72(T) DISTRIBUTIONS

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IRA Withdrawals Without IRS Penalties

If you need access to your retirement assets before age 59½, 72(t) distributions — also referred to as substantially equal periodic payments (SEPPs) — may be an option for you. SEPPs allow for early withdrawals from individual retirement accounts (IRAs) without Internal Revenue Service (IRS) penalties.

If you want to retire early and start a new business, or are faced with a job loss or otherwise need income, your financial professional can help you determine whether taking 72(t) distributions may be right for you. You also should consult with your tax or legal professional before taking any distributions from a retirement plan to be sure your planned withdrawals qualify for the exception to the premature distribution tax.

KEY BENEFITS

- Provides access to your retirement savings early
- Delivers income if you lose a job or are forced or choose to retire early
- Avoids the 10% IRS penalty tax on early withdrawals

POTENTIAL CANDIDATES FOR 72(t) DISTRIBUTIONS

Investors under age 59½ who:

- Want to retire early
- Have suffered a job loss
- Were forced to take early retirement

How 72(t) distributions work

Generally, taking distributions from a traditional IRA before age 59½ will result in an IRS early withdrawal penalty tax of 10%. Under Section 72(t), the penalty can be waived under certain circumstances, including an exception for distributions that are:

- Part of a series of substantially equal periodic payments (SEPPs) made on a regular basis — at least annually[1]
- Continued for at least five years or until the account owner reaches age 59½ — whichever is longer
- Calculated according to one of the three IRS-approved methods:
  - Required minimum distribution (RMD)
  - Fixed amortization method[2]
  - Fixed annuitization method[2]

Any variation from the scheduled 72(t) distribution — taking more or less — will typically result in a 10% premature distribution penalty tax, plus interest, on all past distributions unless the account owner dies, becomes disabled or the account is depleted. You also may face state tax consequences. However, if you select either the fixed amortization or fixed annuitization method, you are allowed a one-time, irrevocable switch to the RMD calculation method without incurring penalties.

While you can take 72(t) distributions from Roth IRAs, it generally is not necessary due to the fact that Roth IRA contributions can be withdrawn free of federal taxes or penalties at any time. In addition, amounts that were converted to a Roth IRA can also be distributed free of federal taxes (and free of the early withdrawal penalty if over age 59½ or at least five years have passed since the time of conversion). Thus, 72(t) distributions would apply only to the earnings in a Roth IRA, which would be taxable and incur a 10% penalty if the account was not held for five years and the owner is younger than 59½ (or other exceptions apply).

In addition to the three IRS-approved methods for calculating your substantially equal periodic payments, you may have a choice of three different life expectancy tables upon which to base your assumptions.[3]

You should discuss the financial impact of taking 72(t) distributions with your tax or legal professional.

Consolidate retirement assets

If you need to set up 72(t) distributions, a rollover IRA can help you consolidate assets from any former employer's plan and provide a holistic picture of your retirement assets. Some experts suggest that individuals explore the possibility of dividing overall retirement investments into two or more IRAs, one for taking 72(t) distributions and one that can continue to grow tax-deferred, thereby allowing individuals to maintain greater flexibility by not locking up all of their retirement savings in the one IRA that is being used for substantially equal periodic payments.

When contemplating a rollover of retirement savings from an employer-sponsored plan to an IRA, there are numerous factors to consider, including, among others: relative cost of investments and other plan services and features, fiduciary status of plan/IRA provider, access to participant loans (available from some employer plans, but not from IRAs), range of permissible investments, level of services provided, and potential tax and penalty implications (current and future).

Talk to your tax or legal professional to find out more.

You should consult with your tax or legal professional before taking any distributions from a retirement account. While 72(t) distributions provide a potentially advantageous way to access IRA assets early, dipping into retirement savings can have serious consequences and should be done only if necessary. Early withdrawal reduces the growth potential of your overall retirement portfolio and increases the risk of outliving your income in retirement. You also should consider whether you may return to the workforce in the future, which affects the size of the distribution you can take and the calculation method you use. Your financial professional can help you identify any potential risks to your retirement strategy.

LEARN MORE

For more information, please contact your financial professional.

This information is general in nature and has been distributed for informational purposes only and is not intended to constitute legal advice or a recommendation of any particular investment, strategy, investment manager or account arrangement. Please consult your legal or tax professional for more detailed information on legal or tax issues and guidance on your specific situation.

[1] Any variation from the calculated distribution amount — taking more or less — will result in a 10% penalty tax, plus interest, retroactively applied to all past distributions through the end of the year of the modification unless the account owner dies or becomes disabled, or the account is depleted.

[2] Account owners who have selected either the fixed amortization or fixed annuitization method are allowed a one-time, irrevocable switch to the RMD method without incurring penalties.

[3] Under the RMD and amortization methods, you must choose a life expectancy table and you must continue taking distributions based on the life expectancy table you initially choose. There are three different life expectancy tables that may be used for calculating substantially equal periodic payments (SEPPs) under those methods.

DRD-698831-2025-03-05
BNYMR-72TSI-0425

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