Chapman and Cutler LLP

Chapman Client Alert

July 31, 2020 Current Issues Relevant to Our Clients

New Rules Impacting Your IRAs: An Update on CARES Act and SECURE Act

Late in 2019, as part of an appropriations bill, Congress passed the SECURE Act, which changed a number of rules regarding distributions from qualified retirement plans and IRAs. Our January 7 Client Alert discussed the impact of the SECURE Act on traditional and Roth IRAs and reviewed some of the planning options. In late March, as part of the COVID-19 financial relief legislation, Congress passed the CARES Act, which provided some additional rules on distributions from qualified retirement plans and IRAs for 2020. In June, the IRS issued several notices that provide more details on both of these acts. This Alert will cover two primary topics: Coronavirus-Related Distribution Rules and the 2020 RMD Waiver Rule.

Coronavirus-Related Distribution Rules

The CARES Act provides special tax rules for any taxpayer who is eligible to take a “coronavirus-related distribution,” or CRD, from a qualified retirement plan or IRA.

Who does it apply to?

The rule applies to any individual taxpayer who has either a qualified retirement account *that permits a CRD*, a traditional IRA or an inherited traditional IRA. You or your spouse or dependents must have experienced certain financial hardships as a result of COVID-19, such as contracting the coronavirus, having a job loss, experiencing a reduction in pay or hours, closure or reduced operating hours of your business, having a job offer rescinded or delayed, or experiencing an inability to work due to the lack of childcare that is related to the pandemic.

What’s permitted?

If eligible, you may take one or more distributions from a traditional IRA or a qualified employer plan that permits a CRD. The tax benefits of a CRD only apply to: (a) distributions that occur between January 1, 2020 – December 31, 2020, and (b) total distributions, from all qualified plans, up to $100,000.

What’s the tax benefit?

If you are under age 59-1/2, there is no 10% early withdrawal penalty (or 25% penalty for SIMPLE IRAs). The distribution is *still* taxable. If you take a CRD, you will receive a Form 1099-R reporting the distribution as taxable. However, you have a few options for managing the reporting and paying the associated tax liability:

- You can elect to include the distribution, ratably, as taxable income over three years or as all taxable in 2020. You will need to make this election when you file your 2020 tax return, on new Form 8915-E Qualified 2020 Disaster Retirement Plan Distributions and Repayments. *You cannot change this election once it is made.*

- *If the distribution is eligible for a rollover*, you can recontribute the distribution to a qualified plan or traditional IRA within three years (measured from the day after the first distribution) and not be taxed.

    - Not all distributions are eligible for rollover. If your CRD is a required minimum distribution (see the next section) or a distribution from an inherited IRA, you may NOT roll over or recontribute the distribution to avoid being taxed.

If the recontribution of a CRD occurs in a year after the CRD is reported and taxed, you will need to amend the prior year’s tax return. For example, if you elected to report and pay all of a CRD as taxable in 2020, and then recontribute that sum in 2022, you would need to file an amended 2020 tax return, amending Form 8915-E to report the recontributed amount. If, however, you place your 2020 tax return on extension (so it is due by October 15, 2021), and you make a recontribution of the CRD on or before that date (e.g., on October 13, 2021), you may report the recontribution on the 2020 Form 8915-E and eliminate any tax payable on the distribution.

If a person makes a three-year election to report and pay tax on a CRD but dies before the three-year period ends, the remaining unreported amount becomes taxable in the year of death.

Should you take a CRD?

Whether it makes financial and tax sense to take a CRD is highly fact specific. First, if you only have employer-sponsored qualified retirement plans, those plans must permit a CRD.

Second, you need to look at your current financial circumstances, your need for cash and your tax rates in 2020, and balance those against your ability to recontribute the CRD in the next three years, your future retirement needs and future tax rates. If you don't have a financial need for a distribution from a retirement plan or IRA but think you will pay at a lower tax in 2020 (or over the next three years) than in the future, a Roth conversion of a qualified plan or IRA may be a better option than a CRD. A good financial planner or accountant may be able to assist you in analyzing the financial and tax benefits of taking a CRD.

2020 RMD Waiver Rule

The CARES Act waived all required minimum distributions (RMDs) for qualified plans and IRAs, including inherited IRAs for 2020.

Who does it apply to?

RMDs are the required distributions for individuals who are over age 70-1/2 (for individuals born before July 1, 1949) or who have retired or for any individual, trust or estate that is the beneficiary of an inherited IRA. For individuals who were born on or after July 1, 1949, RMDs don't begin until age 72 (which will be in 2021 at the earliest).

What's permitted?

If you normally would have an RMD for 2020, including an RMD for an inherited IRA, you do not have to take the distribution in 2020. You may take it, but it is not mandatory. In addition, if you already took part or all of your 2020 RMD, you may recontribute that distribution to the same qualified plan or IRA, **so long as the recontribution is made by August 31, 2020.** Typically, individuals are not permitted to recontribute or return an RMD, and beneficiaries of inherited IRAs are not permitted any recontribution of a distribution, even a distribution made in error. However, the IRS is permitting recontributions since the CARES Act was only issued in late March and many people had already taken or begun taking their 2020 RMD.

What's the tax benefit?

You don't have to report and pay tax on retirement plan or IRA distributions for 2020 unless you opt to take the distribution or fail to make a recontribution. If you typically direct part of your RMD as a direct charitable contribution to avoid the tax reporting on the distribution, you may still make this charitable contribution, even though you do not have a RMD for 2020.

Future Distributions Impacted by 2020 RMD Waiver

If you previously inherited an IRA that is required to be distributed within five years of the IRA owner's death, the year 2020 will not count in that five-year period. If you inherit a qualified plan or IRA in 2020 and are subject to either the five-year or ten-year distribution period, these periods are NOT extended due to the waiver of 2020 RMD.

If you inherited an IRA for someone who died in 2019, you must typically make an election regarding distribution of that inherited IRA by the end of 2020. This election can be deferred until the end of 2021. However, the date for determining the RMD for an inherited IRA has not changed. The determination of who is a beneficiary of the inherited IRA or qualified plan must still be made by September 30, 2020.

For More Information

If you would like further information concerning the matters discussed in this article, please contact any of the following attorneys or the Chapman attorney with whom you regularly work:

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