



*Exceeding customer expectations  
by providing outstanding benefit services  
through professional plan administration  
and sound investment practices.*



## Special Tax Notice





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## INTRODUCTION

This notice is provided by the Missouri State Employees' Retirement System (MOSERS) because all or part of the payment you will soon receive may be eligible for rollover by you or MOSERS to a traditional individual retirement account (traditional IRA) or an eligible employer plan. A rollover is a payment by you or MOSERS of all or part of your benefit to another plan or IRA that allows you to continue to postpone taxation of that benefit until it is paid to you.

The term "traditional IRA," as used in this notice, includes:

- 408(a) individual retirement accounts.
- 408(b) individual retirement annuities.

Your payment cannot be rolled over to a SIMPLE IRA, or Coverdell Education Savings Account (formerly known as an education IRA).

An "eligible employer plan" includes:

- A plan qualified under section 401(a) of the Internal Revenue Code (Code), including a 401(k) plan, profit-sharing plan, defined benefit plan, stock bonus plan, money purchase plan, and the Missouri State Employees' Deferred Compensation Incentive Plan.
- A section 403(a) annuity plan.
- A section 403(b) tax-sheltered annuity.
- An eligible section 457(b) plan maintained by a governmental employer (governmental deferred compensation 457 plan).

An eligible employer plan is not legally required to accept a rollover. Before you decide to roll over your payment to another employer plan, you should find out whether the plan accepts rollovers and, if so, the types of distributions it accepts as a rollover. You should also find out about any documents that are required to be completed before the receiving plan will accept a rollover. Even if a plan accepts rollovers, it might not accept rollovers of certain types of distributions, such as after-tax amounts. If this is the case, and your distribution includes after-tax amounts, you may wish instead to roll your distribution over to a traditional IRA or split your rollover amount between the employer plan in which you will participate and a traditional IRA. If an employer plan accepts your rollover, the plan may restrict subsequent distributions of the rollover amount or may require your spouse's consent for any subsequent distribution. A subsequent distribution from the plan that accepts your rollover may also be subject to different tax treatment than distributions from MOSERS. Check with the administrator of the plan that is to receive your rollover prior to making the rollover.

## PAYMENT OPTIONS

A payment from MOSERS that is eligible for rollover may be taken one of three ways. The choice you make will affect the taxes and/or penalties you owe.

### (1) Direct Rollover Option

Certain payments can be made directly to a traditional IRA that you establish or to an eligible employer plan that will accept it and hold it for your benefit. If you elect the direct rollover option:

- Your payment will **not** be taxed in the year of the rollover and no income tax will be withheld.
- You choose whether your payment will be made directly to your traditional IRA or to an eligible employer plan that accepts your rollover. Your payment **cannot** be rolled over to a SIMPLE IRA, or Coverdell Education Savings Account because these are not traditional IRAs.
- The taxable portion of your payment will be taxed when you take it out of the traditional IRA or the eligible employer plan. Depending on the type of plan, the later distribution may be subject to different tax treatment than it would be if you received a taxable distribution from MOSERS.

Not all eligible employer plans accept rollovers, and some plans only accept rollovers of certain types of funds. Even if a plan accepts rollovers, the plan probably will require you to complete certain paperwork before the rollover can be made. Check with the plan administrator of the receiving plan before you request a rollover.

## (2) Cash Option

By electing the cash option, MOSERS will mail the payment directly to you. If you elect the cash option:

- You will receive only 80% of the taxable portion of the payment. MOSERS is required to withhold 20% of the taxable portion of the payment and send it to the IRS as federal income tax withholding to be credited against your taxes. Applicable state taxes may also apply.
- The taxable portion of your payment will be taxed in the year of distribution unless you later roll it over. Under certain circumstances, 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 may have to pay an additional 10% premature distribution tax.\*
- You can roll over all or part of the payment by paying it to your traditional IRA or another eligible employer plan that will accept your rollover within 60 days after you receive the payment. The taxable amount rolled over will not be taxed until you take it out of the traditional IRA or the eligible employer plan. This is often referred to as an indirect rollover.
- MOSERS is required to withhold 20% of the taxable portion of your distribution for federal taxes. If you want to roll over 100% of the taxable payment to a traditional IRA or another eligible employer plan, you must find other money to replace the 20% withheld. If you roll over only the 80% you received, you will be taxed on the 20% that was withheld and not rolled over. In addition, the 10% premature distribution tax may apply if you are under age 59½\*.

\* see page 14 for exceptions

### (3) Combination Cash and Rollover Option

If you choose the combination cash and rollover option:

- You may specify the amount of your distribution to be made directly to a traditional IRA or an eligible employer plan.
- The balance will be paid directly to you (less the required 20% income tax withholding on the taxable portion of the distribution).
- Your cash payment may be subject to the 10% premature distribution tax if you are under age 59½.

For a detailed explanation of your options, please review the **Direct Rollover** and **Cash Option** sections of this brochure.

### **DIRECT ROLLOVER**

You may choose a direct rollover of all or any portion of your payment that is an eligible rollover distribution. In a direct rollover, the eligible rollover distribution is paid directly from MOSERS to a traditional IRA or an eligible employer plan that will accept rollovers. If you choose a direct rollover, you will not be taxed on any taxable portion of your payment until you later take it out of the traditional IRA or the eligible employer plan. In addition, no income tax withholding is required for any portion of your payment for which you choose a direct rollover.

For more information on what types of distributions qualify as eligible rollover distributions, please see the section of this brochure titled **Payments That Can and Cannot be Rolled Over**.

## Direct Rollover to a Traditional IRA

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

## Direct Rollover to a Plan

If your new employer has an eligible employer plan and you want to make a direct rollover to that plan, ask the administrator of that plan whether it will accept your rollover. An eligible employer plan is not legally required to accept a rollover and may choose to accept only certain types of funds as rollovers. If your new employer's plan will not accept a rollover, you can choose a direct rollover to a traditional IRA. If your new employer's plan accepts your rollover, the plan may provide restrictions on the circumstances under which you may later receive a distribution of the rollover amount or may require spousal consent to any subsequent distribution. Check with the plan administrator before making your decision.

Any payments rolled over to a 457 plan retain their original distribution characteristics.

## **PAYMENTS THAT CAN AND CANNOT BE ROLLED OVER**

Payments from MOSERS may be “eligible rollover distributions.” This means that they can be rolled over to a traditional IRA or another eligible employer plan that accepts rollovers. Payments from MOSERS cannot be rolled over to a SIMPLE IRA, or a Coverdell Education Savings Account. MOSERS will be able to tell you what portion of your payment is an eligible rollover distribution.

### **Payments That Can Be Rolled Over**

- **Pre-Tax Contributions.** These contributions may be rolled to a traditional IRA or an eligible employer plan (if they accept rollovers) as defined on page 2 of this brochure.
- **After-Tax Contributions.** After-tax contributions are made from your own pay that has already been taxed (such as money used from your taxable investments to purchase service credit). If you made after-tax contributions to MOSERS, these contributions may be rolled into either a traditional IRA or to certain retirement plans that accept rollovers of after-tax contributions. The following rules apply:
  - **After-Tax Contributions Rolled Into a Traditional IRA.** You may roll over your after-tax contributions either directly or indirectly (see previous section on payment options). Once you roll your after-tax contributions into a traditional IRA, those amounts cannot be rolled into an employer plan. You should keep track of the after-tax contributions rolled to a traditional IRA on IRS Form 8606, the same form used to track non-deductible traditional IRA contributions. This will facilitate determination of the nontaxable amount of any future distributions from the traditional IRA.

- **After-Tax Contributions Rolled Into an Employer Plan.** You may roll over after-tax contributions to an employer plan that is qualified under Code section 401(a) and is a defined contribution plan. A defined benefit plan under Code section 401(a) is not eligible to receive after-tax contributions through a rollover. You may not roll after-tax contributions to a 403(b) plan (unless it is from one 403(b) plan to another) or a 457 plan. If you want to roll over your after-tax contributions to an employer plan that accepts these rollovers, you cannot have the after-tax contributions paid to you first. You must instruct MOSERS to make a direct rollover on your behalf. Also you cannot first roll over after-tax contributions to a traditional IRA and then roll that amount into an employer plan.

Not all plans will accept rollovers of after-tax contributions. Check with the plan administrator of the receiving plan to make sure after-tax contributions will be accepted.

## Payments That Cannot Be Rolled Over

- **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: (1) your lifetime (or a period measured by your life expectancy), (2) your lifetime and your beneficiary's lifetime (or a period measured by your joint life expectancies), or (3) a period of ten years or more.
- **Required Minimum Payments.** Beginning on April 1 of the year after the year in which you turn age 70½ or retire (whichever is later), a certain portion of your payment generally cannot be rolled over because it is a "required minimum distribution" that must be paid to you.

MOSERS will be able to tell if your payment includes amounts that cannot be rolled over.

## Change in Tax Treatment Resulting From a Direct Rollover

The tax treatment of any payment from the eligible employer plan or traditional IRA receiving your direct rollover might be different than if you received your benefit in a taxable distribution directly from MOSERS. For example, if you were born before January 1, 1936, you might be entitled to ten-year averaging or capital gain treatment, as explained in this brochure. However, if you have your benefit rolled over to a section 403(b) tax-sheltered annuity, a governmental 457 plan, or a traditional IRA in a direct rollover, your benefit will no longer be eligible for that special treatment.

## CASH OPTION

If you have the payment made to you, it is subject to 20% federal income tax withholding on the taxable portion (state tax may also apply). The payment is taxed in the year it is paid unless you roll it over within 60 days to a traditional IRA or an eligible employer plan that accepts rollovers. If you do not roll it over, special tax rules may apply.

### INCOME TAX WITHHOLDING IF ELECTING THE CASH OPTION

#### Mandatory Income Tax Withholding

MOSERS is required by law to withhold 20% of the taxable payment made to you. This amount is sent to the IRS as federal income tax withholding. For example, if you can roll over a taxable payment of \$10,000, only \$8,000 will be paid to you, because MOSERS must withhold \$2,000 as income tax. However, when you prepare your income tax return for the year (unless you make a rollover within 60 days), you must report the full \$10,000 as a taxable payment from MOSERS. You must report the \$2,000 as tax withheld, and it will be credited against any income tax you owe for the year. There will be no income tax withholding if your payments for the year are less than \$200.

#### Voluntary Income Tax Withholding

If any portion of your payment is taxable but is not eligible for rollover as described under the section titled **Payments That Can and Cannot Be Rolled Over**, the mandatory withholding rules described above do not apply. In this case, you may elect not to have withholding apply to that portion of your payment (however, you will still need to pay the tax when you file your tax return). If you do nothing, 10% will be taken out of this portion of your payment for federal income tax withholding. To elect out of withholding, ask a MOSERS benefit counselor for an election form and related information.

## 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 a traditional IRA or another eligible employer plan that accepts rollovers. If you decide to roll the distribution over, you must contribute the amount of the payment you receive to a traditional IRA or another eligible employer plan 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 traditional IRA or the eligible 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 traditional IRA or the eligible employer plan to replace the 20% that was withheld. On the other hand, if you roll over only the 80% you received, you will be taxed on the 20% that was withheld.

Keep in mind that any after-tax payments made to you are not eligible for a rollover to an eligible employer plan. In order to roll after-tax contributions to an eligible employer plan (excluding 457 and 403(b) plans), a direct rollover must be made. Please see the section titled **Payments That Can and Cannot Be Rolled Over** for further details.

## Example

Your eligible rollover distribution is \$10,000 and is entirely taxable. You choose to have it paid to you (cash option). You will receive \$8,000, and \$2,000 will be sent to the IRS as federal income tax withholding. Within 60 days after receiving the \$8,000, you may roll over the entire \$10,000 to a traditional IRA or an eligible employer plan. To do this, you roll over the \$8,000 you received from MOSERS, 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 traditional IRA or an eligible employer plan. If you roll over the entire \$10,000, you may get a refund of part or all of the \$2,000 withheld when you file your income tax return.

On the other hand, if 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, you may have to pay an extra tax equal to 10% of the taxable portion of the payment in addition to the regular income tax.

The additional 10% tax does not apply to:

- Payments that are paid after you separate from service with your employer during or after the year you reach age 55 (age 50 for qualified public safety employees\*).
- Payments that are paid because you retire due to disability.
- Payments that are paid as equal (or almost equal) payments over your life or life expectancy (or your beneficiaries' lives or life expectancies).
- Payments that are paid directly to the government to satisfy a federal tax levy.
- Payments that do not exceed the amount of your deductible medical expenses.
- Payments that are paid to an alternate payee under a division of benefits order (DBO).

For more information on the additional 10% tax, see IRS Form 5329.

If you roll over an eligible plan distribution to an eligible 457 plan, that amount (adjusted for investment returns) will remain subject to the pre-59½ tax when it is distributed from the eligible 457 plan unless one of the exceptions noted above applies.

\* **Qualified Public Safety Employee** - any uniformed state employee who provides police protection, fire fighting services, or emergency medical services for any area within the jurisdiction of Missouri (effective 8/17/06).

## **THE MISSOURI DEFERRED COMPENSATION PLAN (457 PLAN)**

Because the Missouri Deferred Compensation Plan is an eligible 457 plan, your distributions from the 457 plan are generally not subject to the 10% penalty regardless of your age at the time of the distribution. If you roll your 457 plan distributions into another employer plan that is not an eligible 457 plan or into a traditional IRA, any subsequent distributions may be subject to the penalty, unless one of the exceptions noted earlier applies. Moreover, if your distribution includes amounts that were previously rolled over from another employer plan that was not an eligible 457 plan, those amounts remain subject to the penalty unless one of the exceptions apply.

### **SPECIAL TAX TREATMENT ON CERTAIN DISTRIBUTIONS**

If you receive a payment from a 401(a) or a 403(a) plan that can be rolled over and you do not roll it over to a traditional IRA or another eligible employer plan that will accept it, the payment will be taxed in the year you receive it. However, if the payment 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 after you have reached age 59½ or because you have separated from service with your employer.

For a payment to be treated as a lump sum distribution, you must have been a participant in the plan for at least five years before the year in which you received the distribution. The following describes the special tax treatment for lump sum distributions that may be available to you.

## 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 the tax on the payment by using “ten-year averaging” (using 1986 tax rates). Ten-year averaging sometimes reduces the tax you owe.

## Capital Gain Treatment

### if You Were Born Before January 1, 1936

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 MOSERS (if any) taxed as a long-term capital gain at a rate of 20%.

Capital gain and averaging treatment will not be available for any distributions from a qualified plan to which an IRA rollover contribution has been made under the EGTRRA provisions.

In order to qualify for this special tax treatment, a conduit IRA must be established. A conduit IRA is an IRA account that is newly established and only includes your MOSERS distribution. In this situation, you cannot commingle the MOSERS distribution with amounts in an existing IRA.

## Limits on the Special Tax Treatment of Lump Sum Distributions

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 you receive in that same year. If you have previously rolled over a distribution from MOSERS, you cannot use this special averaging treatment for later payments from MOSERS. If you roll over your payment to a traditional IRA, governmental 457 plan, or 403(b) tax-sheltered annuity, you will not be able to use this special tax treatment for later payments from that IRA or annuity. Also, if you roll over only a portion of your payment to a traditional IRA, governmental 457 plan, or 403(b) tax-sheltered annuity, this special tax treatment is not available for the rest of the payment. See IRS Form 4972 for additional information on lump sum distributions and how you elect the special tax treatment.

### **INDIVIDUALS OVER AGE 70½**

You may roll 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 to traditional IRAs or eligible employer plans. Required distributions must begin by April 1 of the year following the year you turn age 70½ or retire, whichever is later.

## **SURVIVING SPOUSES, ALTERNATE PAYEES, AND OTHER BENEFICIARIES**

In general, the rules that apply to payments to employees also apply to payments to surviving spouses of employees and to spouses or former spouses (alternate payees). You are an alternate payee if your interest in MOSERS results from a Division of Benefits Order (DBO), which is an order issued by a court in connection with a divorce. Some of the rules 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.

### **Surviving Spouse or Alternate Payee Payment**

If you are a surviving spouse or alternate payee, you have the same choices as the employee. You may have an eligible rollover distribution paid as a direct rollover or paid to you. If you have the payment paid to you, you can keep it (assuming any tax consequences) or roll it over yourself to a traditional IRA or another eligible employer plan, if that plan accepts rollovers.

### **Payment to Other Beneficiaries**

Effective January 1, 2007, the payment to a non-spouse beneficiary can be rolled over directly to an IRA established for the beneficiary to receive the distribution. The IRA must identify the decedent and the beneficiary (i.e. "Tim Smith as beneficiary of Tom Smith").

The IRA is subject to the distribution rules that apply to inherited IRAs.

## Exemption From 10% Early Distribution Penalty

If you are a surviving spouse, an alternate payee, or another beneficiary, your payment is generally not subject to the additional 10% tax described earlier, 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 five years of participation in MOSERS.

## HOW TO OBTAIN ADDITIONAL INFORMATION

**Please consult a professional tax advisor!** This information is only intended as a signal to alert you to special tax consequences. You are encouraged to consult with your personal tax advisor before you take a payment of your benefits.

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

If your distribution from MOSERS is rolled over to another plan, the distribution from the receiving plan may be subject to different restrictions and tax consequences than those that apply to distributions from MOSERS. Also, you can find more specific information on the tax treatment of payments from qualified retirement plans in IRS Publication 575 *Pension and Annuity Income* and IRS Publication 590 *Individual Retirement Arrangements*. These publications are available on the IRS web site ([www.irs.gov](http://www.irs.gov)), from your local IRS office, or by calling (800) TAX-FORM or (800) 829-1040.

This notice summarizes the federal (not state or local) tax rules that might apply to your payment. It includes provisions of the IRS Safe Harbor Tax Notice (Notice 2000-11), as well as relevant changes made to the Internal Revenue Code by the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), effective January 1, 2002, unless otherwise noted.

This information does not amend or overrule any applicable statute, Code, or administrative rule. In the event of conflict, the applicable statute, Code, or administrative rule will prevail.

This publication may be provided in alternative formats. To obtain accessible formats, please contact MOSERS at:

(573) 632-6100 or (800) 827-1063

Missouri relay numbers are:

7-1-1 (Voice) or (800) 735-2966 (TTY)

MOSERS is an equal opportunity employer.

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