

by multiplying the amount of the payment by 12. Similarly, a quarterly payment may be annualized by multiplying the amount of the payment by 4.

(4) *Alternate withholding procedures*—
(i) *In general.* Any procedure for determining the amount to be deducted and withheld under section 3402(r) may be used, provided that the amount of tax deducted and withheld is substantially the same as it would be using the tables provided by the Commissioner under paragraph (a)(2) of this section. At the election of an Indian tribe, the amount to be deducted and withheld under section 3402(r) shall be determined in accordance with this alternate procedure.

(ii) *Method of election.* It is sufficient for purposes of making an election under this paragraph (a)(4) that an Indian tribe evidence the election in any reasonable way, including use of a particular method. Thus, no written election is required.

(5) *Additional withholding permitted.* Consistent with the provisions of section 3402(p), a tribal member and a tribe may enter into an agreement to provide for the deduction and withholding of additional amounts from payments in order to satisfy the anticipated tax liability of the tribal member. The agreement may be made in a manner similar to that described in § 31.3402(p)-1 (with respect to voluntary withholding agreements between employees and employers).

(b) *Effective date.* This section applies to payments made after December 31, 1994.

[T.D. 8634, 60 FR 65238, Dec. 19, 1995]

§ 31.3403-1 Liability for tax.

Every employer required to deduct and withhold the tax under section 3402 from the wages of an employee is liable for the payment of such tax whether or not it is collected from the employee by the employer. If, for example, the employer deducts less than the correct amount of tax, or if he fails to deduct any part of the tax, he is nevertheless liable for the correct amount of the tax. See, however, § 31.3402(d)-1. The employer is relieved of liability to any other person for the amount of any such tax withheld and paid to the district director or deposited with a duly

designated depository of the United States.

§ 31.3404-1 Return and payment by governmental employer.

If the United States, or a State, Territory, Puerto Rico, or a political subdivision thereof, or the District of Columbia, or any agency or instrumentality of any one or more of the foregoing, is an employer required to deduct and withhold tax under Chapter 24, the return of the amount deducted and withheld as such tax may be made by the officer or employee having control of the payment of the wages or other officer or employee appropriately designated for that purpose. (For provisions relating to the execution and filing of returns, see Subpart G of the regulations in this part.)

§ 31.3405(c)-1 Withholding on eligible rollover distributions; questions and answers.

The following questions and answers relate to withholding on eligible rollover distributions under section 3405(c) of the Internal Revenue Code of 1986, as added by section 522(b) of the Unemployment Compensation Amendments of 1992 (Public Law 102-318, 106 Stat. 290) (UCA). For additional UCA guidance under sections 401(a)(31), 402(c), 402(f), and 403(b)(8) and (10), see §§ 1.401(a)(31)-1, 1.402(c)-2, 1.402(f)-1, and 1.403(b)-2 of this chapter, respectively.

LIST OF QUESTIONS

Q-1: What are the withholding requirements under section 3405 for distributions from qualified plans and section 403(b) annuities?

Q-2: May a distributee elect under section 3405(c) not to have Federal income tax withheld from an eligible rollover distribution?

Q-3: May a distributee be permitted to elect to have more than 20-percent Federal income tax withheld from an eligible rollover distribution?

Q-4: Who has responsibility for complying with section 3405(c) relating to the 20-percent income tax withholding on eligible rollover distributions?

Q-5: May the plan administrator shift the withholding responsibility to the payor and, if so, how?

Q-6: How does the 20-percent withholding requirement under section 3405(c) apply if a distributee elects to have a portion of an eligible rollover distribution paid to an eligible

retirement plan in a direct rollover and to have the remainder of that distribution paid to the distributee?

Q-7: Will the plan administrator be subject to liability for tax, interest, or penalties for failure to withhold 20 percent from an eligible rollover distribution that, because of erroneous information provided by a distributee, is not paid to an eligible retirement plan even though the distributee elected a direct rollover?

Q-8: Is an eligible rollover distribution that is paid to a qualified defined benefit plan subject to 20-percent withholding?

Q-9: If property other than cash, employer securities, or plan loans is distributed, how is the 20-percent income tax withholding required under section 3405(c) accomplished?

Q-10: What assumptions may a plan administrator make regarding whether a benefit is an eligible rollover distribution for purposes of determining the amount of a distribution that is subject to 20-percent mandatory withholding?

Q-11: Are there special rules for applying the 20-percent withholding requirement to employer securities and a plan loan offset amount distributed in an eligible rollover distribution?

Q-12: How does the mandatory withholding rule apply to net unrealized appreciation from employer securities?

Q-13: Does the 20-percent withholding requirement apply to eligible rollover distributions from a qualified plan distributed annuity contract?

Q-14: Must a payor or plan administrator withhold tax from an eligible rollover distribution for which a direct rollover election was not made if the amount of the distribution is less than \$200?

Q-15: If eligible rollover distributions are made from a qualified plan, who has responsibility for making the returns and reports required under these regulations?

Q-16: What eligible rollover distributions must be reported on Form 1099-R?

Q-17: Must the plan administrator, trustee or custodian of the eligible retirement plan report amounts received in a direct rollover?

QUESTIONS AND ANSWERS

Q-1: What are the withholding requirements under section 3405 for distributions from qualified plans and section 403(b) annuities?

A-1: (a) *General rule.* Section 3405(c), added by UCA, provides that any designated distribution that is an eligible rollover distribution (as defined in section 402(f)(2)(A)) from a qualified plan or a section 403(b) annuity is subject to income tax withholding at the rate of 20 percent unless the distributee of the eligible rollover distribution elects to have the distribution paid directly to an eligible retirement plan in a direct

rollover. See § 1.402(c)-2, Q&A-2 of this chapter for the definition of a qualified plan and § 1.403(b)-2, Q&A-1 of this chapter for the definition of a section 403(b) annuity. For purposes of section 3405 and this section, with respect to a distribution from a qualified plan, an eligible retirement plan is a trust qualified under section 401(a), an annuity plan described in section 403(a), or an individual retirement plan (as described in § 1.402(c)-2, Q&A-2 of this chapter). For purposes of section 3405 and this section, with respect to a distribution from a section 403(b) annuity, an eligible retirement plan is an annuity contract, a custodial account, a retirement income account described in section 403(b), or an individual retirement plan. If a designated distribution is not an eligible rollover distribution, it is subject to the elective withholding provisions of section 3405(a) and (b) and § 35.3405-1 of this chapter and is not subject to the mandatory withholding provisions of section 3405(c) and this section.

(b) *Application of other statutory provisions.* See § 1.401(a)(31)-1 of this chapter concerning the requirements and the procedures for electing a direct rollover under section 401(a)(31). See section 402(c)(2) and (4), and § 1.402(c)-2, Q&A-3 through Q&A-10 and Q&A-14 of this chapter for rules to determine what constitutes an eligible rollover distribution. See § 1.402(f)-1, Q&A-1 through Q&A-3 and § 1.403(b)-2, Q&A-3 of this chapter concerning the notice that must be provided to a distributee, within a reasonable period of time before making an eligible rollover distribution. See § 1.403(b)-2, Q&A-1 and Q&A-2 of this chapter for guidance concerning the rollover provisions and direct rollover requirements for distributions from annuities described in section 403(b).

(c) *Effective date—(1) Statutory effective date—(i) General rule.* Section 3405(c), as added by UCA, applies to eligible rollover distributions made on or after January 1, 1993, even if the employee's employment with the employer maintaining the plan terminated before January 1, 1993 and even if the eligible rollover distribution is part of a series of payments that began before January 1, 1993.

(ii) *Special rule for governmental section 403(b) annuities.* Section 522 of UCA provides a special effective date for governmental section 403(b) annuities. This special effective date appears in § 1.403(b)-2T of this chapter (as it appeared in the April 1, 1995 edition of 26 CFR part 1).

(2) *Regulatory effective date.* This section applies to eligible rollover distributions made on or after October 19, 1995. For eligible rollover distributions made on or after January 1, 1993 and before October 19, 1995, § 31.3405(c)-1T (as it appeared in the April 1, 1995 edition of 26 CFR part 1), applies. However, for any distribution made on or after

January 1, 1993 but before October 19, 1995, a plan administrator or payor may comply with the withholding requirements of section 3405(c) by substituting any or all provisions of this section for the corresponding provisions of § 31.3405(c)-1T, if any.

Q-2: May a distributee elect under section 3405(c) not to have Federal income tax withheld from an eligible rollover distribution?

A-2: No. The 20-percent income tax withholding imposed under section 3405(c)(1) applies to an eligible rollover distribution unless the distributee elects under section 401(a)(31) to have the eligible rollover distribution paid directly to an eligible retirement plan in a direct rollover. See § 1.401(a)(31)-1 and § 1.403(b)-2, Q&A-2 of this chapter for provisions concerning the requirement that a distributee of an eligible rollover distribution be permitted to elect a distribution in the form of a direct rollover.

Q-3: May a distributee be permitted to elect to have more than 20-percent Federal income tax withheld from an eligible rollover distribution?

A-3: Yes. Under section 3402(p), a distributee of an eligible rollover distribution and the plan administrator or payor are permitted to enter into an agreement to provide for withholding in excess of 20 percent from an eligible rollover distribution. Any agreement must be made in accordance with applicable forms and instructions. However, no request for withholding will be effective between the plan administrator or payor and the distributee until the plan administrator or payor accepts the request by commencing to withhold from the amounts with respect to which the request was made. An agreement under section 3402(p) shall be effective for such period as the plan administrator or payor and the distributee mutually agree upon. However, either party to the agreement may terminate the agreement prior to the end of such period by furnishing a signed written notice to the other.

Q-4: Who has responsibility for complying with section 3405(c) relating to the 20-percent income tax withholding on eligible rollover distributions?

A-4: Section 3405(d) generally requires the plan administrator of a qualified plan and the payor of a section 403(b) annuity to withhold under section 3405(c)(1) an amount equal to 20 percent of the portion of an eligible rollover distribution that the distributee does not elect to have paid in a direct rollover. When an amount is paid under a qualified plan distributed annuity contract as defined in § 1.402(c)-2, Q&A-10 of this chapter, the payor is treated as the plan administrator. See Q&A-13 of this section concerning eligible rollover distributions from a qualified plan distributed annuity contract.

Q-5: May the plan administrator shift the withholding responsibility to the payor and, if so, how?

A-5: Yes. The plan administrator may shift the withholding responsibility to the payor by following the procedures set forth in § 35.3405-1, Q&A E-2 through E-5 of this chapter (relating to elective withholding on pensions, annuities and certain other deferred income) with appropriate adjustments, including the plan administrator's identification of amounts that constitute required minimum distributions.

Q-6: How does the 20-percent withholding requirement under section 3405(c) apply if a distributee elects to have a portion of an eligible rollover distribution paid to an eligible retirement plan in a direct rollover and to have the remainder of that distribution paid to the distributee?

A-6: If a distributee elects to have a portion of an eligible rollover distribution paid to an eligible retirement plan in a direct rollover and to receive the remainder of the distribution, the 20-percent withholding requirement under section 3405(c) applies only to the portion of the eligible rollover distribution that the distributee receives and not to the portion that is paid in a direct rollover.

Q-7: Will the plan administrator be subject to liability for tax, interest, or penalties for failure to withhold 20 percent from an eligible rollover distribution that, because of erroneous information provided by a distributee, is not paid to an eligible retirement plan even though the distributee elected a direct rollover?

A-7: (a) *General rule.* If the plan administrator reasonably relied on adequate information provided by the distributee (as described in paragraph (b) of this Q&A), the plan administrator will not be subject to liability for taxes, interest, or penalties for failure to withhold income tax from an eligible rollover distribution solely because the distribution is paid to an account or plan that is not an eligible retirement plan (as defined, with respect to distributions from qualified plans, in section 402(c)(8)(B) and § 1.402(c)-2, Q&A-2 of this chapter and, with respect to a distributions from section 403(b) annuities, in § 1.403(b)-2, Q&A-1 of this chapter. Although the plan administrator is not required to verify independently the accuracy of information provided by the distributee, the plan administrator's reliance on the information furnished must be reasonable. For example, it is not reasonable for the plan administrator to rely on information that is clearly erroneous on its face.

(b) *Adequate information.* The plan administrator has obtained from the distributee adequate information on which to rely in making a direct rollover if the distributee furnishes to the plan administrator: the name of the eligible retirement plan; a representation that the recipient plan is an individual retirement plan, a qualified plan, or a section 403(b) annuity, as appropriate; and any

other information that is necessary in order to permit the plan administrator to accomplish the direct rollover by the means it has selected. This information must include any information needed to comply with the specific requirements of § 1.401(a)(31)-1, Q&A-3 and Q&A-4 of this chapter. For example, if the direct rollover is to be made by mailing a check to the trustee of an individual retirement account, the plan administrator must obtain, in addition to the name of the individual retirement account and the representation described above, the name and address of the trustee of the individual retirement account.

Q-8: Is an eligible rollover distribution that is paid to a qualified defined benefit plan subject to 20-percent withholding?

A-8: No. If an eligible rollover distribution is paid in a direct rollover to an eligible retirement plan within the meaning of section 402(c)(8), including a qualified defined benefit plan, it is reasonable to believe that the distribution is not includible in gross income pursuant to section 402(c)(1). Accordingly, pursuant to section 3405(e)(1)(B), the distribution is not a designated distribution and is not subject to 20-percent withholding.

Q-9: If property other than cash, employer securities, or plan loans is distributed, how is the 20-percent income tax withholding required under section 3405(c) accomplished?

A-9: When all or a portion of an eligible rollover distribution subject to 20-percent income tax withholding under section 3405(c) consists of property other than cash, employer securities, or plan loan offset amounts, the plan administrator or payor must apply § 35.3405-1, Q&A F-2 of this chapter and may apply § 35.3405-1, Q&A F-3 of this chapter in determining how to satisfy the withholding requirements.

Q-10: What assumptions may a plan administrator make regarding whether a benefit is an eligible rollover distribution for purposes of determining the amount of a distribution that is subject to 20-percent mandatory withholding?

A-10: (a) *In general.* For purposes of determining the amount of a distribution that is subject to 20-percent mandatory withholding, a plan administrator may make the assumptions described in paragraphs (b), (c), and (d) of this Q&A in determining the amount of a distribution that is an eligible rollover distribution and a designated distribution. Section 1.401(a)(31)-1, Q&A-18 of this chapter provides assumptions for purposes of complying with section 401(a)(31). See § 1.402(c)-2, Q&A-15 of this chapter concerning the effect of these assumptions for purposes of section 402(c).

(b) *\$5,000 death benefit.* A plan administrator may assume that a distribution that qualifies for the \$5,000 death benefit exclusion under section 101(b) is the only death benefit being paid with respect to a deceased

employee that qualifies for that exclusion. Thus, in such a case, the plan administrator may assume that the distribution is not an eligible rollover distribution to the extent that it would be excludible from gross income based on this assumption.

(c) *Required minimum distributions.* The plan administrator is permitted to determine the amount of the minimum distribution required to satisfy section 401(a)(9)(A) for any calendar year by assuming that there is no designated beneficiary.

(d) *Valuation of property.* In the case of a distribution that includes property, in calculating the amount of the distribution for purposes of applying section 3405(c), the value of the property may be determined in accordance with § 35.3405-1, Q&A F-1 of this chapter.

Q-11: Are there special rules for applying the 20-percent withholding requirement to employer securities and a plan loan offset amount distributed in an eligible rollover distribution?

A-11: Yes. The maximum amount to be withheld on any designated distribution (including any eligible rollover distribution) under section 3405(c) must not exceed the sum of the cash and the fair market value of property (excluding employer securities) received in the distribution. The amount of the sum is determined without regard to whether any portion of the cash or property is a designated distribution or an eligible rollover distribution. For purposes of this rule, any plan loan offset amount, as defined in § 1.402(c)-2, Q&A-9 of this chapter, is treated in the same manner as employer securities. Thus, although employer securities and plan loan offset amounts must be included in the amount that is multiplied by 20-percent, the total amount required to be withheld for an eligible rollover distribution is limited to the sum of the cash and the fair market value of property received by the distributee, excluding any amount of the distribution that is a plan loan offset amount or that is distributed in the form of employer securities. For example, if the only portion of an eligible rollover distribution that is not paid in a direct rollover consists of employer securities or a plan loan offset amount, withholding is not required. In addition, if a distribution consists solely of employer securities and cash (not in excess of \$200) in lieu of fractional shares, no amount is required to be withheld as income tax from the distribution under section 3405 (including section 3405(c) and this section). For purposes of section 3405 and this section, employer securities means securities of the employer corporation within the meaning of section 402(e)(4)(E)(ii).

Q-12: How does the mandatory withholding rule apply to net unrealized appreciation from employer securities?

A-12: An eligible rollover distribution can include net unrealized appreciation from employer securities, within the meaning of section 402(e)(4), even if the net unrealized appreciation is excluded from gross income under section 402(e)(4). However, to the extent that it is excludable from gross income pursuant to section 402(e)(4), net unrealized appreciation is not a designated distribution pursuant to section 3405(e)(1)(B) because it is reasonable to believe that it is not includable in gross income. Thus, to the extent that net unrealized appreciation is excludable from gross income pursuant to section 402(e)(4), net unrealized appreciation is not included in the amount of an eligible rollover distribution that is subject to 20-percent withholding.

Q-13: Does the 20-percent withholding requirement apply to eligible rollover distributions from a qualified plan distributed annuity contract?

A-13: The 20-percent withholding requirement applies to eligible rollover distributions from a qualified plan distributed annuity contract as defined in Q&A-10 of § 1.402(c)-2 of this chapter. In the case of an eligible rollover distribution from such an annuity contract, the payor is treated as the plan administrator for purposes of section 3405. See § 1.401(a)(31)-1, Q&A-17 of this chapter concerning the direct rollover requirements that apply to distributions from such an annuity contract and see § 1.402(c)-2, Q&A-10 of this chapter concerning the treatment of distributions from such annuity contracts as eligible rollover distributions.

Q-14: Must a payor or plan administrator withhold tax from an eligible rollover distribution for which a direct rollover election was not made if the amount of the distribution is less than \$200?

A-14: No. However, all eligible rollover distributions received within one taxable year of the distributee under the same plan must be aggregated for purposes of determining whether the \$200 floor is reached. If the plan administrator or payor does not know at the time of the first distribution (that is less than \$200) whether there will be additional eligible rollover distributions during the year for which aggregation is required, the plan administrator need not withhold from the first distribution. If distributions are made within one taxable year under more than one plan of an employer, the plan administrator or payor may, but need not, aggregate distributions for purposes of determining whether the \$200 floor is reached. However, once the \$200 threshold has been reached, the sum of all payments during the year must be used to determine the applicable amount to be withheld from subsequent payments during the year.

Q-15: If eligible rollover distributions are made from a qualified plan, who has respon-

sibility for making the returns and reports required under these regulations?

A-15: Generally, the plan administrator, as defined in section 414(g), is responsible for maintaining the records and making the required reports with respect to eligible rollover distributions from qualified plans. However, if the plan administrator fails to keep the required records and make the required reports, the employer maintaining the plan is responsible for the reports and returns.

Q-16: What eligible rollover distributions must be reported on Form 1099-R?

A-16: Each eligible rollover distribution, including each eligible rollover distribution that is paid directly to an eligible retirement plan in a direct rollover, must be reported on Form 1099-R in accordance with the instructions for Form 1099-R. For purposes of the reporting required under section 6047(e), a direct rollover is treated as a distribution that is immediately rolled over to an eligible retirement plan. Distributions that are not eligible rollover distributions are subject to the reporting requirements set forth in § 35.3405-1 of this chapter and applicable forms and instructions.

Q-17: Must the plan administrator, trustee or custodian of the eligible retirement plan report amounts received in a direct rollover?

A-17: (a) *Individual retirement plan.* If a distributee elects to have an eligible rollover distribution paid to an individual retirement plan in a direct rollover, the eligible rollover distribution is reported on Form 5498 as a rollover contribution to the individual retirement plan, in accordance with the instructions for Form 5498.

(b) *Qualified plan or section 403(b) annuity.* If a distributee elects to have an eligible rollover distribution paid to a qualified plan or section 403(b) annuity, the recipient plan or annuity is not required to report the receipt of the rollover contribution.

[T.D. 8619, 60 FR 49215, Sept. 22, 1995, as amended by T.D. 8880, 65 FR 21315, Apr. 21, 2000]

§ 31.3406-0 Outline of the backup withholding regulations.

This section lists paragraphs contained in §§ 31.3406(a)-1 through 31.3406(i)-1.

§ 31.3406(a)-1 Backup withholding requirement on reportable payments.

- (a) Overview.
- (b) Conditions that invoke the backup withholding requirement.
 - (1) Conditions applicable to all reportable payments.
 - (2) Conditions applicable only to reportable interest or dividend payments.
 - (c) Exceptions.