FIRST AMERICAN BANK

WEALTH MANAGEMENT GROUP

As a Plan Sponsor, you may have heard in the news of upcoming hardship withdrawal rule changes that affect 401(k) plans as a result of the Bipartisan Budget Act of 2018. The IRS recently issued proposed regulations that, once finalized, will implement these changes.

Under current regulations, a participant may withdraw elective deferrals, but not associated earnings on these deferrals, in the event of hardship and if allowed by the plan. A hardship is defined as a serious financial need for which a participant does not have another source of money reasonably available. The current reasons are as follows:

- Costs directly related to the purchase of the participant's principal residence
- Payment of tuition, related to educational fees, and room and board expenses for the next 12 months of post-secondary education for the participant, the participant's spouse, children, or dependents
- Expenses for medical care for the participant, the participant's spouse, or dependents to the extent not covered by insurance
- The need to prevent eviction from the participant's principal residence or foreclosure on the mortgage of the participant's principal residence
- Certain expenses for the repair of damage to the participant's principal residence that would qualify for the casualty loss deduction under IRS Code Section 165
- Burial or funeral expenses for the participant's deceased parent, spouse, child, or dependent

Current regulations state that a participant who receives a hardship withdrawal must stop contributing elective deferrals until the six-month anniversary of the hardship withdrawal. Further, if a plan allows for loans, the participant must apply for a loan prior to being eligible to apply for the hardship withdrawal as a loan is considered to be a reasonable source of money available.

The proposed regulations will change some of the above rules once they are finalized. The proposed regulations allow earnings on elective deferrals to be distributed as part of a hardship withdrawal. In addition, Qualified Non-Elective Contributions (QNECs) and Qualified Matching Contributions (QMACs), including safe harbor contributions, as well as earnings on such contributions, will also be eligible for hardship withdrawal if allowed by the plan.

The proposed regulations eliminate the six-month suspension period from making elective deferrals following receipt of a hardship withdrawal. This is an optional change that can be implemented for the plan year beginning in 2019, but will be a mandatory change for the plan year beginning in 2020.

Another significant change with the proposed regulations is the removal of the requirement to take a plan loan before a hardship withdrawal can be issued. As stated earlier, current regulations indicate a participant must apply for a loan if allowed by the plan prior to being eligible to apply for a hardship withdrawal.

The reasons for hardship withdrawals have also been modified. The proposed regulations add a new withdrawal reason, which now allows hardships due to a federally declared disaster as long as the employee's principal residence or place of employment was located in the disaster area as designated by the Federal Emergency Management Agency (FEMA). This new reason is optional for the plan year beginning in 2019. In addition, hardship withdrawals that are issued to pay for the repair of damage to the participant's principal residence that would qualify for the casualty loss deduction under IRS Code Section 165 are no longer tied to a federally declared disaster. This change is generally going to be effective for the plan year beginning in 2019.

First American Bank is closely monitoring the development of these proposed regulations. The industry standard appears to be moving in the following direction:

- Plans will include earnings on a participant's elective deferrals when determining the amount available for a hardship withdrawal, but hardship withdrawals from QNECs, QMACS or safe harbor contributions will not be available
- If loans are permitted, plans will not require a participant to obtain a loan prior to a hardship withdrawal
- Plans will remove the six-month elective deferral suspension effective for any plan year beginning in 2019 rather than wait until this is required for the plan year beginning in 2020

While the above changes may be put into practice starting for the plan year beginning in 2019, a plan amendment will be required at a later date once the regulations are finalized. At such time, our office will coordinate with you, as the Plan Sponsor, to address any plan document issues that arise from these regulations. In the interim, should a participant request a hardship distribution, our office will work with you on the required and optional provisions to be implemented.

If you would like additional information or have questions about your plan's hardship withdrawal policy, please contact your Relationship Manager/Consultant or First American Bank's Retirement Plan Services Group at (847) 392-2999 or RSAdmin@firstambank.com.

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