

MEMO# 4194

October 22, 1992

TEMPORARY AND PROPOSED REGULATIONS CONCERNING 20-PERCENT MANDATORY PENSION WITHHOLDING

October 22, 1992 TO: PENSION MEMBERS NO. 28-92 OPERATIONS MEMBERS NO. 39-92
TRANSFER AGENT ADVISORY COMMITTEE NO. 62-92 RE: TEMPORARY AND PROPOSED
REGULATIONS CONCERNING 20-PERCENT MANDATORY PENSION WITHHOLDING

Attached is a copy of temporary and proposed regulations under the pension provisions of the Unemployment Compensation Amendments of 1992 ("UCA"). Also attached is a copy of IRS Notice 92-48, which includes a model notice intended to satisfy section 402(f) of the Internal Revenue Code as amended by the UCA. Please note that because the President has not signed the Revenue Act of 1992 (H.R. 11), the temporary and proposed regulations do not include the provisions of the technical corrections to the UCA that were included in H.R. 11. (See Institute Memorandum to Pension Members No. 26-92, Operations Members No. 38-92 and Transfer Agent Advisory Committee No. 59-92, dated October 8, 1992.) General Rules The temporary and proposed regulations exclude the following distributions from the definition of "eligible rollover distribution:" (1) returns of section 401(k) elective deferrals returned as a result of the section 415 limits; (2) corrective distributions of excess contributions, excess deferrals, and excess aggregate contributions, along with income allocable thereto; (3) loans treated as distributions under section 72(p); (4) loans in default (other than unpaid loan balances treated as distributed upon termination of employment); and (5) similar items designated by the Commissioner. In addition, a plan need not permit direct rollovers of, or withhold upon, distributions expected to total less than \$200 for the year. The plan administrator must permit a distributee to elect to have a portion of an eligible rollover distribution directly rolled over and have the remainder paid to the distributee if the total distribution is over \$500, but need not permit such a division if the portion directly rolled over would be less than \$500. In addition, the plan administrator, is not required (but is permitted) to allow the distributee to divide an eligible - 1 - rollover distribution into separate distributions to be paid directly to more than one eligible retirement plan selected by the distributee. The plan administrator is also permitted to establish a default procedure whereby a distributee who fails to make an affirmative election is treated as having either made or not made a direct rollover election, subject to the notice requirements described below. A direct rollover may be accomplished by any reasonable means of direct payment to an eligible retirement plan. "Reasonable means" includes providing a check to the distributee for delivery to the eligible retirement plan, provided that the check is made payable as follows: "[Name of trustee] as trustee of [name of eligible retirement plan]." Unless the name of the distributee is included in the name of the eligible retirement plan, the check must also indicate that it is for the benefit of the distributee. The preamble to the

temporary regulations requests comments concerning a possible requirement that a standard notation, such as "Direct Rollover," appear on the face of any check provided to an employee for delivery. Notice Requirement The UCA provides that the notice described in section 402(f) of the Code must be provided "within a reasonable period of time before making an eligible rollover distribution." For distributions that are subject to the consent requirements under section 411(a)(11), the time frame prescribed by final regulations under the latter section will govern. Thus, under the current section 411(a)(11) regulations, the section 402(f) notice must be given no less than 30 days and no more than 90 days before the annuity starting date. For distributions not governed by section 411(a)(11), such as distributions not exceeding \$3,500, the same time period will apply, but the employee may waive the 30-day period by affirmatively electing to make or not make a direct rollover. The section 402(f) notice in the context of a section 403(b) arrangement must also be provided a reasonable time before the election, and comments are requested concerning the impact of the seven-day redemption rule of section 22(e) of the Investment Company Act of 1940 upon this requirement. Withholding and Reporting The temporary and proposed regulations clarify that direct rollover distributions must be reported on IRS Form 1099-R and direct rollover amounts received by an IRA must be reported on Form 5498. Direct rollover amounts received by qualified plans and section 403(b) arrangements are not required to be reported. Under a transition rule, a plan administrator or payor experiencing undue hardship in complying with the new withholding rules before April 1, 1993 may delay the application of the 20- - 2 - percent withholding requirement if "catch-up" withholding on - 3 - subsequent distributions prior to January 1, 1994 can be accomplished. In addition, the preamble states that any penalties for failure to withhold as required under the UCA from eligible rollover distributions before July 1, 1993, will be abated automatically if the plan administrator or payor has acted diligently and in good faith in attempting to comply. The preamble to the temporary regulations reconfirms the applicability of the three alternative methods of depositing withholding on retirement distributions under Announcement 84-40. The Institute requested such confirmation in its testimony before the IRS concerning proposed tax deposit regulations. (See Institute Memorandum to Tax Committee No. 29-92, Pension Committee No. 27-92, Operations Committee No. 21-92 and Transfer Agent Advisory Committee No. 42-92, dated August 3, 1992.) Under the Announcement, payors may: (1) aggregate withholding amounts from all designated pension distributions under its control with its payroll tax deposits; (2) request a separate Employer Identification Number ("EIN") solely for purposes of reporting the aggregated withholding from the designated pension distributions under its control; or (3) remit the tax under the EIN of each retirement plan separately. We will keep you informed of further developments. Kathy D. Ireland Associate Counsel - Pension Attachments KDI:bmb