

# Details of the SECURE 2.0 Act: Provisions Related to Early Distribution Penalties



RETIREMENT MANAGEMENT SERVICES, LLC  
*Plan Consulting • Administration • Design*

RETIREMENT MANAGEMENT SERVICES, LLC  
905 Lily Creek Road Louisville, KY 40243  
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## *SECURE 2.0 Act: Early Distribution Penalties*

On December 29, 2022, the SECURE 2.0 Act was included as part of a larger omnibus spending package, the Consolidated Appropriations Act, 2023. The legislation contained eight provisions which expanded the exemption to the early distribution penalty. Prior to the SECURE 2.0 Act exceptions to the 10% premature distribution penalty for distributions from qualified plans only included:

- to a beneficiary due to a participant's death;
- to a disabled participant;
- as part of a series of substantially equal periodic payments made over the life of the participant or joint lives of participant and beneficiary which begin after the participant separates from service;
- when the participant separates from service after attaining age 55;
- to an alternate payee pursuant to a qualified domestic relations order;
- for certain medical expenses;
- as part of a qualified reservist distribution;
- to a qualified public safety employee (police, firefighter, emergency medical services) from a governmental defined benefit plan who separates from service after attaining age 50; and
- up to \$5,000 for qualified birth or adoption

### **Section 331 of the Secure 2.0 Act removes the early distribution penalty for distributions due to a Federally Declared Disaster.**

Section 331 under the SECURE 2.0 Act Provided permanent rules relating to the use of retirement funds in the case of qualified disaster. Distributions are limited to \$22,000 per disaster (rather than the \$100K Allowed in Cares Act). May be repaid in 3-year period after distribution. Income inclusion for tax purposes maybe spread over 3 years. Additionally, amounts distributed prior to the disaster to purchase a home would be permitted to be recontributed, and an employer would be permitted to provide for a larger amount be borrowed from a plan by affected individuals and for additional time for repayment of plan loans owed by affected individuals. Exempt from the 10% early withdrawal Penalty

**EFFECTIVE DATE:** This section of the Act is effective for distributions that were made after December 31, 2021.



Retirement Management Services, LLC  
905 Lily Creek Road  
Louisville, KY 40243

**[www.consultRMS.com](http://www.consultRMS.com)** Phone: 502-429-0767

## Section 326 of the Secure 2.0 Act removed the early distribution penalty for distributions to terminally ill participants.

Section 326 of the Secure 2.0 act provided an exception to the 10% early distribution tax for distribution to a terminally ill individual. Participants must provide evidence required by plan administrator to support terminally ill diagnoses. The distribution may be repaid. This is not a special distribution option but rather an exception to the 10% early penalty only.

**EFFECTIVE DATE:** This section of the Act is effective for distributions made after December 29, 2022.

## Section 120 of the Secure 2.0 Act removed the early distribution penalty for auto-portability distributions.

Section 120 of the Secure 2.0 Act added to the list of transaction exemptions for service providers providing automatic portability services, such as automatic transfer of a participant's default IRA (established in connection with a distribution from a former employer's plan) into the participant's new employer's retirement plan, unless the participant elects otherwise.

**EFFECTIVE DATE:** This section of the Act is effective for distributions made after December 31, 2024.

## Section 314 of the Secure 2.0 Act removed the early distribution penalty for victims of domestic abuse.

Under Section 314 of the Secure 2.0 Act a withdrawal is permitted from a qualified plan without penalty to the participant that is a victim of domestic abuse. The amount allowed is the lesser of \$10,000 (indexed) or 50% of balance. This exemption applies to plans not subject to section 417. Withdrawal is exempt from 10% penalty. May be recontributed to applicable eligible retirement plans, subject to certain requirements. This is an optional type of distribution and will be up to individual employers to decide to add to their plan.

**EFFECTIVE DATE:** This section of the Act is effective for distributions made after December 31, 2024.



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## Section 115 of the Secure 2.0 Act removed the early distribution penalty for a personal emergency.

Section 115 of the Secure 2.0 Act allows one distribution per year of up to the lesser of \$1,000 or Vested Account balance, with the OPTION to repay the distribution within 3 years. No further emergency distribution would be permissible during the 3-year repayment period unless recontribution occurs. Exemption from 10% penalty. A plan sponsor may rely on participant certification absent actual knowledge.

**EFFECTIVE DATE:** This section of the Act is effective for distributions made after December 31, 2024.

## Section 323 of the Secure 2.0 Act clarified the early distribution penalty for substantially equal periodic payments.

Section 323 of the Secure 2.0 Act gave clarification of the substantially equal periodic payment rule. The exception from the 10% early distribution tax for substantially equal periodic payments will continue to apply in the case of a rollover of the account, an exchange of an annuity providing the payments, or an annuity that satisfies the required minimum distribution rules. There is no inference on rules prior to enactment.

**EFFECTIVE DATE:** This section of the Act is effective for distributions made after December 31, 2024.

## Section 334 of the Secure 2.0 Act removed the early distribution penalty for the purchase of LTC premiums.

Section 334 of the Secure 2.0 act now allows defined contribution plans to distribute up to \$2,500 (indexed) per year for the payment of premiums for certain specified long-term care insurance policies. Distributions from plans and IRAs to pay such premiums would be exempt from the additional 10% tax on early distributions. The participant is required to file a premium statement with plan insurer. It also required the development of a website of certified LTC providers by the Treasury department.



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**EFFECTIVE DATE:** This section of the Act is effective for distributions made after December 31, 2025.

These sections of the SECURE 2.0 Act are intended to allow participants to take a distribution in specific situations without penalty. There are so many questions on how to administer the changes which will require additional guidance and clarification to implement all new provisions.

Authors Note: We recommend that before a participant takes a distribution prior to attaining age 59½, they and/or plan sponsor should confirm that an available exemption applies to the premature distribution penalty.



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