

## SPECIAL INFORMATION

The (following) is a copy of a Notice (To Those Eligible To Receive a Lump Sum Distribution From The Defined Contribution Plan Of The Retirement System) which is required by the Internal Revenue Code and Regulations. This information is not given as tax advice. It is given as tax information for you to share with your tax advisor. The notice was prepared by the Retirement System's legal advisor in conformity with the Internal Revenue Code and Regulations.

**DEFINED CONTRIBUTION PLAN**

Retirement System Federal I.D. No. 38-2465279

Qualified Defined Contribution Plan IRS Letter March 5, 1987

The Defined Contribution Plan is a "Qualified Plan" and is subject to applicable provisions of the Internal Revenue Code.

**NOTICE TO RECIPIENT OF TOTAL OR PARTIAL LUMP SUM DISTRIBUTION**

Due to the complexity of the tax laws and other considerations, the Board of Trustees does not involve itself with the providing of tax advice. This notice is provided to you in accordance with Internal Revenue Regulation 1.402(f)-1T and Internal Revenue Code Section 402.

Your lump sum distribution includes approximately \$ \_\_\_\_\_ which has not been previously included in your taxable income. This distribution represents a (total) (partial) withdrawal of amounts held in your defined contribution plan (annuity savings funds amounts).

THE BOARD OF TRUSTEES MAKES NO REPRESENTATION OR GIVES NO ASSURANCE WITH RESPECT TO WHAT MAY OR MAY NOT BE PERMISSIBLE UNDER THE TAX LAW. CONSULT YOUR TAX ADVISOR.

**SPECIAL TAX RULES**

The Internal Revenue Code provides several complex rules relating to the taxation of the amounts you received in this distribution. This notice merely summarizes certain rules. You should promptly consult a tax advisor in deciding what course to follow with respect to any distribution from the Defined Contribution Plan of the Retirement System.

**TEXT OF THE SAFE HARBOR EXPLANATION SPECIAL TAX NOTICE REGARDING PLAN PAYMENTS**

This notice contains important information you will need before you decide how to receive your benefits from the Retirement System (the "Plan").

**SUMMARY**

The portion of the payment from the defined contribution plan that is not taxable is not eligible for rollover. The portion of the payment from the Plan that is taxable and

that is eligible for "rollover" can be taken in two ways. You can have *all or any portion* of the part of your payment that is taxable either 1) PAID IN A "DIRECT ROLLOVER" (sometimes called a DIRECT TRANSFER), or 2) PAID TO YOU. A rollover is a payment of your Plan benefits to your individual retirement arrangement (IRA) or to another employer plan. This choice will affect the tax you owe.

**If you choose a DIRECT ROLLOVER/DIRECT TRANSFER of the taxable portion of your withdrawal distribution from your defined contribution plan:**

- Your payment will not be taxed in the current year and no income tax will be withheld.
- Your payment will be made directly to your IRA or, if you choose, to another employer plan that accepts your rollover.

- Your payment will be taxed later when you take it out of the IRA or the employer plan.

**If you choose to have your Plan benefits PAID TO YOU**

- You will receive only 80% of the taxable portion of the payment, because the Plan administrator is required to withhold 20% of the taxable portion of the payment and send it to the IRS as income tax withholding to be credited against your taxes.
- Your payment of the taxable portion of your distribution will be taxed in the current year unless you roll it over. You may be able to use special tax rules that could reduce the tax you owe. However, if you receive the payment before age 59½, you also may have to pay an additional 10% tax. If you receive the payment and are at least age fifty-five (55) AND you terminate employment with the governmental employer, you may not be subject to the additional 10% tax.

- You can roll the taxable portion over by paying it to your IRA or to another employer plan that accepts your rollover within 60 days of receiving the payment. The amount rolled over will not be taxed until you take it out of the IRA or employer plan.
- If you want to roll over 100% of the taxable portion of the payment to an IRA or an employer plan, *you must find other money to replace the 20% that was withheld.* If you roll over only the 80% that you received, you will be taxed on the 20% that was withheld and that is not rolled over.

**I. PAYMENTS THAT CAN AND CANNOT BE ROLLED OVER**

Payments from the Plan may be “eligible rollover distributions.” This means that they can be rolled over to an IRA or to another employer plan that accepts rollovers. Your Plan administrator should be able to tell you what portion of your

payment is an eligible rollover distribution. The following types of payments cannot be rolled over.

**NON-TAXABLE PAYMENTS.**

In general, only the “taxable portion” of your payment is an eligible rollover distribution. If you have made “after-tax” employee contributions to the Plan, these contributions will be non-taxable when they are paid to you, and they cannot be rolled over (After-tax employee contributions generally are contributions you made from your own pay that were already taxed).

**PAYMENTS SPREAD OVER**

**LONG PERIODS.** You cannot roll over a payment if it is part of a series of equal (or almost equal) payments that are made at least once a year and that will last for:

- your lifetime (or your life expectancy), or
- your lifetime and your beneficiary’s lifetime (or life expectancies), or
- a period of ten years or more.

**REQUIRED MINIMUM**

**PAYMENTS.** Beginning in the year you reach age 70½, a certain portion of your payment cannot be rolled over because it is a required “minimum payment” that must be paid to you.

**II. DIRECT ROLLOVER**

You can chose a direct rollover of all or any portion of your payment that is an “eligible rollover distribution,” as described above. In a direct rollover, the eligible rollover distribution is paid directly from the Plan to an IRA or another employer plan that accepts rollovers. If you choose a direct rollover, you are not taxed on a payment until you later take it out of the IRA or the employer plan.

**DIRECT ROLLOVER TO AN**

**IRA.** You can open an IRA to receive the direct rollover. (The term “IRA,” as used in this notice, includes individual retirement accounts and individual retirement annuities.) If you choose to have your payment made directly to an

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IRA, contact an IRA sponsor (usually a financial institution) to find out how to have your payment made in a direct rollover to an IRA at that institution. If you are unsure of how to invest your money, you can temporarily establish an IRA to receive the payment. However, in choosing an IRA, you may wish to consider whether the IRA you choose will allow you to move all or part of your payment to another IRA at a later date, without penalties or other limitations. See IRS Publication 590, *Individual Retirement Arrangements*, for more information on IRAs (including limits on how often you can roll over between IRAs).

**DIRECT ROLLOVER TO A PLAN.** If you are employed by a new employer that has a plan, and you want a direct rollover to that plan, ask the administrator of that plan whether it will accept your rollover. If your new employer's plan does not accept a rollover, you can choose a direct rollover to an IRA.

**DIRECT ROLLOVER OF A SERIES OF PAYMENTS.** If you receive eligible rollover distributions that are paid in a series for less than ten years, your choice to make or not to make a direct rollover for a payment will apply to all later payments in the series until you change your election. You are free to change your election for any later payment in the series.

### III. PAYMENT PAID TO YOU

If you have the payment made to you, the taxable portion is subject to 20% income tax withholding. The payment is taxed in the year you receive it unless, within 60 days, you roll it over to an IRA or another plan that accepts rollovers. If you do not roll it over, special tax rules may apply.

#### INCOME TAX WITHHOLDING:

**MANDATORY WITHHOLDING.** If any portion of the payment to you is an eligible rollover distribution (i.e. taxable), the Plan is required by law to withhold 20% of that amount.

This amount is sent to the IRS as income tax withholding. For example, if your eligible rollover distribution is \$10,000 only \$8,000 will be paid to you because the Plan must withhold \$2,000 as income tax. However, when you prepare your income tax return for the year, you will report the full \$10,000 as a payment from the Plan. You will report the \$2,000 as tax withheld, and it will be credited against any income tax you owe for the year.

**SIXTY-DAY ROLLOVER OPTION.** If you have an eligible rollover distribution paid to you, you can still decide to roll over all or part of it to an IRA or another employer plan that accepts rollovers. If you decide to roll over, *you must make the rollover within 60 days after you receive the payment.* The portion of your payment that is rolled over will not be taxed until you take it out of the IRA or the employer plan.

You can roll over up to 100% of the eligible rollover distribution, including an amount equal

to the 20% that was withheld. If you choose to roll over 100%, you must find other money within the 60-day period to contribute to the IRA or the employer plan to replace the 20% that was withheld. On the other hand, if you roll over only the 80% that you received, you will be taxed on the 20% that was withheld.

**EXAMPLE:** Your eligible rollover distribution is \$10,000, and you choose to have it paid to you. You will receive \$8,000, and \$2,000 will be sent to the IRS as income tax withholding. Within 60 days after receiving the \$8,000, you may roll over the entire \$10,000 to an IRA or employer plan. To do this, you roll over the \$8,000 you received from the Plan, and you will have to find \$2,000 from other sources (your savings, a loan, etc.). In this case, the entire \$10,000 is not taxed until you take it out of the IRA or employer plan. If you roll over the entire \$10,000, when you file your income tax return you may get a refund of the \$2,000 withheld.

If, on the other hand, you roll over only \$8,000, the \$2,000 you did not roll over is taxed in the year it was withheld. When you file your income tax return you may get a refund of part of the \$2,000 withheld. (However, any refund is likely to be larger if you roll over the entire \$10,000).

**ADDITIONAL 10% TAX IF YOU ARE UNDER AGE 59½.**

If you receive a payment before you reach age 59½ and you do not roll it over, then, in addition to the regular income tax, you may have to pay an extra tax equal to 10% of the taxable portion of the payment. The additional 10% tax does not apply to your payment if it is (1) paid to you because you separate from service with your employer during or after the year you reach age 55, (2) paid because you retire due to disability, (3) paid to you as equal (or almost equal) payments over your life or life expectancy (or your and your beneficiary's lives or life expectancies), or (4) used to pay certain medical

expenses. See IRS Form 5329 for more information on the additional 10% tax.

**SPECIAL TAX TREATMENT.**

If your eligible rollover distribution is not rolled over, it will be taxed in the year you receive it. However, if it qualifies as a "lump sum distribution," it may be eligible for special tax treatment. A lump sum distribution is a payment, within one year, of your entire balance under the Plan (and certain other similar plans of the employer) that is payable to you because you have reached age 59½ or have separated from service with your employer (or, in the case of a self-employed individual, because you have reached age 59½ or have become disabled). For a payment to qualify as a lump sum distribution, you must have been a participant in the Plan for at least 5 years. The special tax treatment for lump sum distributions is described below.

**TAX TREATMENT OF PARTIAL DISTRIBUTION.** A partial withdrawal of Defined Contribution Plan amounts generally may be subject to a special rule whereby the distribution is taxable up to the amount of interest earnings. However, an exception to the general rule may be applicable with respect to recovering pre August 14, 1982 (post-tax) contributions without taxable consequence. If you qualify under said exception, only amounts in excess of your pre August 14, 1982 (post-tax) contribution would be taxable (up to the amount of interest credited to your defined contribution plan amounts). Accordingly, you may be subject to tax on partial distributions and a Form 1099-R will be filed by the Retirement System with the Internal Revenue Service.

**EXCLUSIONARY RATIO RULE.** Employees who do not withdraw their contributions to the

Defined Contributions Plan (Annuity), but, instead chose to receive a monthly annuity together with their payments from the Defined Benefit Plan will have the taxable portion of their annuity payment computed in accordance with the Internal Revenue Code.

**FIVE-YEAR AVERAGING.**

If you receive a lump sum distribution after you are age 59½, you may be able to make a one-time election to figure the tax on the payment by using "5-year averaging." Five-year averaging often reduces the tax you owe because it treats the payment much as if it were paid over 5 years. The "Small Business Job Protection Act of 1996 (SBJPA)" repeals the Five-Year Averaging option for tax years beginning after December 31, 1999.

**TEN-YEAR AVERAGING IF YOU WERE BORN BEFORE JANUARY 1, 1936.**

If you receive a lump sum distribution and you were born before January 1, 1936, you can make a one-time election to figure

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the tax on the payment by using “10-year averaging” (using 1986 tax rates) instead of 5-year averaging (using current tax rates). Like the 5-year averaging rules, 10-year averaging often reduces the tax you owe.

**CAPITAL GAIN TREATMENT IF YOU WERE BORN BEFORE JANUARY 1, 1936.** In addition, if you receive a lump sum distribution and you were born before January 1, 1936, you may elect to have the part of your payment that is attributable to your pre-1974 participation in the Plan (if any) taxed as long-term capital gain at a rate of 20%.

There are other limits on the special tax treatment for lump sum distributions. For example you can generally elect this special tax treatment only once in your lifetime, and the election applies to all lump sum distributions that you receive in that same year. If you have previously rolled over a payment from the Plan (or certain other similar plans of

the employer) you cannot use this special tax treatment for later payments from the IRA. Also, if you roll over only a portion of your payment to an IRA, this special tax treatment is not available for the rest of the payment. Additional restrictions are described in IRS Form 4972, which has more information on lump sum distributions and how you elect the special tax treatment.

#### **IV. SURVIVING SPOUSES, ALTERNATIVE PAYEES AND OTHER BENEFICIARIES**

In general, the rules summarized above that apply to payments to employees also apply to payments to surviving spouses of employees and to spouses or former spouses who are “alternate payees.” You are an alternate payee if your interest in the Plan results from a “qualified domestic relations order,” which is an order issued by the court, usually in connection with a divorce or legal separation. Some of the rules summarized

above also apply to a deceased employee’s beneficiary who is not a spouse. However, there are some exceptions for payments to surviving spouses, alternate payees, and other beneficiaries that should be mentioned.

If you are a surviving spouse, you may choose to have an eligible rollover distribution paid in direct rollover to an IRA or paid to you. If you have the payment paid to you, you can keep it or roll it over yourself to an IRA but you cannot roll it over to an employer plan. If you are an alternate payee, you have the same choices as the employee. Thus, you can have the payment paid as a direct rollover or paid to you. If you have it paid to you, you can keep it or roll it over yourself to an IRA or to another employer plan that accepts rollovers. If you are a beneficiary other than the surviving spouse, you cannot choose a direct rollover, and you *cannot* roll over the payment yourself.

If you are a surviving spouse, an alternate payee, or another beneficiary, your payment is not subject to the additional 10% tax described in section III above, even if you are younger than age 59½.

If you are a surviving spouse, an alternate payee, or another beneficiary, you may be able to use the special tax treatment for lump sum distributions. If you receive a payment because of the employee’s death, you may be able to treat the payment as a lump sum distribution if the employee met the appropriate age requirements, whether or not the employee had 5 years of participation in the Plan.

#### **HOW TO OBTAIN ADDITIONAL INFORMATION**

This notice summarizes only the federal (not state or local) tax rules that might apply to your payment. The rules described above are complex and contain many conditions and exceptions that are not

included in this notice. Therefore, you may want to consult with a professional tax advisor *before* you take a payment of your benefits from the Plan. Also, you can find more specific information on the tax treatment of payments from qualified retirement plans in IRS Publication 573, *Pension and Annuity Income*, and IRS Publication 590, *Individual Retirement Arrangements*. These publications are available from your local IRS office or by calling 1-800-TAX-FORMS.

**CONSULT YOUR TAX ADVISOR**

You should consult your tax advisor with respect to your individual tax matters. You should consult your tax advisor regarding any special tax advantages which may be available for you or any special tax rules applicable to you. Benefits payable upon a participant's death or payable pursuant to a domestic relations order may be eligible for special tax treatment.

**OTHER SPECIAL RULES**

If you have made voluntary after-tax nondeductible contributions to the Plan, you should consult a tax advisor as special tax advantages may be available for you to use.

**IRS REPORTING**

In addition to information the Retirement System will report to the IRS on Form 1099R with respect to the taxable portion of your plan distribution, you may also be required to file certain forms if you elect special tax treatment of your distribution. For example, IRS Form 4972 is used if special 5 or 10-year averaging is used. You should consult your tax advisor in this regard.

*The Board Of Trustees makes no representation or gives no assurance with respect to what may or may not be permissible under the tax law. Consult your tax advisor. This notice is intended to provide general information regarding the various tax issues for you to consider regarding (total or partial) lump sum distributions. Because of the complexity of distributions from any type of retirement plan, you should seek the advice of a tax advisor to help you determine if you are eligible for special tax treatment and to determine the tax consequences regarding your withdrawal of the Defined Contribution Plan amounts.*