Leveraging SECURE 2.0 for Disaster Relief: Essential IRS Guidelines

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The SECURE 2.0 Act of 2022 (SECURE 2.0) enacted on December 29, 2022, specifically Section 331, amended the Internal Revenue Code and added special rules for use of retirement funds for individuals impacted by qualified federally declared disasters.

In response, the IRS issued a fact sheet on May 19, 2024, clarifying how these provisions can be applied. Below, we summarize key points from the IRS, helping you understand how these updates may offer financial relief in disaster recovery situations.

Federally Declared Disasters (Qualified Disasters)

- A qualified disaster is any disaster with respect to which a major disaster has been declared by the president.

Qualified Individuals

- The individual's principal residence is in the qualified disaster area and
- The individual has sustained economic loss by reason of the qualified disaster.
    - Economic loss may be loss, damage, or destruction of real or personal property, displacement from home or loss of livelihood due to temporary or permanent layoffs.

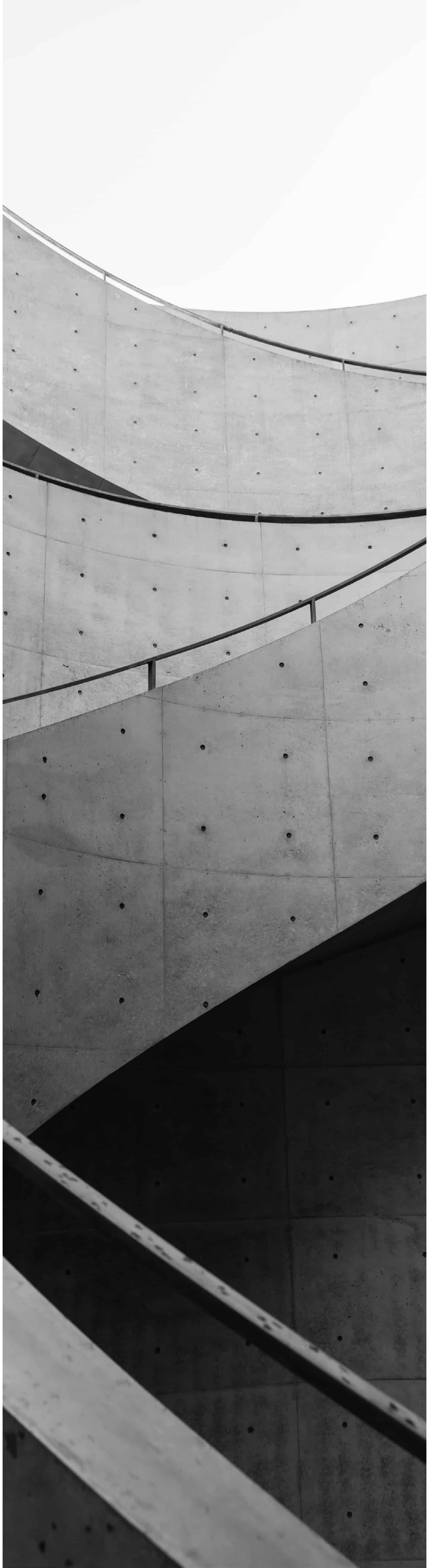
Penalty-Free Withdrawals

Eligibility: Qualified individuals residing in an area affected by a federally declared disaster.

Withdrawal Limit: Up to $22,000 can be withdrawn from qualified retirement plans such as a 401(k), 403(b) and IRAs.

Exemption From 10% Penalty: Early withdrawals made for disaster recovery purposes are exempt from the standard 10% early withdrawal penalty for individuals under age 59 ½.

Tax Treatment: Withdrawals are taxed as income, but the tax burden can be spread over three years. The option to recontribute the funds to the retirement account within three years is also available, which can reduce taxable income.



Repayment of Withdrawals

- If individuals recontribute the disaster-related withdrawal to their retirement account within three years, they can claim a refund of any taxes paid on the distribution.

Retirement Plan Loans

Loan Limit Increase: The loan limit from retirement plans increases to $100,000 or 100% of the vested balance (not including an IRA) for those affected by a federally declared disaster.

Extended Repayment Period: The repayment term for disaster-related loans is extended by one year (in addition to any current payment schedule) to provide more time for affected individuals to recover without financial strain.

Employers have the option to adopt these changes, but individuals can still claim relief when filing taxes.

Prior to the changes made by SECURE 2.0, there was no disaster relief allowing distributions and loans from retirement plans. These new provisions are intended to provide flexibility in tax treatment, loan limits, and repayment periods to ease the burden on those rebuilding after significant disasters.

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Sources

1. https://www.irs.gov/newsroom/disaster-relief-frequent-asked-questions-retirement-plans-and-iras-under-the-secure-20-act-of-2022

Important Disclosures

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