The Coronavirus and Retirement Plans

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The Coronavirus Aid, Relief, and Economic Security Act, also known as the CARES Act, is a law that was passed to address the economic fallout of the Covid-19 pandemic in the United States. The Act contains several measures to assist businesses and individuals in lessening the impact of the shutdown of the U.S. economy, including several benefits for retirement plans. These changes allow people saving for retirement to access current savings early if the need arises to combat any loss of income. These "tax breaks" allow early withdrawals from retirement plans without penalty. For example, withdrawals from these plans before age 59 ½ were charged an additional 10% tax on top of the highest income tax rate for that individual's income level. The CARES Act eliminated the 10% penalty tax and allowed for the payment of taxes due over three years versus one year. The limit on that Covid-19 related withdrawal is up to $100,000.

For the elderly, the Act also allows individuals over 72 to postpone taking required minimum distributions (RMDs). The size of those distributions is a function of the market value of the retirement plan and the age of the retiree. This RMD is an attempt by the government to extract ordinary income taxes from retirees who had built up a savings nest egg over their working years. These RMDs also deplete the size of the savings and could force a retiree to take more than the RMD in retirement as the savings pool became depleted. Unfortunately, this exemption lasts for only one year. Not taking the distribution is a good idea that can also reduce the tax bill for 2020. The "saving" can, over time, make a big difference in the size of the retirement plan.

If you are one of those people who must take a withdrawal from your retirement to tide you over until the virus passes, then it is important for you to consider what assets you should liquidate in order to both satisfy your current needs and maintain the ability for your retirement portfolio to grow over time. Not increasing the chances that one will have to accept a lower standard of living in retirement is key! The first step is to evaluate your portfolio's current asset allocation and deciding which assets offer the most growth potential. Another important factor is: How many years do you have until retirement? If you are in retirement and have built up a substantial nest egg, then you should consider selling riskier assets. Retirees should also evaluate the current return characteristics of investment alternatives to anticipate the risks versus returns of selling one asset versus another. To maintain the current structure of a portfolio, just selling an equal amount of each asset class to raise the needed funds is a viable option. These suggestions also apply to beneficiary IRAs.

For investors with a long-term investment horizon and for those who hold some mix of assets in bonds and stocks, the logical strategy is to sell bonds, which have a low current yield, and maintain positions in a diversified stock portfolio; which are recovering from the impact of the virus as economies begin to re-open. There could be additional stock market volatility until the virus passes, but the worst seems to be past and a general stock market recovery should be a reasonable expectation.