



North Carolina
Total Retirement Plans



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MEMORANDUM

TO: NC Supplemental Retirement Board of Trustees

FROM: Reid Chisholm, Assistant General Counsel

DATE: August 27, 2020

SUBJECT: Revisions to the Supplemental Retirement Plans' Loan Policy

The attached loan policy includes the following revisions.

CARES Act Provision: Increased Loan Maximum

As discussed at the Board's special meeting on April 20, the CARES Act permits plans to increase the maximum loan amount for participants who are eligible for a coronavirus-related distribution (CRD). From March 27, 2020 through September 22, 2020, the maximum loan amount for a CRD-eligible participant is the lesser of \$100,000 or 100% of the participant's account balance. From March 27, 2020 through September 22, 2020, a CRD-eligible participant is permitted to take a second loan from the plans. This provision was implemented following the Board's special meeting on April 20.

CARES Act Provision: Loan Repayment Deferrals

Also, as discussed at the April 20 meeting, the CARES Act permits CRD-eligible participants to defer loan repayments that are due between March 27, 2020 and December 31, 2020.

Repayments are deferred through the end of 2020 and restart in January 2021. The term of the loan is extended to account for the number pay periods in 2020 for which repayments are deferred. However, interest continues to accrue during the deferral period. Following the deferral period, the loan will be re-amortized to account for the extended term and the interest that accrues during the deferral period. This provision was implemented following the Board's special meeting on April 20.

Aggregation of Loans Across Plans

Pursuant to the Internal Revenue Code, the maximum loan amount may be reduced by a participant's previous loans over the prior 12 months from defined contribution plans other than the North Carolina Supplemental Retirement Plans. Prudential does not have access to information from these non-SRP plans; therefore, the loan policy is clarified to place the responsibility on the participant for complying with these restrictions and reducing the requested loan amount from the plans accordingly.



Loan Repayment and Coupon Conversion Following Termination

A participant is required to make loan repayments through payroll deduction during the participant's period of employment. Following termination, a participant can continue to make loan repayments by mailing checks to Prudential. Participants also have the option of purchasing a coupon book from Prudential to manage repayments. The coupon book costs \$100. The current policy requires coupon books, but the amendments make this optional, which is consistent with Prudential's practice.

Application to the NC 403(b) Program

The current loan policy is written explicitly for the two state-sponsored plans, the NC 401(k) and NC 457 Plans. The 403(b) plans that participate in the NC 403(b) Program are sponsored by school districts and community colleges, which are responsible for approving loans to 403(b) participants. Nonetheless, the provisions of the current loan policy effectively govern the administration of loans within the NC 403(b) Program. Therefore, the revised policy explicitly recognizes that the provisions of the loan policy apply to the NC 403(b) Program.

Plan Audit and Administrative Review

With the exception of the CARES Act provision mentioned above, the plans allow only one loan from each plan. Earlier this year as the result of a Plan Audit and Administrative Review, Prudential discovered that it erroneously permitted 16 loans above the one-loan limit from the NC 457 Plan from April 17, 2009 through August 22, 2019. The participants were permitted to take an additional loan from the NC 457 Plan if they defaulted on their first loan and the loan was offset in error when the participant turned 59½ instead of 70½. In-service distributions are allowed at 59½ in the NC 401(k) Plan but at 70½ in the NC 457 Plan. Under the IRS's correction guidelines, this error can be addressed by a retroactive amendment to the loan policy.

Staff recommends that the Board approve the revised loan policy in the attachment.



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Attachment – Revised Loan Policy

Loan Policy for the NC 401(k) and NC 457 Plans and the NC 403(b) Program

This Loan Policy is incorporated into the plan documents for the NC 401(k) Plan and the NC 457 Plan and is intended to be consistent with applicable law. In the event of a conflict between the provisions of this Loan Policy and the provisions of the plan documents and/or applicable law, the provisions of the plan documents and/or applicable law shall control. For the NC 403(b) Program, the school districts and community colleges that sponsor the 403(b) plans are responsible for approving loans.

1. Definitions.

- a. Administrator. The term “Administrator” refers to the North Carolina Department of State Treasurer. The “Primary Administrator,” as described in Articles 8.02(a), 8.02(e), 10.01, and 10.05 of the plan document for the NC 401(k) Plan, and the “Plan Administrator,” as described in Articles 2.23, 9.1(b), and 9.2(l) of the plan document for the NC 457 Plan, are referred to collectively as the “Administrator.”
 - b. Employer. The term “Employer” is defined in Sec. 1.14 of the plan document for the NC 401(k) Plan document and Sec. 2.12 of the plan document for the NC 457 Plan. For the NC 403(b) Program, the term “Employer” refers to the entity that sponsors the 403(b) plan that participates in the NC 403(b) Program.
 - c. Member. The term “Member” is defined, as applicable, as a Member or a Participant, as defined in the plan document for the NC 401(k) Plan and the NC 457 Plan, respectively, who is actively employed by an Employer. The term also applies to a participant in a 403(b) plan that participates in the NC 403(b) Program.
 - d. NC 401(k) Plan. The term “NC 401(k) Plan” is defined as the Supplemental Retirement Income Plan of North Carolina.
 - e. NC 403(b) Program. The term “NC 403(b) Program is defined as the North Carolina Public School Teachers’ and Professional Educators’ Investment Plan.
 - f. NC 457 Plan. The term “NC 457 Plan” is defined as the North Carolina Public Employee Deferred Compensation Plan.
 - g. Plans. The terms “Plan” and “Plans” are defined, respectively, as the NC 401(k) Plan, the NC 457 Plan, and the NC 403(b) Program individually and collectively.
 - h. Recordkeeper. The term “Recordkeeper” is defined as the vendor that provides recordkeeping and communications services for the NC 401(k) and NC 457 Plans, including maintaining Members’ accounts and processing loans.
2. Loan Fee. The Recordkeeper will charge a one-time, non-refundable application fee of \$60.00 to Members for each new loan and may charge a one-time, non-refundable fee of

\$100 to establish loan repayments ~~following a Member's termination of employment other than by payroll deduction (i.e., see~~ Direct Billing Repayments in Section 2618). The Administrator may increase this fee as to new loans and may charge an additional annual maintenance fee for all loans by notice to or agreement with the Recordkeeper or other party administering loans and repayments.

3. **Application Methods.** Members may apply for loans using one of the following methods:
 - a. Interactive Voice Response System (IVR);
 - b. The Plans' website, www.ncplans.prudential.com; or
 - c. Member Service Representative.
4. **Outstanding Loans.** Each Member who applies for a loan must certify as to the existence and the amount of any outstanding loans (including any loans deemed distributed) from the ~~PlansNC 401(k) Plan and the NC 457 Plan~~.
5. **Loan Limit: Small Account.**¹ A Member with an account balance equal to or less than \$20,000 can borrow the lesser of:
 - a. 100% of the Member's vested account balance; or
 - b. \$10,000.
6. **Loan Limit: Large Account.**¹ A Member with an account balance of more than \$20,000 can borrow the lesser of:
 - a. \$50,000 (reduced by the excess, if any, of the Member's highest outstanding balance of loans from the Plans during the one-year period ending on the day before the date on which such loan is made); or
 - b. One-half (1/2) of the Member's vested account balance.
- Pursuant to Internal Revenue Code Section 72(p)(2)(A)&(D), the maximum loan amount may be reduced by a Member's previous loans from defined contribution plans other than the NC 401(k) and NC 457 Plans and the NC 403(b) Program. A Member is solely responsible for complying with these restrictions and reducing the requested loan amount from the Plans accordingly.
7. **Minimum Loan Amount.** A Member may not borrow less than \$1,000.
8. **Maximum Number of Loans.**^{1,2} A Member may simultaneously have only one outstanding loan in ~~each of the Plans NC 401(k) Plan and one outstanding loan in the NC 457 Plan~~. For purposes of this limit, an "outstanding loan" includes a loan for which a "deemed distribution" has occurred, following the Member's default and pursuant to Treas. Reg. §1.72(p)-1, unless the Member repays the outstanding balance of the defaulted loan (including accrued interest through the date of repayment).
9. **Rollovers.** A Member may not make and the Plans will not accept a direct rollover of a loan from the plan of a Member's former employer. A Member may not make a direct rollover of a loan issued under the Plans to another plan. A loan goes into default if a Member rolls

over the unloaned amount of the account to another plan.

10. **Note; Pledge/Assignment**. A Member must agree to the terms of the loan as set forth in a promissory note along with a pledge or assignment of the portion of the account balance used for security on the loan. Negotiation of the loan check signifies acceptance of the loan terms and the pledge or assignment.
11. **Spousal Consent**. The Member is not required to obtain his/her spouse's consent to use the account balance as security for the loan regardless of the value of the Member's account balance.
12. **Loan Account**. A Member's loan is treated as a segregated investment on behalf of the individual Member for whom the loan is made. Payments of principal and interest on the loan shall be credited to the Member's account. Each loan shall be made in cash and shall be deemed to be made on a proportionate basis from each pre-tax type of contribution. Assets from a Roth account shall be included only if pre-tax contributions are insufficient to cover the loan.
13. **Interest Rate**. The interest rate on Members' loans will be equal to the bank prime loan rate, as reported by the U.S. Federal Reserve on the last business day of a calendar quarter, plus one percentage point. The rate will be declared quarterly and will be effective for loans made on and after the first business day of the subsequent quarter. The Administrator reserves the right to change the basis for determining the interest; however, such change will apply only to loans issued after the change takes effect.
14. **Term of Loan Generally.¹** The maximum loan term is five (5) years, except as provided in Items 15 and 22 below. No loan may be made for a term of less than twelve (12) months.
15. **Term of Residential Loan.¹** The maximum loan term for a loan obtained from the Plans that is used to acquire any dwelling unit, which, with a reasonable time, is to be used to purchase a principal residence of the Member, is up to fifteen (15) years. A copy of the purchase contract or signed statement from the Member confirming that the proceeds will be used to purchase or build a principal residence within a stated short period of time will be the level of proof to determine whether a loan is being used to buy a principal residence.
16. **Loan Refinancing**. Loan refinancing is not permitted.
17. **Repayments by Payroll Deductions**. Loan repayments will be made by a deduction from each payroll following issuance of the loan. Repayment will begin as soon as is administratively practicable following issuance of the loan, but no more than two (2) months from the date the loan is issued. Each Employer will remit repayments by payroll deduction in accordance with its own payroll schedule.
18. **Direct Repayments**. Should loan repayments for an actively employed Member not be possible from payroll, payments will be due directly from the Member by check or similar payment method. Should a Member not be expected to be able to use payroll repayment or to return promptly to payroll payment, the Administrator may authorize regular payment no less frequently than quarterly on a revised schedule of amount and payment dates calculated to repay the loan with interest in full in substantially equal payments over the remaining original period of the loan.
19. **Prepayments**. Loans may be paid in full at any time without penalty. Any amount paid in

excess of the scheduled payment will be applied first to interest and then to principal unless otherwise specified by the Member. Prepayments will not change the amount or timing of subsequent payments due prior to pay-off of the loan but will simply reduce the total number of payments to be made unless otherwise specified by the Member.

20. **Timing of Loan**. No loan may be made to a Member sooner than seven (7) calendar days after the satisfaction or termination of a prior loan from the same Plan to the Member.
21. **Suspension of Loan Payments Generally**.¹ A Member with an outstanding loan may suspend loan payments to the Plan from which the loan was made for up to 12 months for any period during which the Member is on an authorized leave of absence without pay or reduced pay that is less than the required loan repayments. Upon the Member's return to employment (or at the end of the 12-month period, if earlier), the Member shall resume making payments on the loan, based on one of the following two alternatives.
 - a. **Payment Alternative #1**. The Member may increase the monthly payments to an amount that is sufficient to repay the loan in full, including interest that accrues during the leave of absence, over the remaining term of the loan.
 - b. **Payment Alternative #2**. The Member may re-amortize the outstanding loan amount, including interest that accrues during the leave of absence, over a period not to exceed five (5) years from the original date of the loan (the "Five-Year Term"); provided that the payment amounts after the suspension period are not less than before the suspension.
22. **Suspension of Loan Payments for Military Leave**. A Member with an outstanding loan who is absent from employment due to a military leave in the uniformed services of the U.S. may have his/her loan payments suspended for any period during which such Member is on military leave. The payment alternatives in Item 21 apply to such Member, except that:
 - a. The Five-Year Term may be extended by the amount of time the Member was on military leave; and
 - b. The interest rate may not exceed 6% during the military leave; provided that the Member provides the Administrator with written notice and a copy of his/her military orders no later than 180 days after the date the Member completes such military service.
23. **Investment of Loan Repayments**. Loan repayments will be invested according to the Member's investment allocation for current contributions.
24. **Grace Period and Default**. If payment is not received, whether because of insufficient payroll or failure to make a scheduled direct payment, the loan will be considered in default unless payment is made within a grace period. The grace period is defined as 90 days after each next expected payment date but may be extended by determination of the **Plan** Administrator to the date the late payment is actually made for specific causes that are beyond the Member's control and that are consistently determined and applied on a nondiscriminatory basis. In no event may the grace period extend beyond the end of the calendar quarter following the calendar quarter in which the payment was originally due.
25. **Deemed Distributions**. Loans are reported to the Internal Revenue Service as deemed

distributions upon a determination by the Administrator (or its agent) of one of the following:

- a. The failure to make a payment within the grace period described in Item 24, above;
- b. Death of the Member, unless repaid within 90 days following the next expected payment date;
- c. Any statement or representation by the Member in connection with the loan which is false or incomplete in any material respect;
- d. Failure of the Member to comply with any of the terms of the note and other loan documentation; or
- e. Termination of the Plan.

26. **Direct Billing.** ~~Follow termination of employment, a Member may continue making payments directly by check or similar payment method (as approved by the Recordkeeper), unless the Member pays the loan in full. The Member must make regular payments no less frequently than quarterly on a schedule of amount and payment dates calculated to repay the loan with interest in full in substantially equal payments over the remaining original period of the loan. To assist in direct billing repayments following termination, a Member may request a coupon book and a re-amortization of the loan, provided that the re-amortization requires payment dates and amounts. Within 90 days of termination of employment, a Member may request to make payments at least quarterly using direct billing on a revised schedule of amount and payment dates calculated by the Administrator Recordkeeper to repay the loan with interest in full in substantially equal payments over the remaining original period of the loan. The Recordkeeper charges a \$100 fee for A the coupon book and re-amortization and requires a request by the Member within 90 days of termination of employment conversion fee of \$100 will apply in changing from payroll deduction to direct billing.~~
27. **Termination of Employment.** The outstanding loan balance of a Member who terminates employment and does not request to make payments using direct billing as described in Item 26 will be reported to the Internal Revenue Service as a distribution for tax purposes on the earlier of the date on which he takes a distribution of all of his account or the end of the grace period described in Item 24.
28. **Offset.** If a Member defaults on a loan and it is deemed distributed, the Plans may not offset the Member's loan balance until the Member is otherwise entitled to an immediate distribution of the portion of the account balance equal to the outstanding loan balance. (For this purpose, a loan default is treated as an immediate distribution event to the extent the law does not prohibit an actual distribution of the type of contributions that would be offset as a result of the loan default.) The Member may repay the outstanding balance of a deemed distributed loan (including accrued interest through the date of repayment) at any time.
29. **Rules for Offset.** Pending the offset of a Member's account balance following a defaulted loan, the following rules apply:
 - a. Post-default interest accrual on a defaulted loan applies only to loans initiated after December 31, 2001;

- b. Interest continues to accrue on the amount in default until the time of the loan offset or, if earlier, the date the loan repayments are made current;
- c. A subsequent offset of the amount in default is not reported as a taxable distribution, except to the extent the taxable portion of the default amount was not previously reported by the Plan as a taxable distribution;
- d. The interest that accrues after a deemed distribution has been included in a loan offset is not reported as a taxable distribution at the time of the offset;
- e. A Member may repay the outstanding balance of a defaulted loan at any time, even if such loan has been reported to the Internal Revenue Service.

Endnotes

¹ To the extent permitted by the Coronavirus Aid, Relief, and Economic Security (CARES) Act (Public Law 116-136), the provisions below apply to this Loan Policy.

CRD-eligible Member

A “CRD-eligible Member” is a Member who qualifies for a “coronavirus-related distribution” pursuant to Section 2202(a)(4)(A)(ii) of the CARES Act.

Increased Loan Maximum

From March 27, 2020 through September 22, 2020, the maximum loan amount for a CRD-eligible Member is the lesser of \$100,000 or 100% of the Member’s account balance. From March 27, 2020 through September 22, 2020, a CRD-eligible Member is permitted to take a second loan from each Plan.

Loan Deferral

If a CRD-eligible Member has an outstanding loan repayment due in the period from March 27, 2020 through December 31, 2020, the Member can defer these repayments through the end of 2020 and restart repayments in January 2021. The term of the loan shall be extended to account for the number pay periods in 2020 for which repayments were deferred. However, interest continues to accrue during the deferral period. Following the deferral period, the Recordkeeper shall re-amortize the loan such that the loan shall be repaid with interest in full in substantially equal payments over the remaining term of the loan.

² From April 17, 2009 through August 22, 2019, a Member was permitted to take a second loan from the NC 457 Plan if such Member defaulted on the first loan and the loan was offset in error when the Member turned 59½ instead of 70½.