



Do We Still Need to Suspend Deferrals Following a Hardship Distribution?

Facts

Larry and Kent are both participants in our company's 401(k) plan. Both recently went back to school on a part-time basis to pursue graduate degrees and will continue working for us. Each of them took hardship distributions to help pay for tuition, Larry on September 18, 2020, and Kent on January 3, 2020. Both of them would like to resume making contributions to the plan as soon as possible.

Question

I know the rules used to require employees to stop deferring for 6 months after taking a hardship distribution, but I seem to recall hearing that those rules changed. When can Larry and Kent start deferring again? Is there anything I need to do in the meantime?

Answer

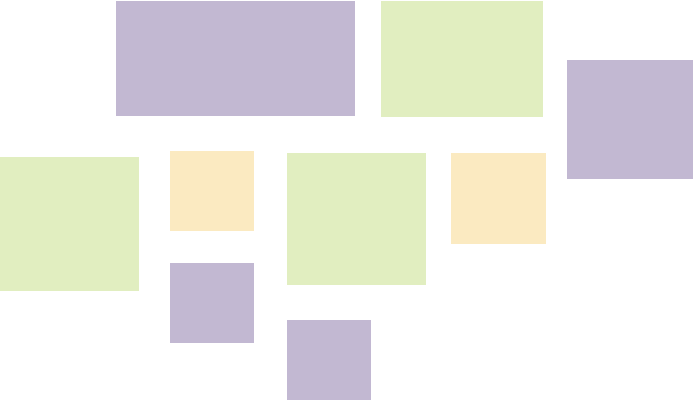
We may be talking about graduate school here, but the answer to your question is similar to that of a note passed in grade school – check “yes”, “no”, or “maybe.” While the rules on resuming deferrals after a hardship distribution have recently been relaxed, we are in a bit of a transition period through the middle of 2020 where the correct way to handle situations like this can be a bit confusing. The answer varies based on timing and decisions.

Let's start with the easy part first. Under [new regulations](#) from the IRS, plans are no longer permitted to suspend employee 401(k) deferrals for any hardship distributions taken after December 31, 2019. Since Kent took his hardship in January 2020, he can continue making deferrals without missing a beat.

So, what about Larry? Since he took his hardship distribution in 2019, you have/had several options:

- **Full Suspension:** Apply the old rules that required employees to suspend deferrals for 6 months immediately following the distribution and make Larry wait until March to resume his contributions;
- **No Suspension:** Eliminate the suspension right away so that Larry can continue deferring without interruption; or,
- **Abbreviated Suspension:** Cut the suspension short and allow Larry to resume deferrals at some point before March 2020 when his suspension would otherwise end.

Based on the facts presented, it appears that Larry's deferrals were suspended at the time of hardship, so that takes the “No Suspension” option off the table. That means you have the option of letting his suspension run its course through March or allowing him to resume deferrals immediately (or at some other date before March). Note, however, that if you have any other participants who took hardships in the latter half of 2019, they will also need to be allowed to resume deferring right away.



Each plan sponsor has the option of how to apply the suspension for hardships taken in 2019. Eventually, plan documents must be amended to reflect what was done in operation. In the meantime, however, plan sponsors should keep track of how they handled pre-2020 hardship suspensions and ensure that all participants are treated the same way.

Fortunately, all this confusion about the suspension will go away once we hit July 1, 2020. By then, we will be beyond the 6-month mark from the end of 2019, so any suspensions that carried over will have expired.

The new hardship distribution rules don't have to be an animal house. If you have more questions about the suspension or any of the other hardship changes, reach out to a DWC Expert.

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