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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-105739-11]

Removal of Allocation Rule for Disbursements from Designated Roth Accounts to Multiple Destinations

RIN 1545- BK08

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed amendments to the regulations that address the tax treatment of distributions from designated Roth accounts under tax-favored retirement plans. The proposed regulations would limit the applicability of the rule regarding the allocation of after-tax amounts when disbursements are made to multiple destinations so the allocation rule applies only to distributions made before the earlier of January 1, 2015 or a date chosen by the taxpayer that is on or after **[INSERT DATE THIS DOCUMENT IS FILED FOR PUBLIC INSPECTION BY THE FEDERAL REGISTER]**. These regulations would affect administrators of, employers maintaining, participants in, and beneficiaries of designated Roth accounts under tax-favored retirement plans.

DATES: Written or electronic comments and requests for a public hearing must be received by **[INSERT DATE 90 DAYS AFTER PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER]**.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-105739-11), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington D.C. 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG-105739-11), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C., or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-105739-11).

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, Michael P. Brewer at (202) 317-6700; concerning submission of comments or to requests for a public hearing, Oluwafunmilayo (Funmi) Taylor at (202) 317-6901 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

**Background**

Section 402(a) provides generally that any amount distributed from a trust described in section 401(a) that is exempt from tax under section 501(a) is taxable to the distributee under section 72 in the taxable year of the distributee in which distributed. Under section 403(b)(1), any amount distributed from a section 403(b) plan is also taxable to the distributee under section 72.

If a participant's account balance in a plan qualified under section 401(a) or in a section 403(b) plan includes both after-tax and pretax amounts, then, under section 72(e)(8), each distribution (other than a distribution that is paid as part of an annuity) from the plan will include a pro rata share of both after-tax and pretax amounts. (Under section 72(d), a different allocation method applies to annuity distributions.)

Under section 402A(d)(4), section 72 is applied separately with respect to distributions and payments from a designated Roth account and other distributions and payments from the plan.

Section 402(c) prescribes rules for amounts that are rolled over from qualified trusts to eligible retirement plans, including individual retirement accounts or annuities (“IRAs”). Subject to certain exceptions, section 402(c)(1) provides that if any portion of an eligible rollover distribution paid to an employee from a qualified trust is transferred to an eligible retirement plan, the portion of the distribution so transferred is not includible in gross income in the taxable year in which paid.

Under section 402(c)(2), the maximum portion of an eligible rollover distribution that may be rolled over in a transfer to which section 402(c)(1) applies generally cannot exceed the portion of the distribution that is otherwise includible in gross income. However, under section 402(c)(2)(A) and (B), the general rule does not apply to such a distribution to the extent that such portion is transferred in a direct trustee-to-trustee transfer to a qualified trust or to an annuity contract described in section 403(b) and such trust or contract provides for separate accounting for amounts so transferred (and earnings thereon), including separately accounting for the portion of such distribution which is includible in gross income and the portion of such distribution which is not so includible, or such portion is transferred to an IRA

In addition, section 402(c)(2) that, in the case of a transfer described in subparagraph (A) or (B), the amount transferred shall be treated as consisting first of the portion of such distribution that is includible in gross income (determined without regard to section 402(c)(1)).

Under section 402A, an applicable retirement plan may include a designated Roth account. An applicable retirement plan is defined in section 402A(e)(1) to mean a plan qualified under section 401(a), a section 403(b) plan, and a governmental section 457(b) plan. Section 402A(d) provides that a qualified distribution (as defined in section 402A(d)(2)) from a designated Roth account is not includible in gross income.

Section 1.402A-1, Q&A-5(a), of the Income Tax Regulations prescribes taxability rules for a distribution from a designated Roth account that is rolled over. Q&A-5(a) provides, in part, that “any amount paid in a direct rollover is treated as a separate distribution from any amount paid directly to the employee.”

Section 402(f) requires that the plan administrator of a plan qualified under section 401(a) provide any recipient of an eligible rollover distribution with a written explanation describing certain provisions of law. Notice 2009-68, 2009-2 CB 423 (September 28, 2009), contains two safe harbor explanations that may be provided to recipients of eligible rollover distributions from an employer plan in order to satisfy section 402(f). The safe harbor explanation with respect to distributions that are not from a designated Roth account provides in part (under the heading “If your payment includes after-tax contributions”) that “[i]f you do a direct rollover of only a portion of the amount paid from the Plan and a portion is paid to you, each of the payments will include an allocable portion of the after-tax contributions.” Similarly, for distributions from a designated Roth account, the safe harbor explanation provides in part (under the heading “How Do I Do a Rollover?”) that “[i]f you do a direct rollover of only a portion of the amount paid from the Plan and a portion is paid to you, each of the

payments will include an allocable portion of the earnings in your designated Roth account.”

Sections 403(b)(8)(B) and 457(e)(16)(B) provide that the rules of section 402(c)(2) through (7), (9), and (11) and the rules of section 402(f) also apply to section 403(b) plans and governmental section 457(b) plans.

In response to Notice 2009-68, comments were received requesting changes to the rules regarding the allocation of basis among simultaneous disbursements to multiple destinations from a retirement plan that contains both after-tax and pretax amounts. Commenters indicated that some plan providers were treating disbursements to separate destinations not as separate distributions but rather as a single distribution of the aggregate disbursement amounts. These plan providers permitted allocation of all the after-tax amounts included in the disbursements to a Roth IRA. The commenters also pointed out that, even under the allocation method described in Notice 2009-68, a participant who wishes to disburse after-tax amounts to one destination and pretax amounts to another could accomplish this result in a series of steps. First, the participant could take an eligible rollover distribution as a single cash distribution. Second, by taking advantage of the rule in section 402(c)(2) that distribution amounts that are rolled over are treated as consisting first of pretax amounts, the participant could roll over the pretax amounts included in the distribution to one destination, such as a traditional IRA. The remaining amount of the distribution would be after-tax, which the participant could either roll over into a Roth IRA or retain without incurring any tax liability. The option to roll over all after-tax amounts into a Roth IRA, however, would be available only to taxpayers with sufficient funds available

outside of the plan to be able to roll over the entire amount distributed, including an amount equal to the 20 percent of the taxable portion of the distribution that is required to be paid to the IRS as withholding pursuant to § 3405(c).

These proposed regulations are being issued in conjunction with Notice 2014-54 (to be published in IRB 2014- 41 (October 6, 2014)), which will permit a taxpayer to direct after-tax and pretax amounts that are simultaneously disbursed to multiple destinations so as to allocate them to specific destinations. Taxpayers will be able to direct these allocations in connection with disbursements that are directly rolled over, not only in connection with 60-day rollovers after receiving a distribution.

### **Explanation of Provisions**

The proposed regulations would limit the applicability of the existing requirement in §1.402A-1, Q&A-5(a), that “any amount paid in a direct rollover is treated as a separate distribution from any amount paid directly to the employee.” Under the proposed regulations, that separate distribution requirement would not apply to distributions made on or after January 1, 2015, or an earlier date chosen by the taxpayer. An earlier date chosen by the taxpayer for this purpose may not be earlier than **[INSERT DATE THIS DOCUMENT IS FILED FOR PUBLIC INSPECTION BY THE FEDERAL REGISTER]**. See the “Proposed Effective Date” section of this preamble for a description of the rules that will apply after the separate distribution rule of §1.402A-1, Q&A-5(a), no longer applies to distributions.

### **Proposed Effective Date**

These regulations are proposed to apply to distributions from designated Roth accounts made on or after January 1, 2015. For distributions from designated Roth

accounts made on or after the applicability date of the Treasury decision that finalizes these proposed regulations (but no earlier than January 1, 2015), the rules in section III of Notice 2014-54 will apply.

For distributions that are made on or after **[INSERT DATE THIS DOCUMENT IS FILED FOR PUBLIC INSPECTION BY THE FEDERAL REGISTER]** and before the applicability date of the Treasury decision that finalizes these proposed regulations, taxpayers may rely on these proposed regulations. Taxpayers relying on these proposed regulations should apply a reasonable interpretation of the last sentence of section 402(c)(2) to allocate after-tax and pretax amounts among disbursements made to multiple destinations. For this purpose, a reasonable interpretation of the last sentence of section 402(c)(2) includes the rules issued by the IRS in section III of Notice 2014-54.

### **Statement of Availability of IRS Documents**

The IRS notices cited in this preamble are published in the Internal Revenue Bulletin or Cumulative Bulletin and are available from the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402, or by visiting the IRS website at <http://www.irs.gov>.

### **Special Analyses**

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 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, these regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

### **Comments and Requests for Public Hearing**

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The Treasury Department and the IRS specifically request comments on the clarity of the proposed regulations and how they may be made easier to understand.

All comments will be available for public inspection and copying at [www.regulations.gov](http://www.regulations.gov) or upon request. A public hearing will be scheduled if requested in writing by any 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 proposed regulations is Michael P. Brewer, IRS Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and the Department of Treasury participated in the development of the proposed regulations.

### **List of Subjects in 26 CFR Part 1**

Income taxes, Reporting and recordkeeping requirements.

### **Proposed Amendments to the Regulations**



Accordingly, 26 CFR part 1 is proposed to be 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 1.402A-1 is amended by adding a sentence after the third sentence of paragraph A-5. (a) to read as follows:

§1.402A-1 Designated Roth Accounts.

\* \* \* \* \*

A-5. (a) \* \* \* The preceding sentence does not apply to distributions made on or after January 1, 2015; in addition, a taxpayer may elect not to apply the preceding sentence to distributions made on or after an earlier date that is no earlier than

**[INSERT DATE THIS DOCUMENT IS FILED FOR PUBLIC INSPECTION BY THE FEDERAL REGISTER]**. \* \* \*

\* \* \* \* \*

John Dalrymple,  
Deputy Commissioner for Services and Enforcement.