

Avoidance of a 10% Early Withdrawal Penalty from Retirement Plans for Taxpayers under age 59-1/2

There are certain circumstances in which the IRS will allow you to make an early withdrawal and not have to pay the appropriate penalty. If claiming an exception to an early withdrawal penalty from a retirement pension, traditional IRA or employer sponsored qualified retirement plan, click on the TaxSlayer "Other Taxes" menu to access Part 1 of Form 5329. An excerpt from Form 5329 Part 1 follows:

Part I - Additional Tax on Early Distributions

Form belongs to

Taxpayer

SIMPLE Retirement Distributions that are not subject to 25% Tax

\$

Early Distributions that are not subject to 10% tax

\$

Select the reason for exemption

-- Please Select --

A distribution code 1 on 1099R forms is used to identify early withdrawals from retirement pensions, traditional IRAs, and employer sponsored qualified retirement plans. A distribution code J is used to identify early distribution code from Roth IRAs. A distribution code S is used to identify early distribution from a SIMPLE IRA.

Withdrawals from a Roth IRA taken before age 59-1/2 and/or held less than 5 years are classified as an early distribution (or nonqualified distribution). The earnings portion of Roth IRA taken early may be subject to a 10% early-distribution penalty unless an exception applies.

Early distributions from Employer sponsored Qualified Retirement Plans (401k, & 403b) are prorated between taxable and nontaxable amounts (Designated Roth) amounts by the Employer Plan and should appear on 1099-R forms. It is possible that the amounts in Block 1 and Block 2 are different if some of the distribution is prorated from a nontaxable Designated Roth. 457b plan is a government retirement plan that is not classified as a qualified retirement plan. Distribution from a 457b plan is not subject to early distribution penalties.

A distribution code J is used to identify an early distribution from a Roth IRA. A distribution code T is used to identify an early distribution from a Roth IRA with exceptions. If the distribution code J or T is incorrect, open a Form 5329 and apply a code 12 exception to show the early distribution penalty does not apply. Distribution codes J or T are out of scope if codes are correct.

Caution: Rules for exempting early withdrawal penalties from (a) retirement pensions, (b) traditional IRAs, (c) Roth IRAs, and (d) employer sponsored qualified retirement IRA plans are different. Counselors must understand what kind of retirement plans the early distributions come from before applying an early distribution exception. TaxSlayer provides warnings when an exception may not apply. Do not ignore these warnings.

Exception codes and explanations for early distributions from IRAs or retirement plans: (Do not rely on this list alone. See Publication 590-B, Distributions from Individual Retirement Arrangements (IRAs), for rules and details pertaining to each exception.)

No.	Exception
01	Qualified retirement plan distributions (doesn't apply to IRAs) if you separated from service in or after the year you reach age 55 (age 50 for qualified public safety employees). For distributions to public safety officers after 12/29/22: <ul style="list-style-type: none"> • "age 50" (above) is replaced by "age 50 or 25 years of service under the plan, whichever is earlier" • The definition of PSO is expanded to include corrections officers, certain forensic security employees, and private sector firefighters. Note: The definition of PSO differs for this exception vs. the health insurance exclusion.
02	Distributions made as part of a series of substantially equal periodic payments (made at least annually) for your life (or life expectancy) or the joint lives (or joint life expectancies) of you and your designated beneficiary (if from an employer plan, payments must begin after separation from service).
03	Distributions due to total and permanent disability. Does not apply if the disability occurred after the distribution.
04	Distributions made on or after the date of death (doesn't apply to modified endowment contracts).
05	Qualified retirement plan distributions up to (1) the amount you paid for unreimbursed medical expenses during the year minus (2) 7.5% of your adjusted gross income for the year. Expenses can also be entered on Schedule A.
06	Qualified retirement plan distributions made to an alternate payee under a qualified domestic relations order (doesn't apply to IRAs).
07	IRA distributions made to unemployed individuals for health insurance premiums. See Code 07 on page H-6.
08	IRA distributions up to the amount you paid for qualified higher education expenses during the year, unless paid with tax-free education aid or Pell grant.
09	IRA distributions made for purchase of a first home, up to \$10,000 per taxpayer and paid within 120 days of distribution.
10	Distributions due to an IRS levy on the qualified retirement plan.
11	Qualified distributions to reservists while serving on active duty for at least 180 days.
12	Distributions incorrectly indicated as early distributions by Code 1, J, or S in Box 7 of Form 1099-R when received at age 59 1/2 or older.
13	Distributions from a Section 457 plan, which aren't from a rollover from a qualified retirement plan.
14	Distributions from a plan maintained by an employer if (1) separated from service by March 1, 1986, (2) as of March 1, 1986, your entire interest was in pay status under a written election that produces a specific schedule for the distribution of your entire interest, and (3) the distribution is actually being made under the written election.
15	Distributions that are dividends paid with respect to stock described in Section 404(k).
16	Distributions from annuity contracts to the extent that the distributions are allocable to the investment in the contract before August 14, 1982. For additional exceptions that apply to annuities, see Tax on Early Distributions under Special Additional Taxes in Pub 575.
17	Distributions that are phased retirement annuity payments made to federal employees. See Pub 721 for more information on the phased retirement program.
18	Permissible withdrawals under Section 414(w).
19	Qualified birth or adoption distributions. A statement must be attached that provides the name, age, and TIN of the child or eligible adoptee.
20*	Distributions due to terminal illness. For distributions made on or after December 30, 2022, you are considered terminally ill if you have been certified by a physician as having an illness or physical condition that can reasonably be expected to result in death in 84 months or less after the date of the certification.
21*	Corrective distributions made on or after December 29, 2022, for excess contributions distributed before the due date of the tax return.
99*	Enter this code if more than one exception applies. Add Note in TaxSlayer indicating exceptions and \$ amount of each.

* As of 2/17/23, TaxSlayer had not implemented codes 20 or 21 (and 99 was being reported as 20).