

2018 Tax Reform Series: A Change to Participant Loan Rollovers

JacksonLewis

Article By

[Raymond P. Turner](#)

[Jackson Lewis P.C.](#)

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One welcome qualified plan change under the [Tax Cuts and Jobs Act](#) is the extension of the period within which a participant may pay the amount of an “offset” of an outstanding plan loan to another qualifying plan or IRA to accomplish a tax-free rollover of the loan offset amount. The change became effective January 1, 2018.

A distribution of a plan loan offset occurs when, under the plan terms, a participant’s accrued benefit is reduced (or offset) in order to repay the loan. A distribution of a plan loan offset amount may occur in a variety of circumstances, such as where the plan terms require that, in the event of the participant’s request for a distribution, a loan be repaid immediately or treated as in default. The new rule applies to unpaid accrued loan amounts that are offset from the participant’s plan account at plan termination or at or after severance from employment if the plan provides that the accrued unpaid loan amount must be offset at such time. Prior to this law change, the deadline to roll over the offset was the 60th day after the date the loan offset arose. As of January 1, 2018, the deadline is the *filing due date (including extensions) for the participant’s tax return for the year in which the loan offset amount arises*. As a result of this change, the loan offset rollover period can be as long as 21 months where the loan offset occurs early in the calendar year and

the participant requests an extension of his or her Form 1040 deadline for the year of the offset.

The change means that a qualifying participant who desires to defer taxes on the maximum amount of distributions by rolling over all of his or her distributed account in a plan (including qualified plans such as 401(k) plans, 403(b) plans or governmental 457(b) plans) will now have significantly more time to accumulate from other sources an amount equal to the accrued and outstanding unpaid principal and interest on any plan loan that was earlier extended to him or her and treated as an offset and then pay and roll over such amount to another qualifying plan or IRA.

Note, however, that such tax-free rollover treatment does *not* apply to any offset amount under a loan that has already been deemed to be taxed as a distribution under the Code (and reportable on Form 1099-R) either because its terms did not comply with the Code or because it remained in default past the plan's default cure period (which cannot be longer than the end of the calendar quarter that begins after the quarter in which the default arises). The amount of such a defaulted loan will, absent correction under the EPCRS plan correction procedures, be treated as of the end of the allowed cure period as if it were a taxable distribution from the plan that can also be subject to the 10% early distribution penalty tax.

Finally, remember that a loan offset amount is treated as both a *repayment* and a *distribution* of a plan loan amount. Therefore, unless a deemed tax distribution (as discussed above) has occurred, the offset amount will be taxed to a participant except where an amount equal to the offset is timely rolled over tax-free by the participant. The new liberalization of the rollover period for offsets will make possible many more such rollovers.

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