

# Special Tax Notice Regarding Refunds, Lump Sum Payments, and Certain Death Benefits

## Your Rollover Options

You are receiving this notice because all or a portion of a payment you are receiving from the North Dakota Teachers' Fund for Retirement (TFFR) is eligible to be rolled over to an IRA or an employer plan. This notice is intended to help you decide whether to do such a rollover. This notice describes the rollover rules that apply to payments from TFFR.

Rules that apply to most payments from TFFR are described in the "General Information about Rollovers" section. Special rules that only apply in certain circumstances are described in the "Special Rules and Options" section.

If you have additional questions after reading this notice, call TFFR toll free at 1-800-952-2970 or (701) 328-9885. You may also want to consult with a professional tax advisor before you take a payment from TFFR.

## General Information about Rollovers

### How can a rollover affect my taxes?

You will be taxed on a payment from TFFR if you do not roll it over. If you are under age 59-1/2 and do not do a rollover, you will also have to pay a 10% additional income tax on early distributions (unless an exception applies). However, if you do a rollover, you will not have to pay tax until you receive payments later and the 10% additional income tax will not apply if those payments are made after you are age 59-1/2 (or if an exception applies).

### Where may I roll over the payment?

You may roll over the payment to either an IRA (an individual retirement account or individual retirement annuity) or an employer plan (a tax-qualified plan, section 403(b) plan, or governmental section 457(b) plan) that will accept the rollover. The rules of the IRA or employer plan that holds the rollover will determine your investment options, fees, and rights to payment from the IRA or employer plan (for example, 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 IRA or employer plan.

### How do I do a rollover?

There are two ways to do a rollover. You can do either a direct rollover or a 60-day rollover.

If you do a direct rollover, TFFR will make the payment directly to your IRA or an employer plan. You should contact the IRA sponsor or the administrator of the employer plan for information on how to do a direct rollover.

If you do not do a direct rollover, you may still do a rollover by making a deposit into an IRA or eligible employer plan that will accept it. You will have 60 days after you receive the payment to make the deposit. If you do not do a direct rollover, TFFR is required to withhold 20% of the taxable amount of the payment for federal income taxes. This means that, in order to roll over the entire payment in a 60-day rollover, you must use other funds to make up for the 20% withheld. If you do not roll over the entire amount of the payment, the portion not rolled over will be taxed and will be subject to the 10% additional income tax on early distributions if you are under age 59-1/2 (unless an exception applies).

### How much may I roll over?

You may rollover all or a part of the amount eligible for rollover. Payments from TFFR made over your lifetime, or over the joint lifetime of you and your beneficiary, or over a period of ten or more years may not be rolled over. All other TFFR payments are eligible for rollover, including the lump-sum portion of a partial lump-sum distribution (PLSO), and a refund of your total accumulated contributions and interest. However, you may not roll over any portion of your payment considered a minimum required distribution paid after age 70 ½ (or after death). TFFR can tell you what portion of a payment is eligible for rollover.

**If I don't do a rollover, will I have to pay the 10% additional income tax on early distributions? See IRS Form 5329 for more information on the additional 10% tax.**

If you are under age 59-1/2, you will pay the 10% additional income tax on early distributions for any payment from TFFR (including amounts withheld for income tax) that are not rolled over, unless an exception listed below applies. This tax is in addition to the regular income tax on the payment not rolled over.

The 10% additional income tax does not apply to the following payments from TFFR:

- 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 made due to disability
- Payments after your death
- Payments made directly to the government to satisfy a federal tax levy
- Payments made under a qualified domestic relations order (QDRO)
- Payments up to the amount of your deductible medical expenses
- 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.

**If I rollover to an IRA, will the 10% additional income tax apply to early distributions from the IRA?**

If you receive a payment from an IRA when you are under age 59-1/2, you will have to pay the 10% additional income tax on early distributions from the IRA, unless an exception applies. In general, the exceptions to the 10% additional income tax for early distributions from an IRA are the same as the exceptions listed above for early distributions from TFFR. However, there are a few differences for payments from an IRA, including:

- There is no exception for payments after separation from service that are made after age 55.
- The exception for qualified domestic relations orders (QDROs) does not apply (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).
- The exception for payments made at least annually in equal or close to equal amounts over a specified period applies without regard to whether you have had a separation from service.
- There are additional exceptions for (1) payments for qualified higher education expenses, (2) payments up to \$10,000 used in a qualified first-time home purchase, and (3) 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).

**Will I owe state income taxes?**

If you are a North Dakota resident, your payment is subject to state taxes at the time of distribution, unless you elect to roll it over. You have the option to have North Dakota state tax withheld from the payment. This notice does not describe local income tax rules or the rules for other states.

### **Special Rules And Options**

**If your payment includes after-tax contributions**

After-tax contributions included in a payment are not taxed. If a payment is only part of your benefit, an allocable portion of your after-tax contributions is generally included in the payment, so you cannot take a payment of only after-tax contributions. You can elect to rollover after-tax contributions to an IRA or another employer plan that will accept the contributions. If you are rolling over after-tax contributions to a Qualified Employer Plan, TFFR will require a letter of acceptance from the employer plan receiving the rollover. **The letter of acceptance must indicate that they will accept the after-tax portion of the rollover.** You may also want to request information from the employer plan regarding how the record-keeping for the funds will be handled once the funds are deposited.

For Rollovers to an IRA: You may roll over to an IRA a payment that includes after-tax contributions through either a direct rollover or a 60-day rollover. You must keep track of the aggregate amount of the after-tax contributions in all of your IRAs (in order to determine your taxable income for later payments from the IRAs). If you do a direct rollover or a 60-day rollover to an IRA of only a portion of the payment made to you, the after-tax contributions are treated as rolled over last. For example, assume you are receiving a complete distribution of your benefit which totals \$12,000, of which \$2,000 is after-tax contributions. In this case, if you roll over \$10,000 to an IRA that is not a Roth IRA, no amount is taxable because the \$2,000 amount not rolled over is treated as being after-tax contributions.

For Rollovers to a Qualified Employer Plan: You may roll over to an employer plan all of a payment that includes after-tax contributions, but only through a direct rollover (and only if the receiving plan separately accounts for after-tax contributions and is not a governmental section 457(b) plan). You can do a 60-day rollover to an employer plan of part of a payment that includes after-tax contributions, but only up to the amount of the payment that would be taxable if not rolled over.

### **If you miss the 60-day rollover deadline**

Generally, the 60-day rollover deadline cannot be extended. However, the IRS has the 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. To apply for a waiver, 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 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**

You can roll over a payment from TFFR to a Roth IRA. If you roll over the payment 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 income tax on early distributions will not apply (unless you take the amount rolled over out of the Roth IRA within 5 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 59-1/2 (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 5 years. In applying this 5-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 income tax on early distributions (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 payment from TFFR to a designated Roth account in an employer plan.

### **If you are not a plan member and receive a lump sum payment as a surviving spouse, alternate payee, or other beneficiary**

If you receive a distribution after the member's death 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 income tax on early distributions does not apply, and the special rule described under the section "If you were born on or before January 1, 1936" applies only if the member was born on or before January 1, 1936.

**If you are a surviving spouse-** If you receive a payment from TFFR as the surviving spouse of a deceased member, you have the same rollover options that the member would have had, as described elsewhere in this notice. In addition, if you choose to do a rollover to an 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 IRA of yours. Payments made to you before age 59-1/2 will be subject to the 10% additional income tax on early distributions (unless an exception applies) and required minimum distributions from your IRA do not have to start until after you are age 70-1/2.

If you treat the IRA as an inherited IRA, payments from the IRA will not be subject to the 10% additional income tax on early distributions. However, if the member had been taking required minimum distributions, you will have to receive required minimum distributions from the inherited IRA. If the member had not started taking required minimum distributions from TFFR, you will not have to start receiving required minimum distributions from the inherited IRA until the year the member would have been age 70-1/2.

**If you are a surviving beneficiary other than a spouse-** If you receive a payment from TFFR because of the member's death and you are a designated beneficiary other than 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 income tax on early distributions. You will have to receive required minimum distributions from the inherited IRA.

Payments to an Alternate Payee under an approved domestic relations order. If you are the spouse or former spouse of the member who receives a payment from TFFR under a qualified domestic relations order (QDRO), you generally have the same options the member would have (for example, you may roll over the payment to your own IRA or an eligible employer plan that will accept it). Payments under the QDRO will not be subject to the 10% additional income tax on early distributions.

#### **If you are a nonresident alien**

If you are a nonresident alien and you do not do a direct rollover to a U.S. IRA or U.S. employer plan, instead of withholding 20%, TFFR 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 your payments for the year are less than \$200, TFFR 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**

You may wish to consult with TFFR or a professional tax advisor before taking a payment from TFFR. You can find more detailed information on the federal tax treatment of payments from employer plans in: 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)* and IRS Publication 571, *Tax-Sheltered Annuity Plans (403(b) Plans)*. These publications are available from a local IRS office, on the web at [www.irs.gov](http://www.irs.gov), or by calling 1-800-TAX-FORM.