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BENEFITS TEAM

How the CARES Act Will Impact Retirement Accounts

The Coronavirus Aid, Relief, and Economic Security (CARES) Act, was passed unanimously by the Senate to help individuals, families, and employers battle the financial ramifications COVID-19 has unleashed upon the world's economy. This 883-page legislation will provide a total of $2.2 trillion in financial relief to Americans.

In addition to this direct economic stimulus, the CARES Act attempts to help individuals and families combat the financial impact of COVID-19 through several changes in group and individual retirement plans. In this article, I'll tell you all about the retirement-related provisions included in the CARES Act. Plus, we'll why these provisions matter and how they could impact your retirement accounts.

Learn all about the 10 key provisions you need to know about the CARES Act.

Who Qualifies?

Not everyone is eligible for the proposed changes to retirement plans in the CARES Act. To qualify, individuals need to meet one of the two main categories for eligibility:

— You, your spouse, or a dependent is diagnosed with COVID-19, the novel coronavirus.

— You have experienced adverse financial consequences as a result of being quarantined, furloughed, laid off, had your work hours reduced, or are unable to work due to a lack of childcare or closures related to the coronavirus epidemic.

What's Changing About Retirement Accounts?

1. Required Minimum Distributions (RMDs)

The SECURE Act, which became law on December 20, 2019, increased the required minimum distribution age from 70 ½ to 72. This new law applies to everyone who didn't reach 70 ½ by the end of 2019. Now, through the CARES Act, retirees have the option to not take required minimum distributions throughout 2020.

Typically, if you're eligible you must take a required minimum distribution by the end of each year or pay a penalty equal to 50 percent of the RMD amount. RMDs are calculated based off an individual's account balances, as of the end of the prior year.

So, the ability to defer these distributions could help millions of retirees from having to take them at a time when their portfolios are down from what were near-record highs on December 31, 2019. Essentially, retirees would be calculating their RMD and taxes owed, based on the value of their portfolio that has subsequently vanished.

2. Hardship Withdrawals and Account Loans

Under the CARES Act, eligible individuals can withdraw up to $100,000, in total, from their retirement accounts. And, these individuals may do so without the typical 10 percent early-withdrawal penalty, as long as they pay back the distributions within three years. Additionally, the law gives people the ability to pay back taxes on loans over a three-year period.

The relief package also doubles the current retirement plan loan limits to the lesser of $100,000 or 100 percent of the participant's vested account balance in the plan. Similarly, individuals with a loan outstanding from their retirement plan, with a repayment due from the date of enactment of the CARES Act through December 31, 2020, can delay repayments for up to one year.

Think Twice Before You Run to Make a Withdrawal…

While these two provisions could be significant and may help a lot of people, many financial experts are warning people to really think about it before you take a retirement account withdrawal or loan. If your overall assets are down in your account a loan or withdrawal may act as a double whammy to the health of your overall retirement account balance.

To begin with, the CARES Act only relieves individuals of the 10 percent early withdrawal penalty that would typically be associated with an early account withdrawal. But individuals still, eventually, owe taxes on withdrawals or loans from traditional 401(k)s or Individual Retirement Accounts (IRAs).

So, if you take these early benefits and have a depleted retirement account, you could end up facing a significant retirement shortfall in your later years. An early withdrawal can be especially painful in the middle of a market downturn. That's because there's an opportunity cost to raiding your retirement savings at an early age.

The opportunity cost you lose out on when you make an early withdrawal from your retirement account is the compounding effect. The compounding effect is one of the most powerful savings tools any individual has. But an early withdrawal or loan on your balance can greatly reduce the effect of compounding.

For example, a $5,000 balance today could be worth $57,900 in 35 years with a standard rate of return of 7 percent. If you take out even a portion of this $5,000 now, the effect from compounding will be greatly reduced. So, make sure you really think about it before taking an early withdrawal or loan from your retirement account. And, if possible, speak to your financial advisor before making any decisions.

The Wrap

The CARES Act could change the way many people use their retirement accounts, especially during this unprecedented time. Still, before you or your employees take advantage of these changes, make sure you talk with a benefits professional or financial advisor.

If you have any questions regarding the CARES Act or these provisions individually, contact The Olson Group, today!