

Notice of Proposed Rulemaking

Special Rules Under Section 417(a)(7) for Written Explanations Provided by Qualified Retirement Plans After Annuity Starting Dates

REG-109481-99

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the special rule added by the Small Business Job Protection Act of 1996 which permits the required written explanations of certain annuity benefits to be provided by qualified retirement plans to plan participants after the annuity starting date. These regulations affect administrators of, participants in, and beneficiaries of qualified retirement plans.

DATES: Written and electronic comments and requests for a public hearing must be received by April 17, 2001.

ADDRESSES: Send submissions to: CC:M&SP:RU (REG-109481-99), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 5 p.m. to: CC:M&SP:RU (REG-109481-99), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington D.C. Alternatively, taxpayers may submit comments electronically via the Internet by selecting the "Tax Regs" option on the IRS Home Page, or by submitting comments directly to the IRS Internet site at http://www.irs.gov/tax_regs/regslst.html.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations,

Robert M. Walsh, (202) 622-6090; concerning submissions and delivery of comments, Sonya Cruse (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in this notice of proposed rulemaking has been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collection of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, W:CAR:MP:FP:S:O, Washington, DC 20224. Comments on the collection of information should be received by March 19, 2001. Comments are specifically requested concerning:

Whether the proposed collection of information is necessary for the proper performance of the functions of the IRS, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collection of information (see below);

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collection of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

The collection of information in this proposed regulation is in §1.417(e)-1(b)(3)(iv)(B) and §1.417(e)-1(b)(3)(v)(A). This collection of information is required by the IRS to ensure that the participant and the participant's spouse consent to a form of distribution from a qualified retirement plan that may result in reduced periodic payments. This information will be used by the plan administrator to verify that the required

consent has been given. The collection of information is required to obtain a benefit. The respondents are individuals who are entitled to receive certain types of distributions from a qualified retirement plan or who are married to individuals entitled to receive certain types of distributions from a qualified retirement plan.

Taxpayers provide the information to administrators of qualified retirement plans when a distribution with a retroactive annuity starting date is elected.

Estimated total annual reporting burden: 12,500 hours.

Estimated average annual burden hours per respondent: 0.25 hours.

Estimated number of respondents: 50,000.

The estimated annual frequency of responses is on occasion.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

This document contains proposed amendments to 26 CFR Part 1 under section 417(a)(7) of the Internal Revenue Code (Code). Section 401(a)(11) provides that, subject to certain exceptions, all distributions from a qualified plan must be made in the form of a qualified joint and survivor annuity (QJSA). One such exception is provided in section 417, which allows a participant to elect to waive the QJSA in favor of another form of distribution. Section 417(a)(2) provides that, for the waiver to be valid, the participant's spouse must consent to the waiver. Section 417(a)(3)(A) requires a qualified plan to provide to each participant, within a reasonable period of time before the annuity starting date, a written explanation (QJSA explanation) that describes the QJSA, the right to waive the QJSA and the rights of the participant's spouse. Under section 417(d), a participant's spouse who has not been married to the participant throughout the 1-year period preceding the annuity

starting date is not required to be treated as the spouse for purposes of entitlement to the QJSA. Section 417(a)(2)(B) provides that spousal consent is not required to waive the QJSA if it is established to the satisfaction of a plan representative that such consent may not be obtained because there is no spouse, because the spouse cannot be located, or because of such other circumstances as the Secretary may by regulations prescribe.

Section 417(a)(7), which was added to the Code by section 1451(a) of the Small Business Job Protection Act of 1996, Public Law 104-188 (110 Stat. 1755) (SBJPA), creates an exception to the rules of section 417(a)(3)(A), effective for plan years beginning after December 31, 1996. Section 417(a)(7)(A) provides that, notwithstanding any other provision of section 417(a), a plan may furnish the QJSA explanation after the annuity starting date, as long as the applicable election period is extended for at least 30 days after the date on which the explanation is furnished. Thus, section 417(a)(7)(A) allows the annuity starting date to be a date that is earlier than the date the QJSA explanation is provided, thereby allowing the retroactive payment of benefits that are attributable to the period before the QJSA explanation is provided. Section 417(a)(7)(A)(ii) provides that the Secretary may limit the application of the provision permitting the selection of a retroactive annuity starting date by regulations, except that the regulations may not limit the period of time by which the annuity starting date precedes the furnishing of the written explanation other than by providing that the retroactive annuity starting date may not be earlier than termination of employment.

Section 205(c)(8) of the Employee Retirement Income Security Act of 1974, Public Law 93-406 (88 Stat. 829) (ERISA), provides a parallel rule to section 417(a)(7) of the Code that applies under Title I of ERISA, and authorizes the Secretary of the Treasury to issue regulations limiting the application of the general rule. Thus, Treasury regulations issued under section 417(a)(7) of the Code apply as well for purposes of section 205(c)(8) of ERISA.

On December 18, 1998, final regulations were published in the **Federal Register** (63 FR 70009) which amended §1.417(e)-1(b)(3)(ii) of the Income Tax Regulations, relating to the timing for the QJSA explanation and the participant waiver of a QJSA

form of distribution. The regulations finalized an earlier set of proposed regulations that were issued in 1995. The regulations specified that the QJSA explanation must be provided before the annuity starting date, except as otherwise provided by section 417(a)(7) for plan years beginning after December 31, 1996, but the regulations did not further address section 417(a)(7).

Explanation of Provisions

In accordance with section 417(a)(7)(A), these proposed regulations would provide that the QJSA explanation may be furnished on or after the annuity starting date under certain circumstances. The proposed regulations refer to the annuity starting date in such cases as the “retroactive annuity starting date”, define how payments are made in the case of a retroactive annuity starting date, and set conditions for the use of retroactive annuity starting dates.

Under the proposed regulations, a retroactive annuity starting date could be used only if the plan provides for it and the participant elects to use the retroactive annuity starting date. The election under the proposed regulations would place the participant in approximately the same situation he or she would have been in had benefit payments actually commenced on the retroactive annuity starting date. Accordingly, the proposed regulations would provide that future periodic payments for a participant who elects a retroactive annuity starting date must be the same as the periodic payments that would have been paid to the participant had payments actually commenced on the retroactive annuity starting date and that the participant must also receive a make-up amount to reflect the missed payments (with an appropriate adjustment for interest from the date the payments would have been made to the date of actual payment).

In addition, because the purpose of a retroactive annuity starting date is to place the participant in approximately the same situation that he or she would have been in had benefits commenced on the retroactive date, the retroactive benefit payments would be required to be based upon the terms of the plan in effect as of the retroactive annuity starting date (taking into account plan amendments executed after the retroactive annuity starting date, but made effective on or before that date). Accord-

ingly, the retroactive annuity starting date could not be earlier than the date the participant could have started receiving benefits if the payments had commenced at the earliest date permitted under the terms of the plan (e.g., the retroactive annuity starting date could not be before the earlier of the date of the participant’s termination of employment or attainment of normal retirement age), and the amount of the benefit must satisfy sections 415 and 417 as of the retroactive annuity starting date.

These proposed regulations would not require plans to provide for a retroactive annuity starting date. Instead, plans could continue to provide that the QJSA explanation is to be provided before the annuity starting date under the rules of section 417(a) without regard to section 417(a)(7)(A). Moreover, if a plan is amended to provide for a retroactive annuity starting date, the plan could impose additional restrictions on availability not imposed under these proposed regulations, provided that the additional restrictions did not violate any of the rules applicable to qualified plans. For example, plans that generally provide benefit options that include annuities and lump sum payments could provide that retroactive annuity starting dates are available only for participants who elect annuities.

These proposed regulations make it clear that the notice, consent, and election rules of section 417(a)(1), (2), and (3), and the regulations thereunder, would apply to the retroactive payment of benefits but with several modifications. These modifications generally reflect the fact that the existing timing rules relating to notice and consent are generally tied to an annuity starting date that is after the furnishing of the QJSA explanation.¹

Section 417(a)(7)(A) specifically permits the QJSA explanation to be made after the annuity starting date and modi-

¹ For example, section 417(a)(1) provides that a participant may elect to waive the QJSA within the “applicable election period” which is defined by section 417(a)(6) as the 90-day period ending on the annuity starting date. Similarly, §1.417(e)-1(b)(3)(i) provides that the written consent of the plan participant and the participant’s spouse must be made no more than 90 days before the annuity starting date. Also, §1.417(e)-1(b)(3)(ii) provides that the QJSA explanation must generally be provided no less than 30 days and no more than 90 days before the annuity starting date.

fies the participant election period in these situations. These regulations would make a comparable adjustment for the timing rules applicable to spousal consent by providing generally that, for retroactive payments under section 417(a)(7), the first date of actual payment is substituted for the annuity starting date in applying the timing rules for notice and consent. These modifications are intended to ensure that the notice and election are generally contemporaneous with the commencement of benefits, but the modifications recognize the need for flexibility in the timing to take into account administrative delays. In furtherance of that goal, these proposed regulations would modify the general timing rule applicable to the furnishing of notices, and to participant elections and spousal consent. The proposed regulations would provide that the participant's election to waive the QJSA under section 417(a)(1)(A)(i) and the spouse's consent under section 417(a)(2) must generally be made before the annuity starting date, but permits a later election if the distribution commences no more than 90 days after the QJSA explanation required by section 417(a)(3)(A) is furnished to the participant. This modification would apply without regard to the retroactivity of annuity starting dates, but would include an exception for reasonable administrative delay in the distribution of benefits.

Pursuant to the regulatory authority provided in section 417(a)(7)(A)(ii), these proposed regulations include a special spousal consent rule in addition to those rules applicable under section 417(a). Under this special rule, if the spouse's survivor annuity under a QJSA with an annuity starting date after the date the QJSA explanation was provided would be greater than the spouse's survivor annuity pursuant to the participant's election of a retroactive annuity starting date, the participant could not elect a retroactive annuity starting date unless the participant's spouse (determined at the time distributions actually commence) consents to the distribution. This special rule applies even if the form of benefit that the participant elects as of the retroactive annuity starting date is a QJSA. Thus, for example, where a QJSA that begins after the QJSA explanation is furnished would provide \$1,000 monthly to the participant

with a survivor annuity of \$500 monthly to the spouse, and a QJSA with a retroactive annuity starting date would provide \$900 monthly to the participant with a survivor annuity of \$450 monthly to the spouse, together with a \$20,000 make-up payment to the participant, the spouse would be required to consent in order for the participant to elect the retroactive annuity starting date. Spousal consent under this special rule would not be required in this example if the spouse's survivor annuity under the retroactive annuity starting date election is at least \$500 per month.

These proposed regulations would also provide that, pursuant to section 417(a)(2)(B), the consent of the participant's spouse as of the retroactive annuity starting date would not be required if that spouse is not the participant's spouse as of the date distributions commence, unless otherwise provided in a qualified domestic relations order (as defined in section 414(p)).

The proposed regulations would impose an additional condition on the availability of a retroactive annuity starting date, regarding the permissible amount of the distribution under sections 417(e)(3) (if applicable) and 415. To satisfy this condition, the distribution would be required to be adjusted, if necessary, to satisfy the requirements of sections 417(e)(3) (if applicable) and 415 if the date the distribution commences is substituted for the annuity starting date.

Proposed Effective Date

These regulations are proposed to be applicable for plan years beginning on or after January 1, 2002.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that the regulations require the collection of plan participants' written elections requesting qualified retirement plan distributions, and written spousal consent to

these distributions, under limited circumstances. It is anticipated that most small businesses affected by these regulations will be sponsors of qualified retirement plans. Since these written participant elections and written spousal consents are required to be collected only for certain distributions, and since, in the case of a small plan, there will be relatively few distributions per year (and even fewer that are subject to these requirements), small plans that provide distributions for which this collection of information is required will only have to collect a small number of participant elections and spousal consents as a result of these regulations. Accordingly, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and 8 copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. A public hearing may be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of these regulations are Robert M. Walsh and Linda S. F. Marshall, Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and Treasury participated in their development.

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Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1 — INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read, in part, as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 1.417(e)–1 is amended by:

1. Revising paragraph (b)(3)(i).
2. Revising paragraph (b)(3)(ii) introductory text.
3. Revising paragraph (b)(3)(ii)(C).
4. Redesignating paragraphs (b)(3)(iii) and (b)(3)(iv) as paragraphs (b)(3)(viii) and (b)(3)(ix), respectively.
5. Adding new paragraphs (b)(3)(iii) through (b)(3)(vii).

The additions and revisions read as follows:

§1.417(e)–1 Restrictions and valuations of distributions from plans subject to sections 401(a)(11) and 417.

* * * * *

(b)* * *

(3)* * *

(i) Written consent of the participant and the participant's spouse to the distribution must be made not more than 90 days before the annuity starting date, and, except as otherwise provided in paragraphs (b)(3)(iii) and (b)(3)(iv) of this section, no later than the annuity starting date.

(ii) A plan must provide participants with the written explanation of the QJSA required by section 417(a)(3) no less than 30 days and no more than 90 days before the annuity starting date, except as provided in paragraph (b)(3)(iv) of this section regarding retroactive annuity starting dates. However, if the participant, after having received the written explanation of the QJSA, affirmatively elects a form of distribution and the spouse consents to that form of distribution (if necessary), a plan will not fail to satisfy the requirements of section 417(a) merely because the written explanation was provided to the participant less than 30 days before the annuity starting date, provided that the following conditions are met:

* * * * *

(C) The annuity starting date is after the date that the explanation of the QJSA is provided to the participant.

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(iii) The plan may permit the annuity starting date to be before the date that any

affirmative distribution election is made by the participant (and before the date that distribution is permitted to commence under paragraph (b)(3)(ii)(D) of this section), provided that, except as otherwise provided in paragraph (b)(3)(vii) of this section regarding administrative delay, distributions commence not more than 90 days after the explanation of the QJSA is provided.

(iv) *Retroactive annuity starting dates.* (A) Notwithstanding the requirements of paragraphs (b)(3)(i) and (ii) of this section, pursuant to section 417(a)(7), a defined benefit plan is permitted to provide benefits based on a retroactive annuity starting date if the requirements described in paragraph (b)(3)(v) of this section are satisfied. A defined benefit plan is not required to provide for retroactive annuity starting dates. If a plan does provide for a retroactive annuity starting date, it may impose conditions on the availability of a retroactive annuity starting date in addition to those imposed by paragraph (b)(3)(v) of this section, provided that imposition of those additional conditions does not violate any of the rules applicable to qualified plans. For example, a plan that includes a single sum payment as a benefit option may limit the election of a retroactive annuity starting date to those participants who do not elect the single sum payment. A defined contribution plan is not permitted to have a retroactive annuity starting date.

(B) For purposes of this section, a "retroactive annuity starting date" is an annuity starting date affirmatively elected by a participant that occurs on or before the date the written explanation required by section 417(a)(3) is provided to the participant. In order for a plan to treat a participant as having elected a retroactive annuity starting date, future periodic payments with respect to a participant who elects a retroactive annuity starting date must be the same as the future periodic payments, if any, that would have been paid with respect to the participant had payments actually commenced on the retroactive annuity starting date. The participant must receive a make-up payment to reflect any missed payment or payments for the period from the retroactive annuity starting date to the date of the actual make-up payment (with an appropriate adjustment for interest from the date

the missed payment or payments would have been made to the date of the actual make-up payment). Thus, the benefit determined as of the retroactive annuity starting date must satisfy the requirements of sections 417(e)(3), if applicable, and section 415 with the applicable interest rate and applicable mortality table determined as of that date. Similarly, a participant is not permitted to elect a retroactive annuity starting date that precedes the date upon which the participant could have otherwise started receiving benefits (e.g., the earlier of the participant's termination of employment or the participant's normal retirement age) under the terms of the plan in effect as of the retroactive annuity starting date. A plan does not fail to treat a participant as having elected a retroactive annuity starting date as described in this paragraph (b)(3)(iv)(B) merely because the distributions are adjusted to the extent necessary to satisfy the requirements of paragraph (b)(3)(v)(B) of this section relating to sections 415 and 417(e)(3).

(C) If the participant's spouse as of the retroactive annuity starting date would not be the participant's spouse determined as if the date distributions commence were the participant's annuity starting date, consent of that former spouse is not needed to waive the QJSA with respect to the retroactive annuity starting date, unless otherwise provided under a qualified domestic relations order (as defined in section 414(p)).

(D) A distribution payable pursuant to a retroactive annuity starting date election is treated as excepted from the present value requirements of paragraph (d) of this section under paragraph (d)(6) of this section if the distribution form would have been described in paragraph (d)(6) of this section had the distribution actually commenced on the retroactive annuity starting date.

(v) *Requirements applicable to retroactive annuity starting dates.* A distribution is permitted to have a retroactive annuity starting date with respect to a participant's benefit only if the following requirements are met:

(A) The participant's spouse (including an alternate payee who is treated as the spouse under a qualified domestic relations order (QDRO), as defined in section 414(p)), determined as if the date distrib-

utions commence were the participant's annuity starting date, consents to the distribution in a manner that would satisfy the requirements of section 417(a)(2). The spousal consent requirement of this paragraph (b)(3)(v)(A) is satisfied if such spouse consents to the distribution under paragraph (b)(2)(i) of this section. The spousal consent requirement of this paragraph (b)(3)(v)(A) does not apply if the amount of such spouse's survivor annuity payments under the retroactive annuity starting date election is no less than the amount that the payments to such spouse would have been under a QJSA with an annuity starting date after the date that the explanation was provided.

(B) The distribution (including appropriate interest adjustments) provided based on the retroactive annuity starting date would satisfy the requirements of section 417(e)(3), if applicable, and section 415 if the date the distribution commences is substituted for the annuity starting date for all purposes, including for purposes of determining the applicable interest rate and the applicable mortality table.

(vi) *Timing of notice and consent requirements in the case of retroactive annuity starting dates.* In the case of a retroactive annuity starting date, the date of the first actual payment of benefits based on the retroactive annuity starting date is substituted for the annuity starting date for purposes of satisfying the timing requirements for giving consent and providing an explanation of the QJSA provided in paragraphs (b)(3)(i) and (ii) of this section, except that the substitution does not apply for purposes of paragraph (b)(3)(iii) of this section. Thus, the written explanation required by section 417(a)(3)(A) must generally be provided no less than 30 days and no more than 90 days before the date of the first payment of benefits and the election to receive the distribution must be made after the written explanation is provided and on or before the date of the first payment. Similarly, the written explanation may also be provided less than 30 days prior to the first payment of benefits if the requirements of paragraph (b)(3)(ii) of this section would be satisfied if the date of the first payment is substituted for the annuity starting date.

(vii) *Administrative delay.* A plan will not fail to satisfy the 90-day timing re-

quirements of paragraphs (b)(3)(iii) and (vi) of this section merely because, due solely to administrative delay, a distribution commences more than 90 days after the written explanation of the QJSA is provided to the participant.

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Robert E. Wenzel,
*Deputy Commissioner
of Internal Revenue.*

(Filed by the Office of the Federal Register on January 16, 2001, 8:45 a.m., and published in the issue of the Federal Register for January 17, 2001, 66 F.R. 3916)
