

## Dos and Don'ts of Hardship Distributions

Given the current economic climate, a greater number of participants may request a [hardship distribution](#) from his or her retirement plan. To avoid jeopardizing the qualified status of the plan, employers and plan administrators must follow both the plan document and legal requirements before making hardship distributions.

Some retirement plans, such as [401\(k\)](#) and [403\(b\)](#) plans, may allow participants to withdraw from their retirement accounts because of a financial hardship, but these withdrawals must follow IRS [guidelines](#). For example, a plan may only make a hardship distribution:

- if permitted by the plan;
- because of an immediate and heavy financial need of the employee and, in certain cases, of the employee's spouse, dependent or beneficiary; and
- in an amount necessary to meet the financial need.

### Before making hardship distributions:

1. Review the terms of the plan, including:
  - i. whether the plan allows hardship distributions;
  - ii. the procedures the employee must follow to request a hardship distribution;
  - iii. the plan's definition of a hardship; and
  - iv. any limits on the amount and type of funds that can be distributed for a hardship from an employee's accounts.
2. Obtain a statement or verification of the employee's hardship as required by the plan's terms.
3. Determine that the exact nature of the employee's hardship qualifies for a distribution under the plan's definition of a hardship.
4. Document, as may be required by the plan, that the employee has exhausted any loans or distributions, other than hardship distributions, that are available from the plan or any other plan of the employer in which the employee participates.
5. If the plan's terms state that a hardship distribution is not considered necessary if the employee has other resources available, such as spousal and [minor children's assets](#), document the employee's lack of other resources.
6. Check that the amount of the hardship distribution does not exceed the amount necessary to satisfy the employee's financial need. However, amounts necessary to pay any [taxes or penalties](#) because of the hardship distribution may be included.
7. Ensure that the amount of the hardship distribution does not exceed any limits under the plan and consists only of eligible amounts. For example, a plan could limit hardship distributions to a specific dollar amount and require that they be made only from [salary reduction contributions](#).
8. If the plan's terms require that the employee is suspended from contributing to the plan and all other employer plans for at least 6 months after receiving a hardship distribution, inform the employee and enforce this provision.

If a plan does not properly make hardship distributions, it may be able to correct this mistake through the [Employee Plans Compliance Resolution System](#) (EPCRS).

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## IRS Retirement Plans Online Navigator

IRS EP has launched a new Web guide to help employers review retirement plan options and to make it easier for their employees to save for the future. The "IRS Retirement Plans Navigator" encourages small business owners to establish retirement plans by helping them choose a plan for their business. It also promotes tax law compliance with information and resources on maintaining plans and correcting plan errors.

Please add [www.retirementplans.irs.gov](http://www.retirementplans.irs.gov) to your organization's Web site so your clients and others visiting your site can benefit from its information and resources.