

## Part IV. Items of General Interest

### Notice of Proposed Rulemaking

#### Relief From Disqualification for Plans Accepting Rollovers

REG-245562-96

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Proposed regulations.

SUMMARY: This document contains proposed regulations that would provide guidance on the qualification of retirement plans that accept rollover contributions from employees. These regulations affect plan administrators of qualified plans that accept rollover contributions.

DATES: Written comments must be received by December 18, 1996.

ADDRESSES: Send submissions to CC:DOM:CORP:R (REG-245562-96), room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to CC:DOM:CORP:R (REG-245562-96), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, DC. 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.ustreas.gov/prod/tax\\_regs/comments.html](http://www.irs.ustreas.gov/prod/tax_regs/comments.html)

FOR FURTHER INFORMATION CONTACT: Marjorie Hoffman, (202) 622-6030 (not a toll-free number).

#### SUPPLEMENTARY INFORMATION:

##### *Background*

On September 22, 1995, Final Income Tax Regulations (TD 8619 [1995-2 C.B. 41]) under sections 401(a)(31) and 402(c) were published in the **Federal Register** (60 FR 49199). The final regulations provide guidance for complying with the Unemployment Compensation Amendments of 1992 (UCA).

UCA expanded the types of distributions from a qualified plan that are eligible to be rolled over to an individual retirement account or individual retirement annuity, or to another qualified plan that accepts rollovers (collectively referred to as eligible retirement

plans). Such distributions are referred to as eligible rollover distributions. UCA also added a new qualification provision under section 401(a)(31) that requires qualified plans to provide employees with a direct rollover option. Under a direct rollover option, an employee may elect to have an eligible rollover distribution paid directly to an eligible retirement plan. The direct rollover option is provided in addition to the pre-existing rollover provisions under section 402. Thus, an employee who receives an eligible rollover distribution but who does not elect a direct rollover still has the option to roll over the distribution to an eligible retirement plan within 60 days of receipt.

The final regulations under section 401(a)(31) provide that a plan that accepts a direct rollover from another plan will not fail to satisfy section 401(a) or 403(a) merely because the plan making the distribution is, in fact, not qualified under section 401(a) or 403(a) at the time of the distribution, if, prior to accepting the rollover, the receiving plan reasonably concluded that the distributing plan was qualified under section 401(a) or 403(a). The regulations provide, as an example, that the receiving plan may reasonably conclude that the distributing plan was qualified under section 401(a) or 403(a) if, prior to accepting the rollover, the plan administrator of the distributing plan provided the receiving plan with a statement that the distributing plan had received a determination letter from the Commissioner indicating that the plan was qualified. The plan administrator is not required to verify this information, such as by obtaining a copy of the distributing plan's plan document or determination letter, in order to reasonably conclude that the distributing plan is qualified under section 401(a) or 403(a).

##### *Explanation of Provisions*

###### 1. Overview

The relief to be provided in these proposed regulations is intended to increase the portability of qualified plan benefits when an employee changes jobs. This objective would be achieved by reassuring a plan sponsor that acceptance of an amount as a rollover contribution, in appropriate circumstances, will not affect the plan's qualification under section 401(a) or 403(a).

###### 2. Expansion of existing relief for receiving plans

These proposed regulations would expand and clarify in several respects the relief provided in the regulations under section 401(a)(31) issued last year. First, the proposed regulations would clarify and expand the relief from disqualification currently provided for plans that accept direct rollovers. The protection would be expanded to be available not only if the plan administrator reasonably concludes the distributing plan is qualified under section 401(a) or 403(a) (even if later it is determined that the distributing plan is not a qualified plan), but also if the plan administrator reasonably concludes that a distribution meets the other requirements to be an eligible rollover distribution (but later it is determined that this conclusion was incorrect). Further, the proposed regulation would clarify that if the plan administrator reaches these conclusions reasonably, and satisfies the corrective distribution requirement described below, the contribution will be treated as a rollover contribution for purposes of applying qualification requirements under section 401(a) or 403(a) to the plan. Thus, if the contribution was not, in fact, a distribution from a qualified plan or for any other reason fails to be an eligible rollover distribution within the meaning of section 402(c), the contribution nevertheless would be treated as a rollover contribution as opposed to, for example, an employee contribution for purposes of section 401(m) or for purposes of section 415.

Second, the regulations would extend this expanded relief from disqualification to plans that accept rollover contributions other than direct rollover contributions. Thus, the relief would apply to plans that accept rollover contributions made by an employee within 60 days of the date of the distribution from a plan. Further, the relief would apply to plans that accept rollover contributions from a "conduit IRAs," i.e., an individual retirement plan that does not contain any amount attributable to any source other than a rollover contribution (as defined in section 402) from a plan qualified under section 401(a) or an annuity qualified under section 403(a). The relief would apply if (a) when accepting a rollover contribution, the plan administrator of the receiving plan reasonably concludes that the contribution is an

eligible rollover distribution from a qualified plan (or an amount distributed from a conduit IRA) and that the contribution satisfies the other applicable requirements of section 402(c) or 408(d)-(3) for treatment as a rollover contribution and (b) the receiving plan satisfies the corrective distribution requirement described below.

The regulations would provide examples of the actions that a plan administrator might take to reasonably conclude that an employee's contribution satisfies the requirements for treatment as a rollover contribution. The examples are intended to be merely illustrative. Plan administrators may develop other approaches or procedures for reasonably reaching this conclusion.

Finally, the regulations would provide that if the receiving plan later obtains actual knowledge or otherwise determines that the distributing plan was not qualified at the time of the distribution, that any portion of the distribution was not an eligible rollover distribution or an amount distributed from a conduit IRA, or that the contribution to the plan otherwise did not satisfy the applicable requirements of section 402 or 408 for treatment as a rollover contribution, a corrective distribution equal to the amount of the contribution plus any earnings attributable to the contribution would be required to be made to the employee within a reasonable time after such determination.

### Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue 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, consider-

ation will be given to any written comments (a signed original and eight (8) copies) or comments transmitted via Internet that are submitted timely to the IRS. All comments will be available for public inspection and copying.

A public hearing may be scheduled if requested in writing by a person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the hearing will be published in the **Federal Register**.

### Drafting Information

The principal author of these regulations is Marjorie Hoffman, Office of the Associate Chief Counsel (Employee Benefits and Exempt Organizations), IRS. However, other personnel from the IRS and Treasury Department participated in their development.

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### Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is 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 1.401(a)(31)-1 is amended as follows:

1. Under the heading "List of Questions," redesignating Q-14 through Q-18 as Q-15 through Q-19, respectively, and adding new Q-14.

2. Under the heading "Question and Answers," removing designation (a) and the paragraph heading, and removing paragraph (b) from A-13.

3. Under the heading "Question and Answers," redesignating Q&A-14 through Q&A-18 as Q&A-15 through Q&A-19, respectively, and adding Q&A-14.

The additions read as follows:

*§ 1.401(a)(31)-1 Requirement to offer direct rollover of eligible rollover distributions; questions and answers.*

\* \* \* \* \*

#### LIST OF QUESTIONS

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Q-14: If a plan accepts an invalid rollover contribution, whether or not as a direct rollover, how will the contribution be treated for purposes of applying

the qualification requirements of section 401(a) or 403(a) to the plan?

\* \* \* \* \*

#### QUESTIONS AND ANSWERS

\* \* \* \* \*

Q-14: If a plan accepts an invalid rollover contribution, whether or not as a direct rollover, how will the contribution be treated for purposes of applying the qualification requirements of section 401(a) or 403(a) to the plan?

A-14: (a) *Acceptance of invalid rollover contribution.* If a plan accepts an invalid rollover contribution, the contribution will be treated, for purposes of applying the qualification requirements of section 401(a) or 403(a) to the receiving plan, as if it were a valid rollover contribution, if the following two conditions are satisfied. First, when accepting the amount from the employee as a rollover contribution, the plan administrator of the receiving plan reasonably concludes that the contribution is a valid rollover contribution. Second, if the plan administrator of the receiving plan later determines that the contribution was an invalid rollover contribution, the amount of the invalid rollover contribution, plus any earnings attributable thereto, is distributed to the employee within a reasonable time after such determination.

(b) *Definitions.* For purposes of this Q&A-14:

(1) An invalid rollover contribution is an amount that is accepted by a plan as a rollover within the meaning of Q&A-1 of § 1.402(c)-2 (or as a rollover contribution within the meaning of section 408(d)(3)(A)(ii)) but that is not an eligible rollover distribution from a qualified plan (or an amount described in section 408(d)(3)(A)(ii)) or that does not satisfy the other requirements of section 401(a)(31), 402(c), or 408(d)(3) for treatment as a rollover or a rollover contribution.

(2) A valid rollover contribution is a contribution that is accepted by a plan as a rollover within the meaning of Q&A-1 of § 1.402(c)-2 or as a rollover contribution within the meaning of section 408(d)(3) and that satisfies the requirements of section 401(a)(31), 402(c), or 408(d)(3) for treatment as a rollover or a rollover contribution.

(c) The provisions of paragraph (a) of this Q&A-14 are illustrated by the following examples:

*Example 1.* (a) Employer X maintains for its employees Plan M, a profit sharing plan qualified under section 401(a). Plan M provides that any

employee of Employer X may make a rollover contribution to Plan M. Employee A is an employee of Employer X, will not have attained age 70 1/2 by the end of the year, and has a vested account balance in Plan O (a plan maintained by Employer A's prior employer). Employee A elects a single sum distribution from Plan O and elects that it be paid to Plan M in a direct rollover.

(b) Employee A provides the plan administrator of Plan M with a letter from the plan administrator of Plan O stating that Plan O has received a determination letter from the Commissioner indicating that Plan O is qualified.

(c) Based upon such a letter, absent facts to the contrary, a plan administrator may reasonably conclude that Plan O is qualified and that the amount paid as a direct rollover is an eligible rollover distribution.

*Example 2.* (a) Same facts as *Example 1*, except that Employee A elects to receive the distribution from Plan O and wishes to make a rollover contribution described in section 402 rather than a direct rollover.

(b) When making the rollover contribution, Employee A certifies that, to the best of Employee A's knowledge, Employee A is entitled to the distribution as an employee and not as a beneficiary, the distribution from Plan O to be contributed to Plan M is not one of a series of periodic payments, the distribution from Plan O was received by Employee A not more than 60 days before the date of the rollover contribution, and the entire amount of the rollover contribution would be includible in gross income if it were not being rolled over.

(c) As support for these certifications, Employee A provides the plan administrator of Plan M with two statements from Plan O. The first is a letter from the plan administrator of Plan O, as described in *Example 1*, stating that Plan O has received a determination letter from the Commissioner indicating that Plan O is qualified. The second is the distribution statement that accompanied the distribution check. The distribution statement indicates that the distribution is being made by Plan O to Employee A, indicates the gross amount of the distribution, and indicates the amount withheld as Federal income tax. The amount withheld as Federal income tax is 20 percent of the gross amount of the distribution. Employee A contributes to Plan M an amount not greater than the gross amount of the distribution stated in the letter from Plan O and the contribution is made within 60 days of the date of the distribution statement from Plan O.

(d) Based on the certifications and documentation provided by Employee A, absent facts to the contrary, a plan administrator may reasonably conclude that Plan O is qualified and that the distribution otherwise satisfies the requirements of section 402(c) for treatment as a rollover contribution.

*Example 3.* (a) The facts are the same as in *Example 2*, except that, rather than contributing the distribution from Plan O to Plan M, Employee A contributes the distribution from Plan O to IRA P, an individual retirement account described in section 408(a). After the contribution of the distribution from Plan O to IRA P, but before the year in which Employee A attains age 70 1/2, Employee A requests a distribution from IRA P and decides to contribute it to Plan M as a rollover contribution. To make the rollover contribution, Employee A endorses the check received from IRA P as payable to Plan M.

(b) In addition to providing the certifications described in *Example 2* with respect to the distribution from Plan O, Employee A certifies that, to the best of Employee A's knowledge, the

contribution to IRA P was made not more than 60 days after the date Employee A received the distribution from Plan O, no amount other than the distribution from Plan O has been contributed to IRA P, and the distribution from IRA P was received not more than 60 days earlier than the rollover contribution to Plan M.

(c) As support for these certifications, in addition to the two statements from Plan O described in *Example 2*, Employee A provides copies of statements from IRA P. The statements indicate that the account is identified as an IRA, the account was established within 60 days of the date of the letter from Plan O informing Employee A that an amount had been distributed, and the opening balance in the IRA does not exceed the amount of the distribution described in the letter from Plan O. There is no indication in the statements that any additional contributions have been made to IRA P since the account was opened. The date on the check from IRA P is less than 60 days before the date that Employee A makes the contribution to Plan M.

(d) Based on the certifications and documentation provided by Employee A, absent facts to the contrary, a plan administrator may reasonably conclude that Plan O is qualified and that the contribution by Employee A is a rollover contribution described in section 408(d)(3)(A)(ii) that satisfies the other requirements of section 408(d)(3) for treatment as a rollover contribution.

Par. 3. Section 1.402(c)-2 is amended by adding a sentence to the end of A-11 to read as follows:

*§ 1.402(c)-2 Eligible rollover distributions; questions and answers.*

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A-11. \* \* \* See § 1.401(a)(31)-1, Q&A-14, for guidance concerning the qualification of a plan that accepts a rollover contribution.

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Michael P. Dolan,  
*Acting Commissioner of Internal Revenue.*

(Filed by the Office of the Federal Register on September 18, 1996, 8:45 a.m., and published in the issue of the Federal Register for September 19, 1996, 61 F.R. 49279)