

## Recent Legislation Will Affect 401(K) Hardship Distributions

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Just a few weeks ago, the federal government avoided a potentially lengthy government shutdown when Congress passed and the President signed into law the [Bipartisan Budget Act of 2018](#) (the “Act”). You may already know that the Act extends funding for the federal government until March 23, 2018. However, what you may not know is that hidden in the Act are provisions that will change some of the rules relating to hardship distributions from 401(k) plans.

### Hardship Distributions from 401(k) Plans

The Internal Revenue Code (the “Code”) and associated regulations place restrictions on participants’ ability to withdraw their elective deferrals from 401(k) plans except in certain circumstances (e.g., reaching age 59 ½; termination of employment). One such exception is that a 401(k) plan is allowed to provide for “hardship distributions.” This means that in certain circumstances (and if the plan allows), an active employee participating in a 401(k) plan can withdraw his or her elective deferrals to pay for certain expenses.

Section 401(k) of the Code and the regulations thereunder place a number of rules and restrictions on hardship distributions. For instance, the distribution must be on account of hardship, meaning that it is pursuant to an immediate and heavy financial need and is necessary to satisfy that need. Immediate and heavy financial needs include things like certain medical care expenses, the cost to purchase a principal residence, certain tuition and educational expenses, the amount necessary to avoid eviction, certain burial or funeral expenses, and certain expenses to repair damage to a principal residence.

An employee that takes a hardship distribution is generally prohibited from making elective deferrals to the plan (or any other plan maintained by the employer) for at least 6 months following the hardship distribution. Also, hardship distributions are only permitted from certain accounts. Except for certain grandfathered amounts, they cannot be taken from the participant’s income on elective deferrals, qualified nonelective contributions (“QNECs”) or qualified matching contributions (“QNECs”). Furthermore, before a hardship distribution can occur, the employee must have taken all other available distributions from the plan (and other plans maintained by the employer), such as a loan (if available).

### What Changes Does the Act Make to Hardship Distributions?

First, the Act will eliminate the 6-month suspension on elective deferrals following a hardship distribution. It requires the Secretary of Treasury to issue regulations removing the 6-month restriction on elective deferrals. The Secretary has up to one year to complete this task. Furthermore, the Act amends Section 401(k) of the Code to allow for hardship distributions to include QNECs, QMACs, and income on elective deferrals. Lastly, the Act removes the requirement to take available loans before taking hardship distributions. These changes are effective for plan years beginning after December 31, 2018.

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National Law Review, Volume VIII, Number 50

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