL announced that it will not take enforcement action with respect to a temporary delay in forwarding these payments or contributions to the plan,but only "solely on the basis of a failure attributable to the COVID-19 outbreak." DOL goes on to say that this enforcement policy requires plans and service providers to act "reasonably, prudently, and in the interest of employees to comply as soon as administratively practicable under the circumstances."

In other words, DOL is providing a temporary period of relaxed enforcement based on good faith efforts to comply—it is not an exemption from the requirements.

SEC Enforcement and PPP Loans

As part of the CARES Act, businesses were able to apply for SBA-backed loans that would be forgiven if 75% of the money was used on payroll costs and employees remained employed for eight weeks. Controversy followed when the first $350 billion allocated for PPP loans was exhausted within days, and businesses such as private equity firms and some well-known public companies received loans while some "Main Street" businesses did not. The second round of funding altered the requirements for the program to address this, while providing an additional $310 billion. Following this public controversy, Congress and various Federal agencies are investigating the program and some of the recipients of the loans. The SEC and FINRA have considered the receipt of such loans by registered investment advisors and broker-dealers, and the result is a mixed bag of disclosure requirements and ongoing enforcement efforts.

SEC Investigating Some PPP Recipients

The SEC's Enforcement Division is sending "voluntary" inquiries requesting information from some public companies that received loans, and the SEC is also monitoring registrants who received PPP loans. It is likely that this issue will be part of future exams as well, and registrants should expect to be able to explain the basis for seeking a PPP loan and the effect on their client relationships.

SEC and FINRA PPP Loan Disclosure Guidance

The SEC's Division of Investment Management recently issued controversial guidance stating that registered investment advisors (RIA) taking PPP loans should consider whether such loans require disclosure in amendments to Forms ADV. Under the guidance, if the circumstances leading to the RIA seeking a PPP loan or other financial assistance "constitute material facts relating to [the] advisory relationship with clients," disclosure likely is required. The SEC does not specify what constitutes "material" in this context. However, the guidance states that "[i]f for instance, you require such assistance to pay the salaries of your employees who are primarily responsible for performing advisory functions for your clients, it is the staff's view that you would need to disclose this fact." The guidance further notes that "[i]f your firm is experiencing conditions that are reasonably likely to impair its ability to meet contractual commitments to its clients, you may be required to disclose this financial condition."

By contrast, FINRA addressed broker-dealers' obligations regarding PPP loans in an FAQ that asked, "[i]f a…PPP loan and the loan or part of the loan is forgiven, will the registered person be required to report that forgiveness in response to Question 14K on their Form U4 as a 'compromise with a creditor?'" FINRA responded: "No, provided the PPP loan or part of the loan is forgiven consistent with the original terms."

The SEC's broad position on disclosure is causing some concern among RIAs because they perceive this view as running counter to the purpose of a PPP loan, which assists registrants to stay in business, thus furthering—not impairing—their ability to meet their commitments to clients. Some observers have noted that the SEC's position has prompted worries that disclosure will constitute a form of "PPP shaming."

Conclusion

The Federal regulatory and enforcement agencies are moving relatively quickly to provide guidance and new enforcement policies in response to the pandemic and to changes in the law. The pace of these efforts may increase given the new Executive Order from President Trump. Plan sponsors and their service providers need to pay close attention to guidance from DOL and Treasury in the coming days and weeks, and it is likely more relief legislation is on the way, starting the guidance and enforcement cycle all over again.

About the Author

Bradford Campbell, partner at Faegre Drinker Biddle & Reath LLP, advises financial service providers and plan sponsors on ERISA Title I issues, including fiduciary conduct and prohibited transactions. A nationally-recognized figure in employer-sponsored retirement plans, Brad is the former Assistant Secretary of Labor for Employee Benefits and head of the Employee Benefits Security Administration. As ERISA's former "top cop" and primary federal regulator, he provides his clients with insight and knowledge across a broad range of ERISA-plan related issues. He also serves as an expert witness in ERISA litigation. Brad has been listed as one of the 100 Most Influential Persons in Defined Contribution by 401kWire and has been listed as one of the top 15 ERISA attorneys in the country by a poll of the National Association of Plan Advisors. In addition, he testified before four Congressional Committees regarding the effects of the Department of Labor fiduciary regulation.

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