FINANCIAL FOCUS

Tax-deferred Accounts Get (Temporary) Boost from CARES Act

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You need to primarily rely on yourself to protect your health during the coronavirus. But from a financial standpoint, you may have gotten some relief – or at least some flexibility from the recently passed $2 trillion Coronavirus Aid, Relief and Economic Security (CARES) Act.

Retirement account holders, including owners of IRAs and 401(k)s are usually required to start taking distributions from these accounts once they reach age 72. The CARES Act waives these required minimum distributions (RMDs) for all employer plans and IRAs in 2020, with the exception of defined benefit plans. If you've already taken your distribution for 2020, you can put the funds back in your retirement account if you meet certain requirements.

Of course, if you needed – or will need – the money from the RMD for your cash flow needs, you won't have to return it. But if you don't really need the money, avoiding an RMD in 2020 or returning an RMD to your retirement account will give the funds more time to grow on a tax-deferred basis before the RMDs are once again required in 2021.

Another CARES Act provision allows for the 10% early withdrawal penalty to be waived for withdrawals up to $100,000 from qualified retirement accounts, including IRAs and 401(k)s, for individuals who qualify for COVID-19 relief. Qualifying individuals include those who are diagnosed with COVID-19, have a spouse or dependent who is diagnosed with COVID-19 or experience adverse financial consequences as a result of COVID-19, including quarantines, layoffs, business closures or child care responsibilities. Income tax on the distribution would still be owed but could be paid over a three-year period. Employer plan participants also may increase the amount that can be taken as a loan from a qualified retirement plan from $50,000 to $100,000 for 2020. While the CARES Act allows these penalty-free withdrawals and increased plan loan amounts, you will need to contact your plan administrator to determine whether these options are available in your plan.

Even though you may be able to access these funds penalty-free, it doesn't necessarily mean you should do so. Try to exhaust some of the other provisions in the CARES Act first, such as the mortgage or student loan relief, or using the direct payment to bridge the gap on current expenses before taking a distribution or loan from your retirement account. If you decide to take a withdrawal or loan, work with your financial advisor to consider developing strategies to contribute/pay back these funds over time to reduce any long-term impact to your retirement goals.

Please consult with your tax professional before making any CARES Act-related moves with your retirement accounts. Partnering with your tax and financial professionals can help in the decision-making process. In the meantime, stay safe, stay healthy and keep looking forward to brighter days ahead.

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