

Interim Guidance on Income Tax Withholding from Retirement and Annuity Distributions

Notice 2020-3

I. PURPOSE

This notice provides guidance for the 2020 calendar year regarding withholding from periodic payments for pensions, annuities, and certain other deferred income under § 3405(a) of the Internal Revenue Code (Code), including the rules for withholding from periodic payments under § 3405(a) when no withholding certificate has been furnished (default rate of withholding). This notice also informs taxpayers that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) are considering whether the 2020 default rate of withholding under § 3405(a) will continue to be appropriate for calendar years after 2020 and request comments related to the potential adoption of a new default rate of withholding. The deadline for submission of comments is February 17, 2020.

II. BACKGROUND

Section 3405 generally requires the payor of certain payments for pensions, annuities, and certain other deferred income to withhold amounts from the payments unless an individual has elected not to have withholding apply.¹ An individual's withholding election under § 3405 (or election not to have withholding apply, if available)

¹ The election not to have withholding apply generally is unavailable with respect to eligible rollover distributions under § 3405(c) and certain payments to be made outside of the United States or its possessions under § 3405(e)(13).

generally is made using Form W-4P, Withholding Certificate for Pension or Annuity Payments.

Section 3405(a) generally requires the payor of periodic payments from pensions, annuities, or certain other deferred income to withhold from those payments as if the payments were wages paid by an employer to an employee, unless an individual has elected not to have withholding apply. Section 3402 requires an employer to deduct and withhold income tax from employees' wages under methods and procedures prescribed by the Secretary. An employee who receives wages subject to withholding under § 3402 is required to furnish a withholding allowance certificate to his or her employer. See § 3402(f)(2), (5); Treas. Reg. § 31.3402(f)(5)-1.

Prior to the 2020 calendar year, information requested on Form W-4P regarding withholding from periodic payments generally paralleled the information requested on Form W-4 for withholding from wages.² The Form W-4 for the 2020 calendar year (which has been renamed the Form W-4, Employee's Withholding Certificate) has been redesigned to increase transparency and accuracy of the withholding system. Beginning in calendar year 2020, employers are required to use the redesigned form for all new employees and employees hired prior to 2020 who wish to adjust their withholding. As a result, information requested on the 2020 Form W-4 no longer parallels information requested on Form W-4P for withholding from periodic payments. Among other changes, the redesigned Form W-4 requests the employee's filing status, rather than marital status, and no longer requests the number of withholding allowances

² The no-withholding election that is generally available for periodic payments under § 3405(a) is not available for wages; therefore, the no-withholding election on Line 1 of the 2019 Form W-4P does not parallel the conditions to claim exemption from wage withholding on the 2019 Form W-4.

the employee is claiming. The 2020 Form W-4 also includes a new method by which an employee may request withholding using higher withholding rate tables. Importantly, the Treasury Department and the IRS have designed the withholding tables and computational procedures in the 2020 Publication 15-T, Federal Income Tax Withholding Methods, to work with both a 2019 or earlier Form W-4 and the redesigned 2020 Form W-4. Therefore, for purposes of withholding from periodic payments under § 3405(a), the IRS plans to provide in the 2020 Publication 15-A, Employer's Supplemental Tax Guide, that the 2020 Form W-4P will work with certain withholding tables and computational procedures in the 2020 Publication 15-T that are applicable to a 2019 or earlier Form W-4.

Section 3405(a)(4) was amended by section 11041(c)(2)(G) of the Tax Cuts and Jobs Act, Pub. L. 115-97 (TCJA) to provide that the withholding rate for periodic payments when no withholding certificate has been furnished “shall be determined under rules prescribed by the Secretary.” Under the law in effect before 2018, § 3405(a)(4) provided that, in the case of a payee entitled to periodic payments with respect to which a withholding certificate had not been furnished, the amount to be withheld from each such payment “shall be determined by treating the payee as a married individual claiming 3 withholding exemptions.” Temporary Treasury Regulations issued under § 3405 (as in effect before 2018) continue to provide that, if no withholding certificate has been furnished with respect to periodic payments under § 3405(a), then the payor must base withholding on the rates for a married person claiming three withholding allowances. See Temp. Treas. Reg. § 35.3405-1T, Q&As A-10, B-3, B-4.

Following enactment of TCJA, the Treasury Department and the IRS issued guidance to address changes made by TCJA to withholding rules under §§ 3401, 3402, and 3405. See Notice 2018-14, 2018-7 I.R.B. 353, and Notice 2018-92, 2018-51 I.R.B. 1038. With respect to § 3405(a), section V of Notice 2018-14 provided that, for 2018, the default rate of withholding would parallel the rules for prior years and would be based on treating the payee as a married individual claiming three withholding allowances. Similarly, section 10 of Notice 2018-92 provided that, for 2019, the default rate of withholding under § 3405(a)(4) would parallel the rules for prior years, and would be based on treating the payee as a married individual claiming three withholding allowances.

III. 2020 FORM W-4P AND RELATED TABLES AND COMPUTATIONAL PROCEDURES FOR WITHHOLDING UNDER SECTION 3405(a)

The information requested on the 2020 Form W-4P for periodic payments (other than the no-withholding election on Line 1) generally will continue to parallel the information requested on Form W-4 prior to 2020. Payees of periodic payments may use either the worksheets to Form W-4P or the Tax Withholding Estimator (www.irs.gov/W4App) to assist in determining their entries on the 2020 Form W-4P. As explained in Section II of this notice, certain withholding tables and computational procedures in the 2020 Publication 15-T that are applicable to a 2019 or earlier Form W-4 will also work with the 2020 Form W-4P.

IV. RULES FOR 2020 FOR WITHHOLDING FROM PERIODIC PAYMENTS UNDER SECTION 3405(a) WHEN NO WITHHOLDING CERTIFICATE HAS BEEN FURNISHED

For the 2020 calendar year, the rules for withholding from periodic payments under § 3405(a) when no withholding certificate has been furnished will continue to

parallel the rules for prior years. Therefore, for 2020, the default rate of withholding from periodic payments under § 3405(a) will be based on treating the payee as a married individual claiming three withholding allowances and applying that status to the applicable withholding tables and related computational procedures in the 2020 Publication 15-T. The IRS plans to provide in the 2020 Publication 15-A that this default rate of withholding will work with certain withholding tables and computational procedures in the 2020 Publication 15-T that are applicable to a 2019 or earlier Form W-4.

V. WITHHOLDING UNDER SECTION 3405(a) FOR YEARS AFTER 2020

The Treasury Department and the IRS will provide the rules and procedures that apply for calendar years after 2020 for withholding from periodic payments under § 3405(a) in applicable forms, instructions, publications, and other guidance. In addition, the Treasury Department and the IRS are considering whether the default rate of withholding from periodic payments under § 3405(a) described in section IV of this notice will continue to be appropriate for calendar years after 2020.

VI. REQUEST FOR COMMENTS

The Treasury Department and the IRS invite comments on whether the adoption of a new default rate of withholding from periodic payments under § 3405(a) that would apply prospectively (that is, would only apply to periodic payments that begin after the effective date of the new default withholding rate) would present any administrative challenges.

Comments should be submitted in writing on or before February 17, 2020. Comments should include a reference to Notice 2020-3. Comments may be submitted

electronically via the Federal eRulemaking Portal at www.regulations.gov (type IRS-2019-0051 in the search field on the **regulations.gov** homepage to find this notice and submit comments). Alternatively, comments may be mailed to: CC:PA:LPD:PR (Notice 2020-3), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. All comments will be available for public inspection and copying in their entirety.

VII. PAPERWORK REDUCTION ACT

Any collection of information associated with this notice has been submitted to the Office of Management and Budget for review under OMB control number 1545-0074 in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). In general, the collection of information is required under § 3405(a). 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 OMB control number.

VIII. DRAFTING INFORMATION

The principal author of this notice is Kara M. Soderstrom of the Office of the Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). However, other personnel from the Treasury Department and the IRS participated in the development of this guidance. For further information regarding this notice, contact Ms. Soderstrom at 202-317-6799 (not a toll-free number).