

**Vanguard**<sup>®</sup>

# **SECURE 2.0**

## **Act optional provision guide**

Terminal Illness Exception



## Effective date: Upon enactment of SECURE 2.0 (December 29, 2022)

Effective for 401(k), 403(b), and 401(a)

### Purpose

The SECURE 2.0 Act's optional Terminal Illness Exception (TIE) provision builds on recent industry and government momentum to give retirement plan participants more access to their retirement savings in certain situations. The TIE provision provides those participants who have been diagnosed with a terminal illness access to their retirement savings without a 10% early withdrawal penalty, as well as the ability to repay any portion of the distribution within three years. These options give participants facing a terminal illness more control over their retirement savings.

### Provision overview

This optional provision created an exception to the 10% early distribution penalty tax for terminally ill individuals who take a distribution from a qualified plan, effective for distributions taken after December 29, 2022. Participants who take a distribution when or after a physician has certified they are terminally ill also have the option to repay any portion of the distribution within three years.

- A terminally ill individual is someone certified by a physician that death is expected within 84 months.
- A terminal illness itself does not entitle a participant to a distribution. ("Terminal illness" is not a new distribution type; the participant must be otherwise eligible for a distribution from the plan.)
- Subject to the terms of the plan, there is no limit to the amount that a terminally ill participant may distribute.
- It is the participant's responsibility to claim the exception to the 10% excise tax for their distribution as part of their tax filing.

On December 20, 2023, the Internal Revenue Service (IRS) issued [Notice 2024-2](#) (the "Notice"), which, in addition to confirming that the repayment portion of the Terminal Illness Exception is optional for plan sponsors, significantly affects other key components of this provision.

- Plan sponsors do not have to recognize distributions to terminally ill participants when reporting the distribution (i.e., no special tax reporting or withholding is needed).
- Participants can treat any distribution (regardless of how it is categorized by the plan sponsor) as due to a terminal illness as long as it meets physician certification and timing requirements.
- A terminally ill participant may recontribute any portion of a distribution (up to the entire amount) to an IRA within three years of the original distribution.
- A participant's recontribution to their IRA will be treated as a rollover. Vanguard will not be reviewing rollovers to the plan to determine if the rollover constitutes repayment of a terminal illness distribution.

## Vanguard's approach

Vanguard's approach to the TIE simplifies the administrative requirements of plan sponsors, while still providing the benefits of both the exception and repayment options of this provision to plan participants.

In light of the Notice, Vanguard's recommendation for plan sponsors is to allow terminally ill participants to take in-service distributions for which they are already eligible, file for the 10% exception on their individual tax returns, and, if they choose, repay the distributions within three years to an IRA.

Provision detail	Plan sponsor guidance	Participant guidance
<b>Terminally ill individuals who take a distribution from a qualified plan after December 29, 2022, may qualify for an exception to the 10% early distribution penalty tax.</b>	The Notice made clear that terminal illness is not a new distribution type. Plan sponsors are not subject to any special reporting or withholding requirements for distributions to terminally ill participants. Participants can treat any distribution from their plan as due to terminal illness on their tax return, provided they have obtained a physician's certification at or before the time of the distribution.	Participants can treat any distribution from their plan as due to terminal illness on their tax return, provided they have obtained a physician's certification at or before the time of the distribution.
<b>Participants who take a distribution when or after a physician has certified they are terminally ill may repay any portion of the distribution to an IRA within three years.</b>	Due to complex requirements for a physician's certification of terminal illness, Vanguard is not supporting terminally ill participants' recontributions to an employer plan. Terminally ill participants may retribute any portion of a distribution to an IRA within three years of the original distribution. Recontributions will be treated as a rollover.	Terminally ill participants may retribute any portion of a distribution to an IRA within three years of the original distribution. Recontributions will be treated as a rollover.

## What to expect

Vanguard continues to monitor for regulatory updates related to the Terminal Illness Exception provision of SECURE 2.0. As with any large piece of legislation, there are some items in SECURE 2.0 that still need to be clarified or corrected. This will likely be done through a technical corrections bill, which has the potential to establish a separate distribution option for terminal illness. If a separate distribution reason for terminal illness becomes available, Vanguard will reevaluate our service offer and will share additional information with plan sponsors at that time.

As always, your Vanguard client success executive is here to help you with any questions you have about the Terminal Illness Exception or the SECURE 2.0 Act.

