

SECURE 2.0 Provides New Ways to Take Penalty-Free Distributions



The SECURE 2.0 Act provides more ways for individuals to access their retirement savings and creates new exceptions to the 10% early distribution penalty tax. Normally, IRA owners and retirement plan participants are subject to this penalty tax if they withdraw assets before age 59½. Many exceptions already existed before SECURE 2.0.

We cover some of the new SECURE 2.0 provisions—such as those that allow distributions to be taken for certain emergency expenses and that create pension-linked emergency savings accounts—in separate articles. But here we’ll focus on several new distributable events and penalty tax exceptions that provide more alternatives for account owners.

Distributions for Domestic Abuse Victims

SECURE 2.0 creates an optional distribution provision for defined contribution plans (including 401(k) plans, 403(b) plans, and governmental 457(b) plans) that are not subject to the joint and survivor annuity rules. Individuals may also take these penalty-free distributions from SEP plans, SIMPLE plans, and IRAs.

- Domestic abuse victims may withdraw up to the lesser of
 - \$10,000 (indexed), or
 - one-half of their IRA balance or vested retirement plan account balance.
- The distribution must occur within one year of the abuse by a spouse or domestic partner and is not subject to the 10% early distribution penalty tax.
- Individuals can repay these distributions within a three-year period, starting the day after the date on which the distribution was received. (This rule is similar to the qualified birth or adoption distribution (QBAD) repayment rule.)
- This distribution option is available starting in 2024.

Distributions for Individuals with a Terminal Illness

SECURE 2.0 creates a new 10% early distribution penalty tax exception for terminally ill individuals. But this is not a new distributable event for employer plans; participants must still have another permissible distribution event from their 401(a) defined contribution plan (including a 401(k) plan), 403(a) annuity plan, or 403(b) plan. Terminally ill individuals may also take penalty-free distributions from their Traditional and Roth IRAs.

- There is no limit to the amount that an individual may distribute.
- A physician must certify that the individual has an illness that can reasonably be expected to result in death within 84 months after the certification.
- Individuals may repay these distributions under the same rules that apply to QBADs.
- This penalty tax exception applies to distributions taken after December 29, 2022.

Distributions for Public Safety Employees and Private Sector Firefighters

Plan participants who separate from service during or after the calendar year in which they attain age 55 are not subject to the 10 percent early distribution penalty tax on distributions that they receive after the separation.

Previously, the same penalty tax exception applied to qualified public safety employees who separated from service from a governmental plan during or after the calendar year in which they attained age 50.

SECURE 2.0 contains three provisions that expand this penalty tax exception in the following ways.

- Private sector firefighters are now eligible for the same treatment when they take distributions at age 50 from 401(a) defined contribution plans (including 401(k) plans) and defined benefit plans, 403(a) annuity plans, and 403(b) annuity plans.
- The 10 percent early distribution penalty tax is now waived for those qualified public safety employees and private sector firefighters who separate from service after attaining age 50 or who incur 25 years of service under the plan, whichever is earlier. This applies to distributions taken from 401(a) defined contribution plans (including 401(k) plans) and defined benefit plans, 403(a) annuity plans, and 403(b) annuity plans.
- The definition of “qualified public safety employee” now includes those who provide “services as a corrections officer or as a forensic security employee providing for the care, custody, and control of forensic patients.”

It's important to note that if the plan document does not treat separation from service as a distributable event, then the participant will need to have another distributable event (e.g., disability) in order to take a distribution.

These provisions apply to distributions taken after December 29, 2022.

More Guidance to Come

As with many of the SECURE 2.0 provisions, we expect further guidance from the IRS and the Department of Labor. Employers may decide to delay offering these distribution options to plan participants. But IRA owners and plan participants can individually decide whether to use the penalty tax exceptions when filing their taxes. The IRS has released an updated 2022 Form 5329, *Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts*, to incorporate the new penalty tax exceptions that became effective in 2022. And we may receive guidance that provides some interim relief while we await regulations or other pronouncements.

