# Special Tax Notice

(Lump Sum Distributions)

## INTRODUCTION

This is a general guide regarding the tax consequences of lump-sum distributions, such as BackDROP or refund of 2011 Tier employee contributions. You are receiving this notice because all or a portion of a payment you are receiving from the MoDOT and Patrol Employees' Retirement System (MPERS) is eligible to be rolled over to a qualified individual retirement account (IRA) or another eligible employer retirement plan/account. This notice is intended to provide you with information that may impact your decision.

MPERS operates as a tax-qualified plan under section 401(a) of the Internal Revenue Code. The information contained in this brochure applies only to MPERS-related lump-sum distributions. This brochure is for informational purposes only and is not tax advice. If you have additional questions, please contact a tax professional regarding your personal circumstances.

## Simplified Summary of Payment Options

A lump-sum payment from MPERS that is rollover eligible, may be distributed in one of the three ways listed below. The choice you make may affect individual taxes and/or penalties owed. The *Special Tax Notice* is provided as a convenience only; it is not tax advice. Please consult a tax professional before making a payment election.

**1. Rollover Option**

- The payment is made directly to a qualified IRA or employer plan.
- Income tax is not withheld from the rollover amount.

**2. Cash Option**

- The BackDROP distribution is electronically deposited into the same account authorized for monthly retirement benefit payments. If the distribution is a refund of employee contributions, it is paid by check.
- MPERS is required by law to withhold 20% of a cash distribution and send it to the IRS as a federal income tax payment.
- The cash payment may be subject to the IRS 10% additional early distribution tax (unless an exception applies). Applicable state taxes may apply but will not be withheld from the payment.

**3. Combination Cash and Rollover Option**

- This option allows you to specify how much of the payment to receive as cash and how much is rolled over to a qualified account or plan.
- The combination option has the same tax implications as mentioned in payment options one and two.


MODOT & Patrol Employees' Retirement System
1913 William Street Jefferson City, MO 65109
www.mpers.org mpers@mpers.org

# GENERAL INFORMATION ABOUT ROLLOVERS

## How can a rollover affect my taxes?

Lump-sum payments that are not rolled over to a qualifying plan will be taxed. If you are under age 59½ and do not choose a rollover payment option, you will also have to pay the 10% additional early distribution tax unless an exception applies. If you choose a rollover option, taxes may be deferred until distributions are made by the receiving plan.

## What types of retirement accounts and plans will accept my rollover?

You may roll over the lump-sum payment to an eligible individual retirement account, individual retirement annuity, or an eligible employer plan (e.g., a tax-qualified plan, section 403(b) plan, or governmental section 457(b) plan). The receiving plan will determine the investment options, fees, and rights to payment (e.g., no spousal consent rules apply to IRAs and IRAs may not provide loans). Further, the amount rolled over will become subject to the tax rules that apply to the receiving plan.

## How can I do a rollover?

There are two types of rollovers: direct rollover and 60-day rollover.

**Direct Rollover -** If a direct rollover is elected, MPERS will make the payment directly to the qualified plan. Please contact the IRA sponsor or plan administrator for information on how to complete a direct rollover.

**60-Day Rollover -** If you elect to take your MPERS distribution as cash and later change your mind, you may still complete a rollover by making a deposit into an IRA or eligible employer plan that will accept it. Generally, you will have 60 days after you receive the payment to make the deposit. If you elect not to do a direct rollover, MPERS is required to withhold 20% of the payment for federal income tax. This means that to roll over the entire payment in a 60-day rollover, you must use other funds to make up for the 20% withholding. If the entire amount of the payment is not rolled over, the portion not rolled over will be taxed and subject to the 10% additional early distribution tax if you are under age 59½ (unless an exception applies). The 20% withheld by MPERS will be applied to your tax liability for the tax year and credited or refunded as determined by the IRS.

### Individuals Over Age 72 and Required Minimum Distributions

Required minimum distributions must begin by April 1 of the year following the year you turn age 72 or retire, whichever is later. You may roll over that portion of your eligible rollover distribution that is not a required distribution (under Section 401(a)(9) of the Internal Revenue Code) into a traditional IRA or eligible employer plan. Required minimum distributions may not be rolled over and must be paid to you.

## How much may I roll over?

If you wish to do a rollover, you may roll over all or part of the amount eligible for rollover. Any payment from MPERS is eligible for rollover, except:

- Certain payments spread over a period of at least 10 years or over your life or life expectancy (or the lives or joint life expectancy of you and your beneficiary);
- Required minimum distributions after age 72 (or after death); and
- Corrective distributions of contributions that exceed tax law limitations.

## If I do not do a rollover, will I have to pay the 10% additional early distribution tax?

The IRS generally defines an early distribution or early withdrawal as the taking of funds out of a retirement plan before a person reaches age 59½.

If you are under age 59½, you will have to pay the 10% additional early distribution tax for any payment from MPERS (including amounts withheld for income tax) that you do not roll over, unless one of the exceptions listed below applies. This tax applies to the part of the distribution that you must include in income and is in addition to the regular income tax on the payment not rolled over to an eligible plan.

The 10% additional early distribution tax does not apply to the following payments from MPERS:

- Payments made after you separate from service if you will be at least age 55 in the year of the separation;
- Payments that start after you separate from service if paid at least annually in equal or close to equal amounts over your life or life expectancy (or the lives or joint life expectancy of you and your beneficiary);
- Payments from a governmental plan made after you separate from service if you are a public safety employee and you will be at least age 50 in the year of the separation;
- Payments made due to disability;
- Payments made after your death;
- Corrective distributions of contributions that exceed tax law limitations;
- Payments made directly to the government to satisfy a federal tax levy;
- Payments made to an alternate payee under a Division of Benefits Order (DBO);
- Payments up to the amount of your deductible medical expenses; and
- Certain payments made while you are on active duty if you were a member of a reserve component called to duty after September 11, 2001, for more than 179 days.

## Will I owe state income tax?

This notice does not cover any state or local income tax rules including withholding rules. You should consult a professional tax advisor and your state and/or local taxing authority about other tax liabilities before taking a lump-sum distribution.

## If I do a rollover to an eligible IRA, will the 10% additional early distribution tax apply to early distributions from the IRA?

If you receive a payment from an eligible IRA before reaching age 59½, you will have to pay the 10% additional early distribution tax on the part of the distribution that you must include in income, unless an exception applies. In general, the exceptions to the 10% additional early distribution tax from an IRA are the same as the exceptions listed on the previous page for early distributions from a retirement plan; however, there are a few differences for payments from an IRA.

The 10% additional early distribution tax does **not** apply to the following payments:

- Payments made after you separate from service if you will be at least age 55 in the year of the separation (or age 50 for qualified public safety employees).
- Payments made under a qualified domestic relations order (QDRO) (although a special rule applies under which, as part of a divorce or separation agreement, a tax-free transfer may be made directly to an IRA of a spouse or former spouse).
- Payments made at least annually in equal or close to equal amounts over a specified period applies without regard to whether or not you have had a separation from service.
- Payments for qualified higher education expenses.
- Payments up to $10,000 used in a qualified first-time home purchase.
- Payments for health insurance premiums after you have received unemployment compensation for 12 consecutive weeks (or would have been eligible to receive unemployment compensation but for self-employed status).

### State of Missouri Deferred Compensation Plan

You have the option of rolling over the lump-sum distribution into the State of Missouri Deferred Compensation Plan. You can defer taxation on the balance until you start withdrawing money from the plan (must begin at age 72), at which time you will be taxed only on the amount withdrawn. If you retire after age 55, but prior to age 59½, you can access your BackDROP funds from the State of Missouri Deferred Compensation Plan without an early withdrawal penalty.

**Phone: (800) 392-0925**
**www.modeferredcomp.org**

# SPECIAL RULES AND OPTIONS

## If you miss the 60-day rollover deadline

Generally, the 60-day rollover deadline cannot be extended. However, the IRS has limited authority to waive the deadline under certain extraordinary circumstances, such as when external events prevented you from completing the rollover by the 60-day rollover deadline.

Under certain circumstances, you may claim eligibility for a waiver of the 60-day rollover deadline by making a written self-certification. Otherwise, to apply for a waiver from the IRS, you must file a Private Letter Ruling request with the IRS. Private Letter Ruling requests require the payment of a nonrefundable user fee. For more information, see IRS Publication 590–A, Contributions to Individual Retirement Arrangements (IRAs).

## If you were born on or before January 1, 1936

If you were born on or before January 1, 1936, and receive a lump sum distribution that you do not roll over, special rules for calculating the amount of the tax on the payment might apply to you. For more information, see IRS Publication 575, Pension and Annuity Income.

## If you roll over your payment to a Roth IRA

If you roll over a payment from MPERS to a Roth IRA, a special rule applies under which the amount of the payment rolled over (reduced by any after-tax amounts) will be taxed. However, the 10% additional early distribution tax will not apply (unless you take the amount rolled over out of the Roth IRA within five years, counting from January 1 of the year of the rollover).

If you roll over the payment to a Roth IRA, later payments from the Roth IRA that are qualified distributions will not be taxed (including earnings after the rollover). A qualified distribution from a Roth IRA is a payment made after you are age 59½ (or after your death or disability, or as a qualified first-time homebuyer distribution of up to $10,000) and after you have had a Roth IRA for at least five years. In applying this five-year rule, you count from January 1 of the year for which your first contribution was made to a Roth IRA. Payments from the Roth IRA that are not qualified distributions will be taxed to the extent of earnings after the rollover, including the 10% additional early distribution tax (unless an exception applies). You do not have to take required minimum distributions from a Roth IRA during your lifetime. For more information, see IRS Publication 590–A, Contributions to Individual Retirement Arrangements (IRAs), and IRS Publication 590–B, Distributions from Individual Retirement Arrangements (IRAs).

You cannot roll over a distribution from MPERS to a designated Roth account in another employer plan.

## If you are not a participant of MPERS

**Payments after death of the participant.** If you receive a distribution that you do not roll over, the distribution will generally be taxed in the same manner described elsewhere in this notice. However, the 10% additional early distribution tax and the special rules for public safety officers do not apply, and the special rule described under the section "If you were born on or before January 1, 1936," applies only if the participant was born on or before January 1, 1936.

**If you are a surviving spouse.** If you receive a payment from MPERS as the surviving spouse of a deceased participant, you have the same rollover options that the participant would have had, as described elsewhere in this notice. In addition, if you choose to do a rollover to an eligible IRA, you may treat the IRA as your own or as an inherited IRA.

An IRA you treat as your own is treated like any other of your IRAs, so that payments made to you before you are age 59½ will be subject to the 10% additional early distribution tax (unless an exception applies) and required minimum distributions from your IRA do not have to start until after you are age 72.

If you treat the IRA as an inherited IRA, payments from the IRA will not be subject to the 10% additional early distribution tax. However, if the participant had started taking required minimum distributions, you will have to receive required minimum distributions from the inherited IRA. If the participant had not started taking required minimum distributions from MPERS, you will not have to start receiving required minimum distributions from the inherited IRA until the year the participant would have been age 72.

**If you are a surviving beneficiary other than a spouse.** If you receive a payment from the plan because of the participant's death and you are not a surviving spouse, the only rollover option you have is to do a direct rollover to an inherited IRA. Payments from the inherited IRA will not be subject to the 10% additional early distribution tax. You will have to receive required minimum distributions from the inherited IRA.

## If you are a nonresident alien

If you are a nonresident alien and you do not do a direct rollover to an eligible U.S. IRA or U.S. employer plan, instead of withholding 20%, MPERS is generally required to withhold 30% of the payment for federal income taxes. If the amount withheld exceeds the amount of tax you owe (as may happen if you do a 60-day rollover), you may request an income tax refund by filing Form 1040NR and attaching your Form 1042–S. See Form W–8BEN for claiming that you are entitled to a reduced rate of withholding under an income tax treaty. For more information, see also *IRS Publication 519, U.S. Tax Guide for Aliens* and *IRS Publication 515, Withholding of Tax on Nonresident Aliens and Foreign Entities*.

## Other special rules

If a payment is one in a series of payments for less than 10 years, your choice whether to make a direct rollover will apply to all later payments in the series (unless you make a different choice for later payments).

If your payments for the year are less than $200, MPERS is not required to allow you to do a direct rollover and is not required to withhold for federal income taxes. However, you may do a 60-day rollover.

You may have special rollover rights if you recently served in the U.S. Armed Forces. For more information, see *IRS Publication 3, Armed Forces' Tax Guide*.

# FOR MORE INFORMATION

This *Special Tax Notice* summarizes only the federal (not state or local) tax rules that might apply to your lump sum distribution. The rules are complex and contain many conditions and exceptions that may not be included in this notice.

You may wish to consult with an MPERS benefit specialist or a professional tax advisor before taking a lump-sum payment from MPERS. Also, you can find more detailed information on the federal tax treatment of payments from employer plans in the following IRS Publications:

- *IRS Publication 575, Pension and Annuity Income*
- *IRS Publication 590–A, Contributions to Individual Retirement Arrangements (IRAs)*
- *IRS Publication 590–B, Distributions from Individual Retirement Arrangements (IRAs)*
- *IRS Publication 571, Tax-Sheltered Annuity Plans (403(b) Plans)*

These publications are on the web at www.irs.gov, or by calling 1-800-TAX-FORM.

The information contained in this brochure is excerpted from information published by the IRS (*Safe Harbor Explanations - Eligible Rollover Distributions Notice 2018-74* and *Safe Harbor Explanations - Eligible Rollover Distributions Notice 2020-62*) and is being provided for informational purposes only. MPERS is **NOT** responsible for the accuracy of the information contained herein and members should consult their tax advisor regarding any planned distributions.

The contents of this brochure do not amend or overrule any applicable statute, IRS Code, or administrative rule. In the event of conflict, the applicable statute, IRS Code, or administrative rule will prevail.