Client Articles

What Is a Hardship Withdrawal?

Description

A hardship withdrawal is a special type of distribution from an employer-sponsored retirement plan, which the IRS allows only for participants who can prove they are facing an "immediate and heavy financial need." However, the IRS does not require retirement plans to allow hardship withdrawals. Instead, it leaves that decision up to each individual plan.

To determine whether your plan allows hardship withdrawals, ask your plan sponsor or plan administrator. You can also check in the plan document, which is the official communication that details all of your plan's rules and regulations.

The money a participant receives from a hardship withdrawal can be taken from his or her accumulated elective contributions, but not from earnings on those contributions. Employer contributions may also be included in a hardship withdrawal, but only if the plan allows.

In order to qualify for a hardship withdrawal, a participant must prove that the money will be used to pay for at least one of the following expenses:

- Medical care for the participant, the participant's spouse, dependents, and/or beneficiaries.
- The purchase of the participant's principle residence (not including mortgage payments).
- Post-secondary education expenses for the participant, participant's spouse, dependents, and/or beneficiaries.
- Payments to prevent eviction or foreclosure.
- Funeral costs.

In addition, the worker requesting the hardship withdrawal needs to have previously obtained all other possible distributions and non-taxable loans available through the retirement plan.

The amount of a hardship withdrawal may not exceed the amount of the participant's stated financial need, and will be subject to ordinary income taxes and a 10% early withdrawal penalty. Participants who receive a hardship withdrawal are not allowed to repay the money back to the retirement plan and are generally not allowed to resume contributions to the plan for six months.

Required Attribution

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