Changes under the CARES Act for Senior Citizens

The Coronavirus Aid, Relief, and Economic Security (CARES) Act, passed on March 27, 2020, aims to relieve some of the financial consequences of the Covid-19 outbreak. Changes to the rules regarding tax-advantaged retirement accounts are quite extraordinary, and they provide financial flexibility for people when they need it the most.

The CARES Act suspends the required minimum distributions (RMDs) from tax-deferred retirement accounts. This provision hopefully allows retirement accounts more time to bounce back from the current market downturn. Under prior law, individuals over the age of 70-1/2 (those born before July 1, 1949), those over the age of 72 (for those born after July 1, 1949), and most non-spousal heirs were required to take an annual RMD. The size of the RMD for the current tax year is calculated taking into account the balance of the account as of December 31 of the year before, and many investment accounts have shrunken considerably in the months since then. Individuals who have already taken their 2020 distributions within the past 60 days are allowed to treat it as an eligible rollover and put it back into their account. Currently, no legislation has been passed to address an RMD taken more than 60 days ago. The provision to waive the 2020 RMD is optional. It allows retirees to take out only as much as they need, rather than a required amount. Investors should consult their plan administrators about how to do this.

The CARES Act also makes it easier to withdraw funds from tax-deferred retirement accounts like 401(k)s and traditional IRAs by relaxing penalties on certain early withdrawals and plan loans. The legislation restricts relief to participants with a valid COVID-19 related reason for early access to retirement money, including being diagnosed with COVID-19; having a spouse or dependent diagnosed with the disease; suffering a layoff or other work reduction due to COVID-19; or lacking childcare because of COVID-19. Assuming your employer or plan sponsor accepts the CARES Act early withdrawal provisions (and not all are required to do this), the following breaks are available. Participants under age 59-1/2 are allowed a penalty-free early distribution of up to $100,000 during calendar year 2020 and suspends the mandatory 20% withholding requirement that normally applies to such distributions. Although the resulting tax liability is not waived, it can be spread over three years. Those who redeposit the withdrawn amount within three years will not owe any tax at all.

The CARES Act also increases the amount of loans allowed from certain workplace retirement accounts to $100,000 or 100% of the account balance, whichever is less. This option applies to any loans taken out during the six-month period from March 27 to September 23, 2020. The CARES Act permits borrowers to forgo repayment during 2020, starting the five-year repayment clock in 2021. Borrowers who lose their job after taking a loan have until October 15, 2021 to repay the loan before it is treated as a taxable distribution. Clearly, this is an improvement over the prior 60-day rule but still may be a hardship for individuals laid off or furloughed from their jobs.

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