

Notice 2019-18

Offering a Lump-Sum Payment Option to Retirees Currently Receiving Annuity Payments under a Defined Benefit Plan

I. PURPOSE

This notice is to inform taxpayers that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) no longer intend to amend the required minimum distribution regulations under § 401(a)(9) of the Internal Revenue Code (Code) to address the practice of offering retirees and beneficiaries who are currently receiving annuity payments under a defined benefit plan a temporary option to elect a lump-sum payment in lieu of future annuity payments.

II. BACKGROUND

A. Section 401(a)(9) and Required Minimum Distributions

Section 401(a)(9) prescribes required minimum distribution rules for a qualified plan under § 401(a). In general, under these rules, distribution of each employee's entire interest must begin by the required beginning date. The required beginning date generally is April 1 of the calendar year following the later of (1) the calendar year in which the employee attains age 70½, or (2) the calendar year in which the employee retires. However, the ability to delay distribution until the calendar year in which an employee retires does not apply in the case of a 5-percent owner (as defined in § 416).

If the employee's entire interest is not distributed by the required beginning date, § 401(a)(9)(A) provides that the entire interest must be distributed, beginning not later than the required beginning date, in accordance with regulations, over the life of the employee or lives of the employee and a designated beneficiary (or a period not extending beyond the life expectancy of the employee or the life expectancy of the employee and a designated beneficiary). Section 401(a)(9)(B) prescribes required minimum distribution rules that apply after the death of the employee.

Section 1.401(a)(9)-6, A-1(a) provides that, absent an applicable exception, in order to satisfy § 401(a)(9), distributions of an employee's entire interest under a defined benefit plan must be paid in the form of periodic annuity payments for the employee's or beneficiary's life (or the joint lives of the employee and beneficiary) or over a period certain that is no longer than a period permitted under § 1.401(a)(9)-6, A-3 or A-10, as applicable (which is approximately equal to the joint and last survivor life expectancy of the employee and an assumed beneficiary who is 10 years younger than the employee, with a longer period if the sole beneficiary is the employee's spouse and the spouse is more than 10 years younger). The regulations prohibit any change in the

period or form of the distribution after it has commenced, except in accordance with § 1.401(a)(9)-6, A-13. If certain conditions are met, § 1.401(a)(9)-6, A-13(a) permits changes to the payment period after payments have commenced in association with an annuity payment increase described in § 1.401(a)(9)-6, A-14.

Section 1.401(a)(9)-6, A-1(a) also provides that periodic annuity payments must be nonincreasing or may increase only as otherwise provided, such as permitted increases described in § 1.401(a)(9)-6, A-14. Section 1.401(a)(9)-6, A-14(a)(4) permits annuity payments to increase “[t]o pay increased benefits that result from a plan amendment.” In addition, § 1.401(a)(9)-6, A-14(a)(5) permits annuity payments to increase “to allow a beneficiary to convert the survivor portion of a joint and survivor annuity into a lump sum upon the employee’s death,” but no similar rule is provided with respect to conversion of an employee’s annuity benefit during an employee’s life or conversion of a beneficiary’s annuity other than upon the employee’s death.

B. Notice 2015-49 and Participant Elections to Convert Annuities to Immediate Lump Sum Payments

A number of sponsors of defined benefit plans have amended their plans to provide a limited period during which certain retirees who are currently receiving lifetime annuity payments from those plans may elect to convert their annuities into lump sums that are payable immediately. These arrangements are sometimes referred to as retiree lump-sum windows. Although the treatment under § 401(a)(9) of such a right to convert a current annuity into an immediate lump sum payment has not been addressed explicitly in regulations or other generally applicable published guidance, the addition of such a right to a plan has been treated in some instances as an increase in benefits that is described in § 1.401(a)(9)-6, A-14(a)(4) (with the result that the annuity payment period would be permitted to change under § 1.401(a)(9)-6, A-13(a)).

On July 9, 2015, the IRS issued Notice 2015-49, 2015-30 I.R.B. 79, which informed taxpayers that the Treasury Department and the IRS intended to propose amendments to the required minimum distribution regulations under § 401(a)(9) to address the use of lump-sum payments to replace ongoing annuity payments under a qualified defined benefit plan. These amendments to the regulations would have provided that a lump-sum or other accelerated payment made pursuant to a plan amendment to a qualified defined benefit plan that gives a participant currently receiving annuity payments the right to convert those annuity payments into an immediate lump-sum or other accelerated payment is not treated as a payment of increased benefits described in § 1.401(a)(9)-6, A-14(a)(4). Consequently, a retiree lump-sum window would not have been eligible for the § 1.401(a)(9)-6, A-13(a) exception under which an annuity payment period may be changed in association with an annuity payment increase described in § 1.401(a)(9)-6, A-14. Notice 2015-49 explained that the

§ 401(a)(9) provisions and related regulations regarding pension plan annuities were crafted to provide an administrable way to ensure that a distribution of the employee's benefit will not be unduly tax-deferred. For example, a pension plan may not permit an employee who has passed the required beginning date to defer distribution of the bulk of the employee's benefit (and thus defer the tax) until later in life, while taking relatively small periodic benefits in the interim. In addition, under the regulations, a defined benefit plan may not permit the annuity payment period to be changed or the annuity payment to be increased, except in a narrow set of circumstances specified in the regulations, such as in the case of retirement, death, or plan termination. Notice 2015-49 further explained that if a participant has the ability to accelerate annuity distributions at any time, then the actuarial cost associated with that acceleration right would result in smaller initial benefits, which would contravene the purpose of § 401(a)(9).

Notice 2015-49 provided that the Treasury Department and the IRS intended that these amendments to the regulations would apply as of July 9, 2015, except in the case of a retiree lump-sum window with respect to which specified concrete steps (adoption, specific authorization to adopt, collective bargaining, or written communication furnished to participants) with respect to the plan amendment had been taken, or a determination letter or letter ruling had been received, before that date. In addition, Notice 2015-49 provided that the IRS would not express an opinion in private letter rulings or determination letters as to the federal tax consequences of a retiree lump-sum window.

III. RETRACTION OF INTENT TO PROPOSE REGULATIONS UNDER § 401(a)(9)

The Treasury Department and the IRS no longer intend to propose the amendments to the regulations under § 401(a)(9) that were described in Notice 2015-49. However, the Treasury Department and the IRS will continue to study the issue of retiree lump-sum windows. Until further guidance is issued, the IRS will not assert that a plan amendment providing for a retiree lump-sum window program causes the plan to violate § 401(a)(9), but will continue to evaluate whether the plan, as amended, satisfies the requirements of §§ 401(a)(4), 411, 415, 417, 436, and other sections of the Code. During this period, the IRS will not issue private letter rulings with regard to retiree lump-sum windows. However, if a taxpayer is eligible to apply for and receive a determination letter, the IRS will no longer include a caveat expressing no opinion regarding the tax consequences of such a window in the letter.

IV. EFFECT ON OTHER DOCUMENTS

Notice 2015-49 is superseded.

V. DRAFTING INFORMATION

The principal author of this notice is Thomas C. Morgan of the Office of the Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). However, other personnel from the IRS participated in development of this guidance. For further information regarding this notice, please contact Mr. Morgan at (202) 317-6700 (not a toll-free number).