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## The IRS Issues Proposed Regulations Regarding Hardship Distribution Rules

For plan years beginning after December 31, 2018, the Bipartisan Budget Act of 2018 (the "Budget Act") gave plan sponsors the ability to eliminate certain restrictions on hardship withdrawals. Specifically, the Budget Act eliminated: (i) the mandatory six-month suspension of new elective deferrals following a hardship withdrawal from an employer-sponsored plan; (ii) the requirement that a participant take all permissible plan loans before taking a hardship withdrawal; and (iii) the restriction on taking a hardship withdrawal from qualified nonelective contributions (QNECs), qualified matching contributions (QMACs), and earnings on elective deferrals. Accordingly, the Internal Revenue Service (IRS) has issued proposed regulations executing and expanding on these changes and revising the list of safe harbor expenses for hardship distributions as follows.

***New and Modified Safe Harbor Expenses.*** Pursuant to the proposed regulations, hardship distributions may now be made for qualifying medical, educational, and funeral expenses incurred for a primary beneficiary under the plan and for losses incurred on account of disaster designated by FEMA for individual assistance. The regulations also clarify that hardship distributions relating to casualty losses do not need to result from a federally declared disaster to be distributed on account of hardship.

These revised safe harbor expenses may apply to distributions made on or after January 1, 2018. As such, plans may be amended to apply these revised safe harbor expenses to expenses incurred by a participant in 2018. Plan sponsors should note that, if a plan allowed hardship distributions in 2018 for casualty losses not related to a federally declared natural disaster, the plan sponsor must amend the plan to apply the revised safe harbor expenses to distributions made in 2018 so that the plan's provisions conform to its operation.

***Distribution Necessary to Satisfy Financial Need.*** The proposed regulations modify the rules for determining

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whether a requested distribution is necessary to satisfy an immediate and heavy financial need by eliminating the current facts and circumstances standard and adding a new standard. For a hardship distribution to be deemed necessary under this new standard, the participant must have obtained other available distributions under the plan and must represent that he or she has insufficient cash or other liquid assets to satisfy the financial need. A plan administrator may rely on the participant's representation, unless it has actual knowledge to the contrary. Plan administrators are not required to obtain this representation until January 1, 2020.

***Plan Loans and Suspension of Elective Deferrals.*** Plans generally may provide for additional conditions to demonstrate that a distribution is necessary to satisfy an immediate and heavy financial need. Pursuant to the Budget Act, the proposed regulations modify the conditions plan sponsors may require. For plan years beginning after December 31, 2018, a plan may require participants to take all available plan loans prior to receiving a hardship distribution, but does not have to do so. For distributions made on or after January 1, 2020, plans will be prohibited from requiring a suspension of elective deferrals as a condition of obtaining a hardship distribution. Pursuant to the Budget Act, plan sponsors may amend their plans to no longer require suspension of deferrals for plan years beginning after December 31, 2018, even if the distribution was made in the prior plan year. For example, a calendar-year plan may be amended to allow a participant who received a hardship distribution in late 2018 (and who would be subject to the suspension requirement) to begin making deferrals again as of January 1, 2019.

***Expanded Sources for Distribution.*** As changed by the Budget Act, for plan years beginning after December 31, 2018, the proposed regulations permit hardship distributions from elective deferrals, QNECs, QMACs, and earnings on these amounts. Safe harbor contributions made to a plan with an automatic contribution arrangement may also be distributed on account of a hardship. However, plans may limit the sources available for hardship distribution and whether earnings on those amounts may be distributed. For 403(b) plans, QNECs and QMACs in a custodial account and earnings on elective deferrals will remain ineligible for distribution on account of hardship.

Plan sponsors should consider whether they need to or will implement these changes and plan to timely adopt an amendment and update participant communications accordingly. All changes made by the final regulations, when issued, will be treated as integrally related to a disqualifying provision. As such, plan sponsors will need to appropriately amend their plans by the end of the second calendar year after the Required Amendments Lists is issued listing these changes.

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