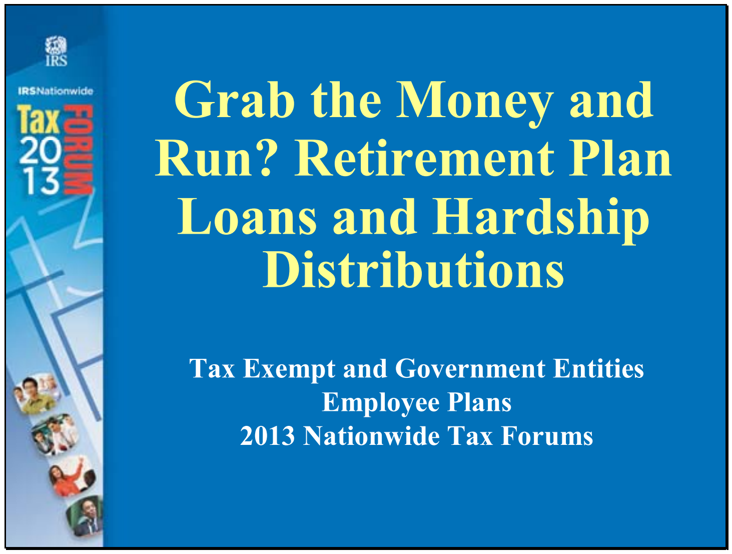
Slide 1



Herbert Hoover once said, “About the time we can make the ends meet, somebody moves the ends.” Many of us, I’m sure, have felt this way about the economy in recent years. When times are tough like this, retirement plan participants may be especially tempted to view their account balance as a way to make ends meet.

Today, we’ll talk about two common means for employees to access their retirement savings: loans and hardship distributions. We’ll talk about when they’re allowed, how the money may be taxed to employees, and what special rules apply to employers who offer loans and hardship withdrawals in a retirement plan.

We’ll also talk about things that can go wrong, such as when loans aren’t repaid on time or when business owners bend the rules. We’ll also address what you can do to fix a mistake in your retirement plan to avoid adverse tax consequences.

Our goal is to help you stay on track as you balance the urgent needs of today and the secure retirement your plan is designed to provide in the future.

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Let's start with the basics. A ***loan*** from a retirement plan is similar to a loan from a bank, except the loan funds come from the employee's retirement account. As long as the employee keeps up with the payment schedule and follows the other rules for loans, the IRS won't treat the loan as a distribution and the employee won't owe taxes on the borrowed funds.

A ***hardship*** distribution, on the other hand, is a distribution from the employee's retirement account - the employee takes out what's needed for immediate use and reports it as taxable income. In most cases, the employee will also owe a 10% additional tax on early distributions. Unlike loans, which have no restrictions on the use of the funds, hardship distributions require the employee to show that the funds will be used for an allowable emergency purpose.

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Before we get into the rules for loans and hardship distributions, let's clarify which plans are eligible to offer these features. Nearly all participant loans come from retirement plans with separate accounts - profit-sharing, 401(k) plans, 403(b), 457(b), and money purchase plans.

Even though defined benefit plans don't have participant accounts, they are allowed to have loans. However, a loan program in a defined benefit plan is a rare occurrence. It involves an actuary, complicated actuarial calculations, and can be very difficult to administer, especially when there are mistakes.

We'll spend our time today discussing loans from plans with separate participant accounts; profit-sharing, 401(k), 403(b), 457(b), and money purchase plans.

IRA-based plans, such as a SEP, SARSEP or SIMPLE IRA plan, cannot offer loans.

Hardship distributions are limited to defined contribution plans that allow employee salary deferrals, such as 401(k), 403(b) or 457(b) plans.

You won’t find hardship distributions in IRA-based plans because you can take money from the IRA at any time for any reason.

Slide 4

Even if your plan is eligible to offer loans and hardship distributions, it doesn't have to offer them. The decision to offer them should be based on a careful balancing of employees' needs, the burdens of administering loan and hardship distribution programs, and the employer's desire to plan for a secure retirement for participants.

Today we're going to talk about what the law allows for loans and hardship distributions. Your plan doesn't have to offer everything allowed under the law. Your plan can limit loans to lower amounts or even for specific purposes, or it can offer hardship distributions for some, but not others.

If you do allow loans and hardship distributions, you have to apply the same rules for everyone, including the business owner and other highly paid employees.

Here are some questions to ask before anyone takes a loan or a hardship distribution from your plan:

- Does the plan document allow for the type of loan or hardship distribution requested?

- Are administrative procedures in place to ensure that loan repayments are timely and accurate?

- Do the employees taking hardship distributions understand the income tax consequences of their choice? For example, hardship distributions are taxed immediately and may also be subject to a 10% early distribution tax.

- And finally, do the employees understand the impact of loans and hardship distributions on future retirement savings? This question is important because the lost compound earnings caused by early withdrawals can have a significant impact on your final savings.

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Let's turn our discussion to plan loans. Loans allow you to access retirement savings without receiving a plan distribution. They're most common in 401(k) plans, which is no surprise since most retirement plans are 401(k)s. Loans aren't allowed from IRAs or IRA-based plans. Any money taken from an IRA is a distribution.

If you decide to offer loans from your retirement plan, the program must meet some basic requirements.

- The plan document has to authorize loans. Even though ***the law*** allows for loans from a 401(k) plan, loans shouldn't be made unless the plan document authorizes them.

- Every loan should have a written loan agreement. The loan agreement should show a genuine debtor-creditor relationship and establish the repayment schedule and interest rate.

- Electronic loan agreements can be used if they are confidential, clearly set out the loan terms and give the borrower a chance to change the loan request after receiving a confirmation.

- The loan must be secured, typically by the participant’s account balance.

- To avoid a taxable distribution, the loan can’t generally be more than 50% of the account balance or $50,000, whichever is less.

- The loan should charge a reasonable rate of interest, which is generally the market rate for similar secured loans.

- By its terms, the loan should require regular payments to be made at least quarterly, and the loan term shouldn’t exceed five years, unless it’s used for the purchase of the employee’s main home.

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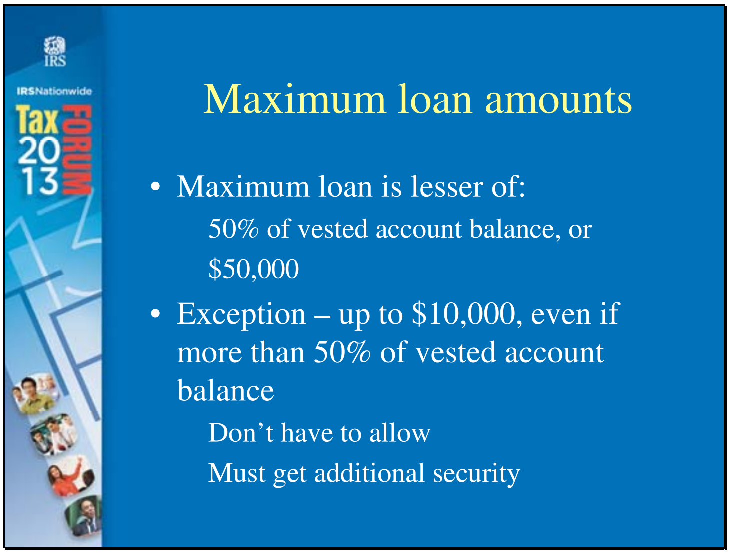

So…how much can you take as a loan from your retirement plan?

The most you can borrow from your plan is 50% of your vested account balance, but no more than $50,000, whichever is less.

Plans can have a lower loan limit but not a higher one. And, some plans allow you to take a loan of $10,000, even if that's more than 50% of your account balance. Plans are not required to allow this exception, and most don't. If your plan allows loans that are more than 50% of the account balance, the $10,000 exception, the employee will have to find another way to secure the loan. Unsecured loans aren't allowed.

Let's look at some examples.

Bill's vested account balance is $80,000. Bill may take a loan up to $40,000, which is the lesser of 50% of his vested account balance and $50,000.

Sue has a vested account balance of $120,000. 50% of that is $60,000, so Sue may take a loan up to $50,000.

Read your plan document carefully to determine if it requires written spousal consent before giving a loan.

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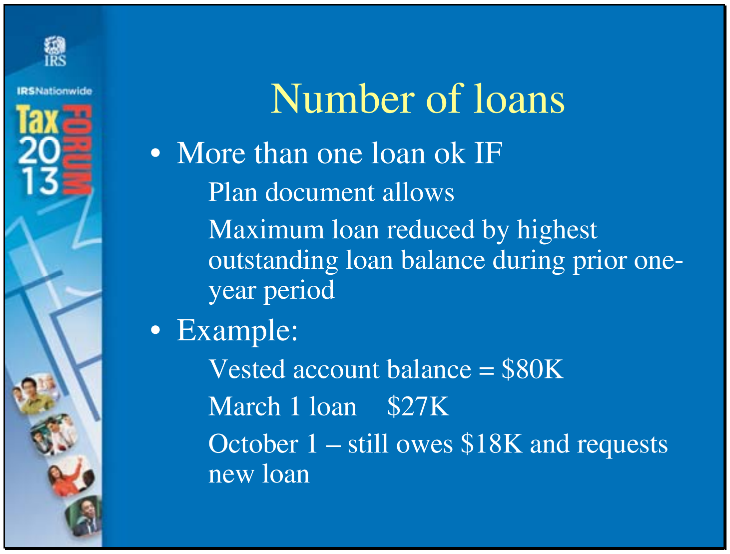

Some of you may be wondering if you can “double dip,” or have more than one loan at once.

The answer is “yes,” if the plan allows it. However, if you took a loan within one year prior to the new loan, the maximum loan amount is reduced by the highest outstanding balance during that year. The maximum is reduced even if you paid back the first loan in full before taking a second loan.

Let’s look at an example:
Jim’s employer sponsors a 401k plan that allows for more than one loan. On October 1, Jim has a vested account balance of $80,000. He decides to take out a second plan loan. Jim had borrowed $27,000 earlier that year and still owes $18,000 on that first loan. How much can he borrow as a second loan?

The new loan *plus the outstanding balance of all other loans* must be limited to the lesser of two amounts:

The first is the $50,000 limit, but it must be reduced since Jim had another outstanding loan during the year before taking the second one. For the $50,000 limit, find the difference between the highest outstanding balance of all of Jim's loans over the last year and the balance on the day before the new loan. That's $27,000, the highest balance, less the balance the day before, $18,000, is equal to $9,000. $50,000 reduced by $9,000 gives you a total loan maximum of $41,000 under the first prong of the test.

The second limit is 50% of the vested account balance. In this example, Jim's vested account balance is $80,000. The limit under this second prong is 50% of that amount - $40,000. Since $40,000 is less than $41,000 - all of Jim's loans can't exceed $40,000.

Jim's loan balance at the time of the second loan is $18,000. This allows him to borrow an additional $22,000 – that is the $40,000 maximum loan minus the $18,000 existing loan.

Would it benefit Jim to repay the first loan before requesting a second loan? Let's crunch the numbers.

The law bases Jim's maximum loan on all of his loans that were outstanding during the 12 months prior to the new loan. So, there isn't a significant advantage for Jim to pay off his first loan before requesting a second.

If Jim repaid the $18,000 before applying for the second loan, he would be limited to the lesser of the $50,000 maximum reduced by his highest loan balance of $27,000, less the balance of any loans the day before the new loan – in this case $0 because he paid it off – for a maximum loan of $23,000 compared to half of his account balance, or $40,000. In this case, the maximum permissible loan amount would be $23,000.

When Jim doesn't pay off the first loan, he has a total of $40,000 in loans outstanding. By paying off the first loan, Jim's total loan balance after taking out the second loan is just $23,000.

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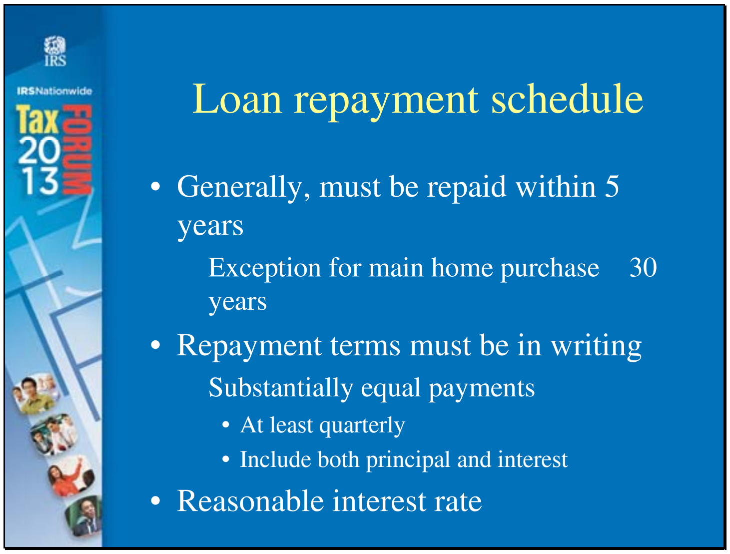

So how long do you have to repay the loan?

Generally, you must repay it within 5 years. However, if the loan is for the purchase of your main home, it can be up to 30 years.

The repayment terms – length, frequency of payment and the method for determining the interest rate – must be in a legally enforceable agreement. Many loan agreements are in an electronic form.

Your loan must require substantially equal payments, at least quarterly, that include both principal and interest. You'll find that most plans require payments to be made by payroll deduction. As with limits on loan amounts, it's ok for a plan to require payments that are more frequent than this minimum.

The plan has to use a "reasonable" rate of interest for loans. The determination of "reasonable" is made based on facts and circumstances. You might consider rates charged by local banks for a similar secured loan.

With interest rates, the main issue we find on our audits is that rank-and-file employees are charged a higher rate than the rate for the highly paid employees.

You may be asking yourself, “Can the plan charge a fee for a loan?” The answer is “Yes, within limits” – for example, the federal government’s Thrift Savings Plan, charges participants a $50 loan fee.

Also, in the case of military personnel, the loan repayment can – but doesn’t have to be – suspended while the participant is in military service. Interest continues to accrue during any repayment suspension.

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We often see participants missing their payments on a loan. The plan terms will generally specify when a default occurs. A plan may provide that a “cure period” that provides that a loan doesn’t become a “deemed distribution” until the end of the calendar quarter following the quarter in which the repayment was missed.

For example, if Ann missed a payment due March 31, the first quarter of the year, she would have until the end of the second quarter, June 30, to bring the loan current. If not, the loan would be treated as a taxable distribution on June 30.

Not all plans have such a generous cure period. You’ll need to check the loan procedures outlined in the plan document to determine when a loan is treated as a distribution.

It’s easy for a loan to be in default. Participants are hesitant to let the payroll department know that the payments never started or quit being deducted from their paycheck.

A loan that goes into default will be treated as if it were distributed to you. This distribution isn’t eligible for rollover to another plan or IRA and is subject to the 10% additional tax on early distributions.

The plan document will determine whether this defaulted loan is offset from the participant’s account balance or if it’s treated as a deemed distribution. If the plan provides for in-service distributions, the defaulted loan is offset from the participant’s account. A Form 1099-R is issued with a box 7 code of 1 if the participant was under 59 ½, code 2 if over.

If the plan doesn’t provide for in-service distributions, the defaulted loan is considered a deemed distribution. A Form 1099-R is issued with box 7 codes of L and 1 for participants under 59 ½, L and 2 for participants over 59 ½. A deemed distribution isn’t offset from the participant’s account. This unpaid amount will be recorded as an outstanding loan on the plan’s books until a distribution can occur under the plan terms.

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What happens if you have a participant loan and you leave your job before you repay it? The terms of the loan will likely require you to immediately pay your outstanding balance in full. Very few plan administrators want to attempt to collect loan payments from terminated employees.

If you don't repay the outstanding balance, it'll be deducted from your account and is treated as a distribution. The offset loan balance must be included in your gross income and may be subject to the 10% additional tax on early distributions. The distribution is reported on Form 1099-R.

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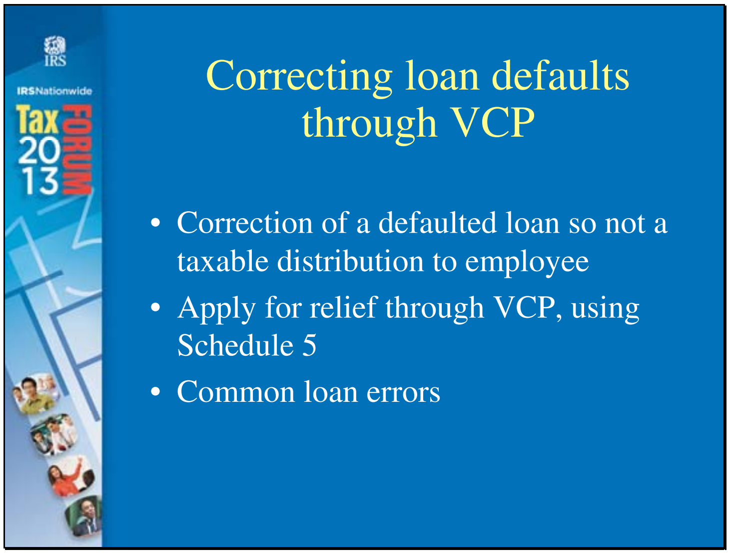

We often see loan payments that are missed because of a mistake by the employer or the plan administrator. This can happen, for example, when the payroll provider stops deducting loan payments from the employee's paycheck before the loan is fully paid off, or the deductions are made but the payments are not transferred to the plan trust. If these mistakes aren't corrected within the grace period provided in the plan, the loans are in default.

An employer may be able to correct these defaulted loans without having to treat the loan as a taxable distribution by using an IRS correction program. If a loan is still within the original five-year repayment period, the employer can reamortize the loan over the remaining loan term. This method is permitted under the Voluntary Correction Program. You can find information about this program and fillable documents on our Correcting Plan Errors web page at irs.gov/retirement.

We have a special schedule you can use for loan mistakes under the VCP - Schedule 5. It describes the different options you have for recalculating the remaining loan payments.

By using VCP to correct these loan mistakes, participants can avoid having their loans treated as distributions. This can save valuable tax dollars for your employees as well as preserving the qualification of your plan.

Even if the original five-year repayment period has already expired, you still may want to file a VCP submission to fix problems with a loan default. Perhaps a loan default occurred in a prior year, but you didn't provide the employee with a Form 1099-R for that year.

By using the Voluntary Correction Program, you can generally report the deemed distribution in the year of your VCP submission, instead of the year the distribution occurred. Again, you'd make this request on Schedule 5 using model submission documents you can find on our website.

If your loan failure affected fewer than 25% of the participants in any year and you aren't reporting any other failures with your submission, you may be eligible for a 50% fee reduction.

So what are some of the other problem areas with participant loans that we see in our correction programs and audits?

We often see--

- loans or multiple loans when the plan document doesn't allow them,
- missed or irregular payments,
- deemed distributions where no 1099-R was issued,
- no loan documentation,
- interest rates that are too low or too high,
- loans with no interest – for example, an employer that effectively borrowed from the plan by not paying salary deferrals to the trust or IRA timely,
- loans made to highly compensated employees on terms not available to the rank-and-file employees,

- loans that exceed the maximum amount, and
- loans where the employer continues to withhold payments after the loan was repaid.

Many of these errors can be corrected by using IRS correction programs.

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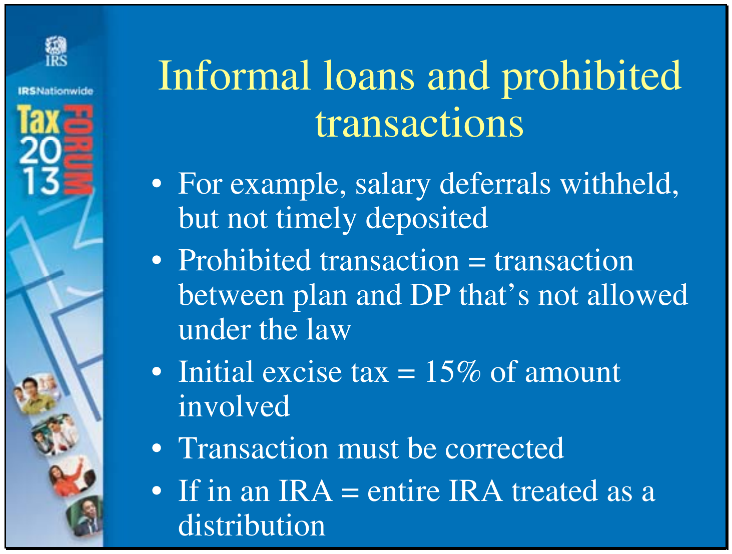

So far, we've been talking about actual loans - the kind where you apply for a loan and enter into a written loan agreement.

What about the situation where the employer withholds salary deferrals from employees' pay intending to deposit the money in its 401(k) plan, but doesn't? This is never OK.

You must deposit the money as soon as it can reasonably be segregated from your business assets. For plans with fewer than 100 participants, DOL allows 7 business days after the deferrals are withheld from an employee's paycheck to deposit them. Otherwise, this is considered an informal loan and a prohibited transaction.

So what is a prohibited transaction and what are the consequences?

Prohibited transactions are transactions between a retirement plan and a disqualified person that are prohibited by law. These transactions generally include self-dealing between the plan and a disqualified person, including lending money or extending credit.

A disqualified person is an individual who, by virtue of their relationship to the plan, is in a position to self-deal. Generally, you're a disqualified person if you're an employer or owner, a fiduciary or service provider. In addition, many family members of disqualified persons can be considered disqualified persons. This includes spouses, parents and children. If you're a disqualified person who takes part in a prohibited transaction, you must pay a tax and you must correct the transaction.

We only touched on the more common disqualified persons and prohibited transactions. For a complete list, see IRS Publication 560, *Retirement Plans for Small Business*.

Plan loans that satisfy the legal requirements are exempt from the prohibited transactions rules. However, the benefit must be on the same terms as for all participants.

Let's look at an example of a typical loan that turns into a prohibited transaction. Bill, owns his own company. He borrowed $40,000 from his 401k plan, with monthly payments due for the next five years. Bill quits making payments on the loan after the first year. Since Bill is a disqualified person, the fact that his loan went into default makes the loan a prohibited transaction.

The initial tax on a prohibited transaction is 15% of the amount involved for each year. The disqualified person pays this tax on Form 5330, *Return of Excise Taxes Related to Employee Benefit Plans.* If the prohibited transaction isn't corrected, the tax increases to 100%.

To correct this prohibited transaction, Bill must place the plan in the same position it would've been in had the prohibited transaction not occurred. To do so, Bill needs to pay back to the plan, the balance of the loan, including any accrued interest. Bill also needs to file a Form 5330 and pay the 15% excise tax.

For IRAs, the consequences of prohibited transactions are different. A prohibited transaction with an IRA occurs if the owner or beneficiary of the IRA engages in any of the transactions we described earlier. No excise tax is imposed. Instead, the law provides that the account is no longer an IRA. The IRA is treated as if the assets were distributed on the first day of the taxable year in which the prohibited transaction occurred.

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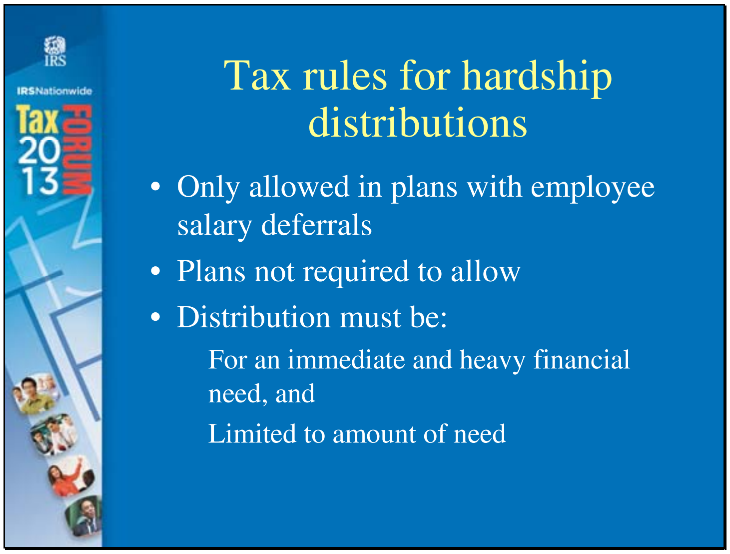

Let’s talk about hardship distributions. As I mentioned earlier, you can only have hardship distributions from a defined contribution plan, such as a 401(k), 403(b) or 457(b) plan – the kind that allow employee salary deferrals. We’ll focus our discussion today on 401(k) plans.

A 401(k) plan is not required to provide hardship distributions. But if it does, that distribution can only come from the employee’s elective salary deferrals, and it must also meet two additional requirements. The withdrawal must be:

- for an immediate and heavy financial need, and
- limited to the amount necessary to satisfy that need.

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So what is an immediate and heavy financial need?

We all have an idea of what we think hardship means – illness, job loss, natural disasters, or taking care of elderly family members. However, a retirement plan must specify the criteria for determining if a hardship exists.

Under IRS regulations, certain types of expenses are automatically considered immediate and heavy financial needs. These are:

- Medical expenses incurred by you, your spouse, dependents, or plan beneficiary;
- Costs directly related to the purchase your principal residence (but *not* mortgage payments);
- Tuition and related educational fees, such as room and board for the next 12 months for you, your spouse, dependents, or plan beneficiary;
- Necessary payments to prevent foreclosure on the mortgage of your principal residence or eviction from your home;
- Funeral expenses for you, your spouse, children, parents, dependents, or plan beneficiary; or
- Expenses to repair casualty damage to your principal residence.

Remember, these expenses are eligible for hardship distributions only if your plan provides for them. This is a common problem that we see in our audits and correction program submissions – where participants take hardship distributions that would be allowed under the law, but the plan document doesn't permit them. In other words, the plan document is more restrictive than the law.

A financial need can be immediate and heavy even if it you incurred it voluntarily. For example, you might purchase a home or enroll in college and be eligible for a hardship distribution under IRS rules.

Consumer purchases, such as a new boat or incurring credit card debt, aren't considered a hardship. However, if you develop high blood pressure as a result of worrying about your debt, your medical expenses could be grounds to receive a hardship distribution under your 401(k) plan.

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Even if an eligible hardship exists, you still have to satisfy the second prong of the test. You're only allowed to take the amount necessary to satisfy the need - that is, the amount you need along with the taxes associated with the hardship distribution.

The distribution isn't considered necessary if you have other resources available to meet the need, including a loan from your retirement plan or your spouse's and minor children's assets.

Whether you have other resources available to pay your expenses is determined based on facts and circumstances.

How are you expected to show that a hardship exists and the distribution is necessary to meet it? Unless an employer has actual knowledge to the contrary, the employer may rely on your written representation that you're experiencing an immediate and heavy financial need that can't be relieved from other resources, including:

1. insurance or other reimbursement,
2. liquidation of your assets,
3. your pay - by stopping elective or after-tax employee contributions,

4. plan loans, or
5. reasonable commercial loans.

You must generally take a plan loan before requesting a hardship distribution, if your plan offers both. However, if taking the loan would increase your hardship, you don't have to. For example, if taking a plan loan would disqualify you from a home loan, you can request a hardship distribution without taking the plan loan.

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So you’ve shown that you have an immediate and heavy financial need, and the need can’t be satisfied from other sources. The next question is - what portion of your retirement account is available for the hardship distribution?

A hardship distribution must generally be limited to your salary deferral contributions made under the plan as of the date of the distribution. Some plans may also permit hardship distributions regular matching and profit-sharing contributions.

Earnings, qualified nonelective contributions and qualified matching contributions aren’t included. This total is reduced by the amount of any previous distributions of elective deferrals.

If your plan is a Roth 401(k), you can choose to take your hardship distribution from your Roth account. A hardship distribution from a Roth account will consist of a pro-rata share of earnings and your Roth contributions. The earnings portion will be included in gross income unless you’ve had the designated Roth account for five years *and* you’re either disabled or over age 59 ½.

The part of the distribution attributable to Roth contributions is a return of after-tax money and is non-taxable. The portion of the distribution attributable to earnings on the Roth account is taxable and is subject to the additional 10% early distribution tax.

Let’s look at an example. Assume Doug has $45,000 in his pre-tax deferral account and another $45,000 in his Roth account. In each account, $20,000 is deferrals and the other $25,000 is earnings. Doug can take a hardship distribution of up to $40,000 and he can take it either from the pre-tax account, the Roth account or some from each. If Doug takes the distribution from the Roth account and is either age 59-½ or disabled and has had his Roth account for at least five years, Doug’s distribution will be entirely nontaxable.

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As a final step, if you take a hardship distribution, you must suspend all contributions to any plans maintained by your employer for six months after receiving the distribution. This requirement must be written in the plan document or another legally enforceable agreement.

This is another common error that we see – when the employee is given a hardship distribution, but continues deferring salary. Sometimes, the IRS may waive this requirement in disaster situations, as we did for victims of Hurricane Sandy.

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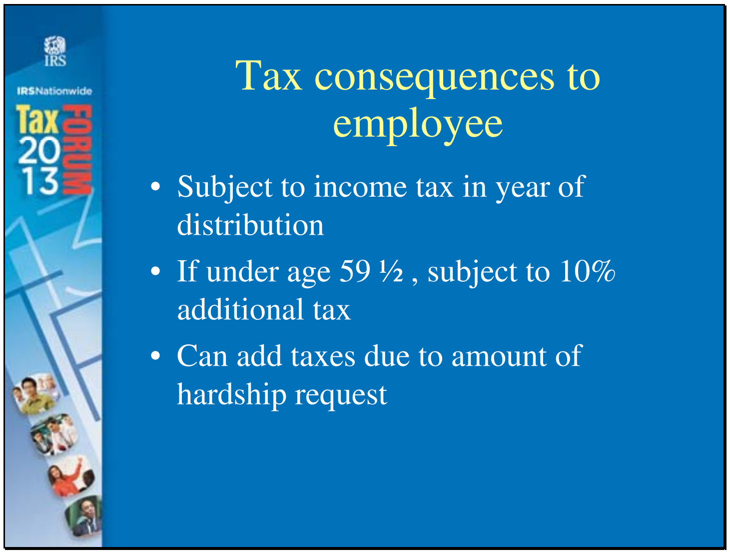

Although hardship distributions can be a lifesaver, it isn't free money. Hardship distributions taken from a pre-tax account are subject to income tax in the year of distribution. In addition, if you're under age 59 ½, you'll owe the 10% tax on early distributions, unless you qualify for an exception. We'll tell you more about it on a later slide, but you should take a look at our Pub 5036. It contains a list of the exceptions to the 10% penalty.

Even though you'll have to pay income tax on the distribution, your employer doesn't have to withhold taxes from it.

Instead, you should determine how much you'll owe in federal and state income taxes and add that amount to your distribution request. Put that money away, or better yet, go ahead and send it to the IRS so you're not tempted to spend it. Taxes on these distributions could amount to 40% or more.

Let's look at an example. John, age 40, has a vested account balance of $200,000, including $100,000 in pre-tax elective salary deferrals. He needs $26,000 to pay his daughter's college tuition. Assume John is in the 25% federal and 5% state tax brackets.

He’s subject to the additional 10% early distribution tax because he is under 59 ½ and doesn’t qualify for another exception. He would need a distribution of approximately $43,000 to satisfy his hardship and related tax liabilities. That’s because he’ll need 40% of the $43,000 distribution, or $17,000, to pay the taxes he’ll owe on the distribution, leaving John with $26,000 to pay college tuition.

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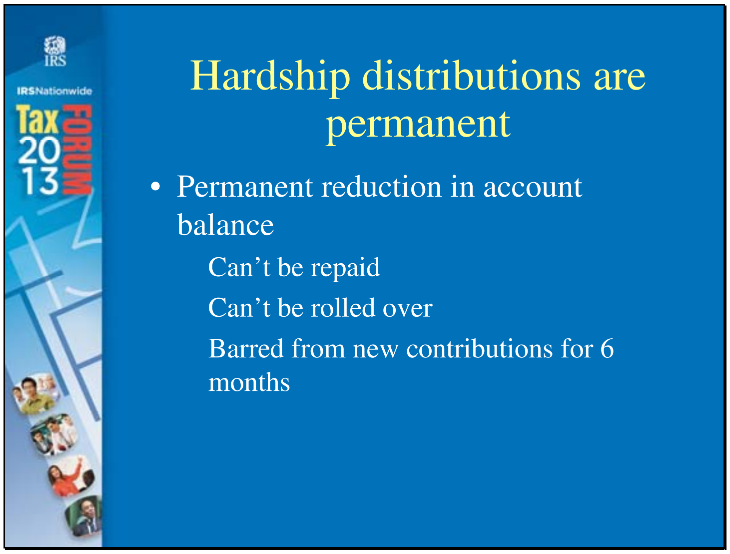

One last thing you should consider before requesting a hardship distribution is that it’s irreversible. Unlike plan loans, a hardship distribution is a permanent reduction in your account balance. Even if your circumstances change and you no longer need the money, you can’t pay it back.

Likewise, the distribution can’t be rolled over to another retirement plan or IRA. You’ll also be barred from making new contributions to their retirement account for six months after the distribution. For these reasons, hardship distributions should be considered a last resort. They can have a devastating impact on your retirement savings.

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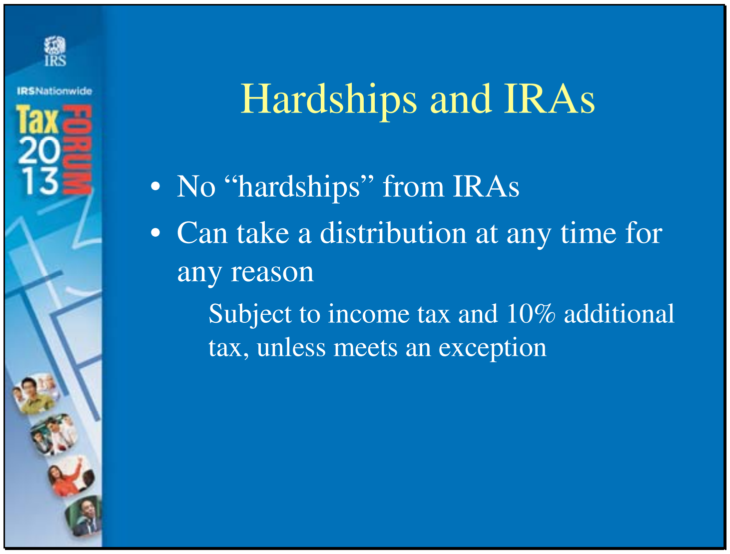


Let's talk about IRAs for a moment. If you have a SEP or SIMPLE IRA plan, the money in the plan is held in traditional IRAs. These accounts, referred to as SEP-IRAs or SIMPLE-IRAs, are taxed under the same rules that apply to other traditional IRAs.

There's no such thing as a hardship distribution from an IRA. You can take a distribution from an IRA for any reason at any time. However, money you do withdraw from an your IRA is subject to income tax and you may also owe the additional 10% early distribution tax if you're under age 59 ½.

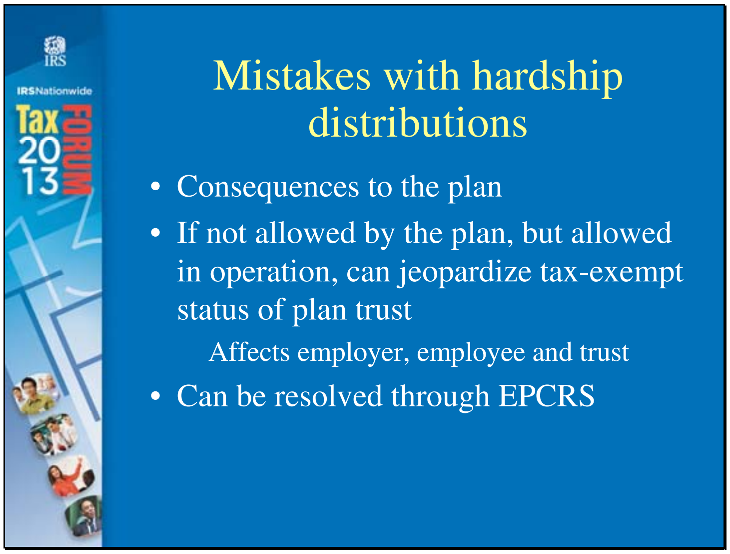
In a SIMPLE IRA plan, the early distribution tax is increased to 25% if you withdraw money within the first two years of participation.

Certain IRA distributions may be exempt from the early distribution tax. For example, a distribution from an IRA to pay for higher education expenses, or to finance a first-time home purchase, won't require the extra 10% tax.

We have a great resource for you - a chart showing the exceptions to the 10% additional early distribution tax for IRAs and qualified plans on our website, irs.gov/retirement.

Look for IRS Publication number 5036, *Retirement Plan Distributions: Exceptions to 10% Additional Tax*.

Slide 21



Loans or hardship distributions that don’t comply with the rules may affect the entire plan. If, for example, the plan document doesn’t allow loans, but a participant receives a loan from the plan, the plan document terms aren’t being followed in operation. This jeopardizes the tax-exempt status of the entire plan, and involves some harsh tax consequences for both the employer and the employees. You can go to irs.gov/retirement and enter “Tax Consequences of Plan Disqualification” in the search bar to read the detailed information.

Let’s take a moment and talk about the types of mistakes we see with hardship distributions in our audits and correction program submissions.

As I stated earlier, we often see failures to suspend contributions after a participant received a hardship distribution. That’s a very common problem.

We also see hardship distributions when the plan document didn’t allow them. Another problem area is where the plan administrator doesn’t retain the documentation for the hardship distribution. As an auditor, when they don’t have the proper documentation, you have to wonder how well the hardship distributions were being monitored.

With many employers now starting to use electronic hardship applications, documentation is becoming a bigger problem. If a participant can just go online, click on a few of the correct boxes, and receive a hardship distribution, it makes us very uncomfortable. The hardship still needs to have the proper documentation. Plus, if it's too easy, it may happen too often.

All of these problems can all be resolved through our correction programs. Let's look at a few examples.

What if your plan document didn't provide for hardships distributions, but employees were allowed to take them. In this situation, our correction programs will generally allow you to retroactively amend your plan document to to allow for hardship distributions. If you meet certain requirements, you can even self-correct this mistake. Under self-correction, you don't need to contact the IRS. Check out mistake #10 on the 401(k) Fix-It Guide at irs.gov/retirement for more information.

As a second example, let's say you didn't suspend elective deferrals following a hardship distribution, as required by the terms of the plan. This error is treated as an excess deferral under the plan. To correct, you must distribute the excess deferrals, plus earnings. Depending on the relative significance of the mistake and how much time has passed since you discovered it, you may be able to correct it on your own, without IRS approval, or you may need to make a VCP submission.

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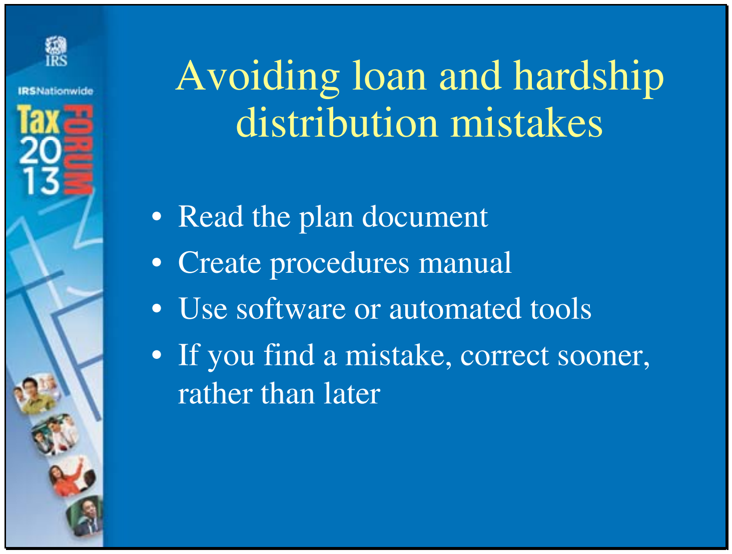

And finally, we'd like to offer some advice on ways to avoid making mistakes in the first place when you're carrying out a loan or hardship program.

First, be sure you know what your plan document provides. Don't assume you know what's in it. If you amend your plan or adopt a new plan when you change providers, be sure to check your elections in the new plan to be sure they reflect what the plan is doing in operation.

Determine how many loans are allowed, the permissible amounts and what kind of cure period is offered for missed payments and which events qualify as hardships before you make the distributions.

Create a procedures manual so everyone who works with the plan, including payroll providers or third party administrators, understand the process of administering loans and hardship distributions.

Establish a written policy for approving plan loans, such as the interest rate and repayment period. Develop a system for determining a participant's maximum loan amount. This is a good spot to use software or other automated tools. Any exceptions you make to the general rules you've established should be documented.

Late loan payments can be a headache. How are you going to monitor payments? Work with payroll to make sure payments are being withheld from paychecks and forwarded to the plan. It's important to have a reasonable cure period.

Make sure employees understand their responsibility to let plan administrators know if loan payments are not coming out of their payroll checks. After all, missing payments could lead to a large tax bill for that employee.

Your procedures manual for hardship distributions should outline how to apply for a hardship, the approval process and the suspension of elective deferrals.

Despite your best efforts, it's still possible to make mistakes in carrying out a loan or hardship distribution program. If that happens, it's time to consider which IRS correction program you'll use to bring the plan back into compliance.

You can self-correct some loan and hardship mistakes, others require a voluntary correction program submission. You can read more about our correction programs on the Correcting Plan Errors page of our website.

If your plan is under audit, you may still correct errors through the Audit Closing Agreement Program. But if you're thinking you'll wait and just correct under Audit CAP, it's considerably more expensive than the other IRS correction programs. It always pays to find and correct mistakes as soon as possible.

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We've developed many tools to assist you and your clients with retirement plans, whether your question is "How do I choose a retirement plan?" or "How much money can I contribute to my retirement plan?"

You can visit our website at www.irs.gov/retirement. Or you can find Retirement Plans from the main irs.gov landing page by clicking the drop down arrow to the right of "information for."

There are two different ways you can discuss your questions with a retirement plan specialist. You can email us at RetirementPlanQuestions@irs.gov or, if you prefer, call our Customer Account Services toll-free at (877) 829-5500. Our specialists must respond to all email questions by telephone, so please remember to include your phone number.

We also have two free, electronic newsletters, the *Employee Plans News* and *Retirement News for Employers*.

You can easily subscribe to these newsletters. Just click on "Newsletters" on our Retirement Plans landing page, then "Subscribe," and provide us with your email address.

That’s all it takes. Then, whenever we issue an edition, you’ll receive a message in your email inbox with a link.

Thanks for joining us in our discussion of plan loans and hardship distributions. For more information about tax rules for retirement plans, be sure to visit us soon at www.irs.gov/retirement.

Questions?