TriStar Pension Consulting

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LOANS

Can a participant borrow money from a qualified retirement plan?

Each plan varies as to whether the employer allows for loans. A plan may allow for loans but is not required to. If loans are allowed in the plan, then that information can be found in the participants summary plan description (SPD). Check with your HR department or call TriStar to find out if the plan allows for loans.

How much can a participant borrow from their retirement plan?

If the plan allows for loans, then the participant can borrow up to 50% of the *vested* account balance, not to exceed the $50,000 maximum set forth by the IRS. For instance; if a participant has a vested account balance of $40,000, the maximum amount that can be borrowed from the account is $20,000. Example 2, if a participant has a vested account balance of $110,000, the maximum loan amount would be $50,000.

What is a vested account balance?

A vested account balance is the portion of your account balance that 100% belongs to the employee. An employer cannot forfeit or take any part of the balance back for any reason. These amounts are determined by the plan's vesting schedule. When an employer sets up a retirement plan, they also choose a vesting schedule. Some vesting schedules require employees be employed for a specific period of time before the funds are considered vested.

How long does a participant have to pay back the loan?

A participant must repay the loan in full within 5 years from the issuance of the loan but other payment plans can be adjusted to pay off the loan sooner. If the participant is using the loan to purchase a primary residence, then the loan may be amortized over an extended number of years by the loan procedure, not to exceed 30 years.

What happens if the loan is not repaid within its terms?

If a participant defaults on a loan, they will be taxed, penalized and will receive a 1099-R, reporting the loan amount and any interest accrued as taxable income. Exceptions to this rule are:

- A plan may suspend loan repayments if the employee is performing in a military service.
- A plan may also suspend loan repayments during a leave of absence for up to one year, however in this case the employee must make up the missed payments upon return. Make up payments can be made either in a lump sum or by increasing monthly payments. This is so that the loan does not exceed the original 5 year term.

How does a participant pay back a loan?

Loan payments will be automatically withdrawn from the employee's paycheck each pay period. Employees are responsible for paying back the loan therefore they should ensure that the payments are being deducted each pay period. When a participant pays back a loan, they do so with after-tax dollars.

What is the interest rate on a retirement plan loan?

The interest rate on a loan is typically the prime lending rate plus an additional percentage or two.

Where does the interest paid on a loan go?

The interest paid on a loan will go back into the participant's account, so essentially, a participant is paying themselves back.

What if a participant leaves an employer and has an outstanding loan?

Many plans allow a participant 60 days from the termination date to repay the loan in full. After that, the loan will be considered taxable income and the participant will receive a 1099-R, reporting the funds to the IRS. The participant's loan will then be taxed and penalized.

When would spousal consent be necessary for taking a loan?

Some plans may require spousal consent in order for a participant to borrow from the plan. This is not a requirement from the IRS rather it is implemented by the plan document and employer.

Will a participant be taxed on a loan?

Loans are not taxed unless there is a default in payment on the loan. In the event the participant defaults on the loan, the outstanding loan balance plus any accrued interest will be considered a distribution and will be reported to the IRS on a 1099-R as taxable income. Defaults on the loan will not be reported to credit agencies and therefore will not appear on a participant's credit report or be reflected on a credit report.

How long will it take for a participant to receive a loan check?

TriStar Pension will process the loan within 7 business days of receiving the completed loan request information. TriStar requests the loan from the fund company, where the participants assets are held, and the funds will be delivered to the participant within 10 business days of TriStar processing the loan. Of course, this time frame may vary depending on the fund company.

Can a participant have more than one loan from their qualified retirement plan?

It is possible for an employer to allow for more than one outstanding loan from the plan at a time. The second loan, when added to the highest outstanding balance of the original loan, cannot exceed the maximum loan amount (i.e. 50% of the vested account balance or $50,000).

Let's say Susie has a vested account balance of $100,000 and took a loan of $40,000 on January 1, 2010. Susie makes payments on her loan for a year and on January 1, 2011, the outstanding balance is now $33,322. Susie wants to take out another loan. The highest plan balance for the preceding year was $40,000, subtract the outstanding balance on the day of the new loan $33,322, and the difference is $6,678. The new loan plus the old loan can't exceed $43,322 ($50,000 -$6,678). The most Susie will be able to borrow for her second loan is $10,000.

Original Loan and Highest Loan Balance	**= $40,000**
Outstanding Loan Balance	= $33,322
Amount Paid on Loan	$40,000-$33,322= $6,678
Maximum Loan Amount Allowed	= $50,000
Max. Loan Amount Minus Amount Paid Down	$50,000-$6,678= $43,322
$43,322-$33,322	= $10,000

DISTRIBUTIONS- Withdrawing money from the account

For what reasons can a participant request a distribution (withdrawal from the account)?

If allowed by the plan, a distribution can be taken if one of the following occurs:

- A participant dies, becomes disabled or if terminates employment.
- The plan terminates and there is no longer a plan offered by the employer.
- A participant reaches the age 59 ½ and takes an in-service withdrawal.
- A participant qualifies for a hardship withdrawal.

When is a distribution required?

An RMD or required minimum distribution, is required to be taken by the participant the calendar year in which the participant reaches the age 70 ½. Distributions are also mandatory upon a participant's death.

Is a plan sponsor required to make contributions if a participant is 70 ½ and taking RMD's?

Yes. A plan sponsor must continue making contributions to an employee's account and provide the option for employees to continue to make salary deferrals as long as the employee is eligible to participate in the plan.

How do I request a distribution?

1. Most fund companies have the option of setting up and managing your account online. If you have an online account with your fund company, you can quickly request a distribution by visiting their website.
2. OR, Call TriStar and we will e-mail, mail, or fax you the paperwork to fill out. It is very important that you fill out this paperwork accurately and fully in order for us to process your request.

How long does it take to receive a check for a distribution request?

TriStar Pension will process the distribution within 7 business days of receiving the completed loan request information. TriStar requests the distribution from the fund company, where your assets are held, and the funds will be delivered to the participant within 10 business days of TriStar processing the distribution. Of course, this time frame may vary depending on the fund company.

What are the taxes and penalties for an early distribution?

Early distributions will receive a 10% penalty, along with state and federal taxes.

When is a distribution considered early?

An early distribution is when a participant withdraws from the account prior to the age 59 ½. There are a few exceptions which may qualify for a penalty-free withdrawal of funds.

HARDSHIP WITHDRAWALS

What events qualify for a hardship withdrawal?

If the plan permits a hardship withdrawal, then the following are a few reasons why a participant might qualify: to pay for medical expenses, the purchase of a primary residence, tuition expenses, or to prevent eviction or foreclosure of a primary residence. Documentation is required for the hardship withdrawal process to begin.

Is a participant required to pay back the amount distributed from the hardship withdrawal?

Hardship distributions are not repaid to the plan and are included as gross income. A participant will receive a 1099 and will be taxed and penalized for withdrawing from the plan early.

CONTRIBUTIONS-Adding money to the account

How much can a participant defer?

The IRS caps the amount a participant can defer. These guidelines are updated each calendar year. For 2014, a participant can defer up to $17,500. This deferral amount may also be restricted depending upon the plan adoption agreement.

How frequently can a participant change their deferral percentage?

Changes in deferral percentages can be made depending on the plan document. A plan can be designed to allow for deferral changes as frequent as every payroll period.

What is a catch-up contribution?

A catch-up contribution is an additional contribution which can be made by those who are 50 or older. The 2014 catch-up contribution is an additional $5,500.

When must a plan sponsor deposit matching and profit sharing contributions?

Deposits must be made to participant's accounts within 7 days of payroll.

ELIGIBILITY

When is a participant eligible to participate in the plan?

Each plan has different eligibility requirements. Please review the employer's plan description summary to find out more about eligibility requirements such as; length of employment and minimum age requirements.

What documents are required when an employee is eligible to enter the plan?

An employer must provide the summary plan description, enrollment package, beneficiary designation form, and, salary deferral election form.

- **Summary Plan Description (SPD)-** This form identities the basic guidelines of the plan, including a participant's rights. This must be provided within 90 days of a participant receiving benefits.
- **Enrollment Package**- Is general information about the plan and how to enroll. This can be provided at any time prior to plan participation.
- **Beneficiary Designation Form**- This form can be changed at any time and will appoint a beneficiary to the account if the participant dies.
- **Salary Deferral Election Form**- This form designates how much money to withhold form the participant's paycheck and deposited into the account.

This article provides general guidance to frequently asked questions. TriStar Pension Consulting is not responsible for the advice given in this article. For a more accurate and detailed answer, please call TriStar Pension directly.