The CARES Act
Recent tax law changes may affect your estate plan

The Coronavirus Aid, Relief and Economic Security (CARES) Act is designed to provide tax relief to individuals and businesses struggling to make ends meet due to the COVID-19 pandemic. But this law may also have a long-reaching impact on your estate plan. Notably, the CARES Act includes several provisions for participants in qualified retirement plans and IRAs that could span generations.

Required minimum distributions

Most individuals are familiar with the basic rules for required minimum distributions (RMDs). Generally, you must begin taking RMDs from qualified plans and traditional IRAs after attaining a specified age. Failing to do so results in a tax penalty equal to 50% of the amount that should have been withdrawn, in addition to the regular income tax.

Typically, account owners want to minimize RMDs so they can preserve more wealth for their heirs. But the Setting Every Community Up for Retirement Enhancement (SECURE) Act essentially eliminated the use of “stretch IRAs,” where RMDs from plans or IRAs could be stretched over the long life expectancies of nonspousal beneficiaries. Beginning this year, for those inheriting a retirement account from someone other than their spouse, the account generally must be withdrawn within 10 years of the owner’s death. Consider whether you want to revise your beneficiary designations in light of the new requirements.

Previously, the required beginning date for RMDs was April 1 of the year following the year in which you turned age 70½. However, the SECURE Act postponed the required beginning date from age 70½ to 72, effective in 2020, for those who were not 70½ as of the end of 2019 — that is, anyone born on or after July 1, 1949. This allows account owners the opportunity to accumulate more wealth through tax-deferred compounding.

The CARES Act adds even more protection. It allows you to suspend all RMDs for 2020 — even those for inherited accounts — without penalty. In other words, you don't have to take the usual RMDs, keeping your account intact. If you've already taken RMDs for the 2020 tax year, you have several options at your disposal. (See the sidebar "Available options for early RMDs.")

COVID-19 distributions

The CARES Act carves out special tax breaks for qualified plan and IRA participants who are affected by the COVID-19 pandemic. As with the rules for RMDs, you have more flexibility in managing retirement assets.

For starters, you can avoid a tax whammy if you withdraw funds from a qualified plan or IRA prematurely. Generally, you owe a 10% penalty tax — plus regular income tax — for distributions made before age 59½. But the tax code includes certain exceptions to this general rule (such as for distributions made on account of disability). Now the CARES Act adds to the list in certain situations.

Specifically, the new law waives the additional 10% tax for distributions of up to $100,000 for an individual (or spouse) who is diagnosed with COVID-19 or has experienced adverse financial consequences due to the virus, such as being quarantined, being furloughed or laid off, having hours reduced or losing child care.

Furthermore, although COVID-19 distributions remain taxable, you can choose to pay off the resulting tax liability ratably over three years. Alternatively, you may avoid tax completely by "rolling over" the funds to a qualified plan or IRA within the three-year period. (See the sidebar "Available options for early

RMDs.”) Be aware that the standard time period for a rollover is 60 days from the date of the distribution.

Retirement plan loans

If your 401(k) plan or profit-sharing plan permits it, you can borrow from your account, within certain limits, in times of need. Currently, the loan can’t exceed the lesser of $50,000 or 50% of your vested account balance. For instance, if you have $500,000 in the account, you can borrow only up to $50,000.

Again, the CARES Act provides plan participants with extra flexibility. For hardship loans made between March 27, 2020, and September 23, 2020, you can borrow up to the lesser of $100,000 and 100% of your vested balance.

This gives plan participants considerably more wiggle room. Going back to our example where you have $500,0000 in an account, you can now borrow $100,000 — twice as much as before.

In addition, the CARES Act extends the due date for loan repayments due in 2020 by one year. Generally, loans must be repaid within five years.

Finally, the new law permits employer-provided retirement plans to adopt these provisions immediately even if loans aren’t currently allowed. Note that the plan must be amended by 2022.

Time to review your estate plan

It’s always wise to review your estate plan from time to time, but especially after a potentially significant change in circumstances. Considering that the COVID-19 pandemic may have impacted your plan, it would be an appropriate time to consult with your estate planning advisor to determine if any of your strategies need to be revised.

Sidebar: Available options for early RMDs

The Coronavirus Aid, Relief and Economic Security (CARES) Act allows you to skip RMDs in 2020. But what if you took RMDs earlier in the year? If you did, when was the distribution taken? You may have 60 days to "undo" the distribution by depositing it back into your account. There's a fair amount of nuance with respect to the 60-day rule, and the timing is critical, so if this may be a possibility for you—be sure you understand the specifics. Note, also, that if the amount withdrawn qualifies as a COVID-19 distribution, you can roll the funds into another plan or IRA within three years, which means that there's less urgency to make a decision.

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