



Important Tax Information About Thrift Savings Plan Death Benefit Payments

Except as noted below for uniformed services accounts and in Section 2 for transfers and rollovers, death benefits paid from the accounts of deceased Thrift Savings Plan (TSP) participants are taxable income for Federal income tax purposes in the year in which the payment is made. The person receiving the payment is responsible for paying the tax.

We are required by law to provide you with this tax notice, which summarizes the tax rules applicable to TSP payments made following a participant's death. Because the tax rules are complex, however, you may wish to consult a tax advisor before you make any decision that might be affected by them.

Special Note for Uniformed Services Accounts

TSP accounts for members of the uniformed services may include contributions from pay earned in a combat zone. Pay earned in combat zone is exempt from Federal income taxes; therefore, TSP contributions from pay earned in a combat zone are also exempt from Federal income taxes when they are subsequently distributed from a TSP uniformed services account. (This is not true for the earnings attributable to contributions from pay earned in a combat zone; all earnings are taxable when they are distributed from a TSP account.)

The TSP will make all payments from a uniformed services account on a *pro rata* basis from both taxable and tax-exempt balances. A death benefit payment will therefore include taxable and tax-exempt balances if the account includes contributions from pay earned in a combat zone. Internal Revenue Service (IRS) Form 1099-R, Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., which the TSP provides you, will separately state the total amount of the distribution to you and the amount of the taxable distribution. (See *Section 3 of this notice*.)

Unless otherwise noted, the following discussion applies **only** to the taxable portion of a death benefit payment.

1. Tax Withholding

The Federal income tax withholding and rollover rules for TSP death benefit payments depend upon whether the payment is made to the surviving spouse or to someone other than the surviving spouse.

Tax Withholding on Death Benefit Payments Made to Surviving Spouses

A death benefit payment to a surviving spouse is considered an **eligible rollover distribution**. The following tax withholding rules apply:

- The mandatory tax withholding on all eligible rollover distributions of \$200 or more paid by the TSP in a single year is 20%. The 20% is tax withholding, not actual tax due; therefore, when the surviving spouse files an annual Federal income tax return, he or she may be entitled to a refund of a portion of this amount, or may be required to pay an additional amount.
- A surviving spouse can avoid the 20% withholding on all or any portion of an eligible rollover distribution by asking the TSP to transfer that amount to a "traditional IRA" or an eligible employer plan.¹ However, the recipient **cannot** avoid the mandatory 20% withholding on any amount that he or she elects to receive directly, including payments made by direct deposit (electronic funds transfer (EFT)) to his or her personal checking or savings account, even if the payment is then rolled over to a traditional IRA or eligible employer plan. (See *Section 2 of this notice*.)

¹ A "traditional IRA" is an individual retirement account described at § 408(a) of the Internal Revenue Code (I.R.C.) or an individual retirement annuity described at I.R.C. § 408(b). (It does not include a Roth IRA, a SIMPLE IRA, or a Coverdell Education Savings Account (formerly known as an education IRA).) An "eligible employer plan" includes a plan qualified under I.R.C. § 401(a), including a § 401(k) plan, profit-sharing plan, defined benefit plan, stock bonus plan, and money purchase plan; an I.R.C. § 403(a) annuity plan; an I.R.C. § 403(b) tax-sheltered annuity; and an eligible I.R.C. § 457(b) plan maintained by a governmental employer.

- A surviving spouse may elect to have an amount withheld in addition to the 20% withholding by completing Line 3 of IRS Form W-4P, Withholding Certificate for Pension or Annuity Payments,² and submitting the form to the TSP Service Office at the address provided at the end of this notice. Line 1 and Line 2 are not valid elections for this type of payment.
- There is no mandatory withholding if the total death benefit payment to the surviving spouse is less than \$200. However, the spouse can still elect withholding for a payment less than \$200 by completing Line 3 of Form W-4P.

Tax Withholding on Death Benefit Payments Made to Persons Other Than Surviving Spouses

A death benefit payment to a person who is not the surviving spouse of the deceased participant is treated as a **non-periodic payment** for Federal income tax withholding purposes.

The TSP will withhold 10% for Federal income tax from the payment unless the TSP Service Office receives IRS Form W-4P, Withholding Certificate for Pension or Annuity Payments, from the payee.

If you submit IRS Form W-4P, you may elect:

- to have no Federal income tax withheld, by completing Line 1 of Form W-4P; or
- to have an amount withheld in addition to the 10%, by completing Line 3 of Form W-4P.

Line 2 of Form W-4P is not a valid election for this type of payment.

Special Note for Beneficiaries of Non-resident Aliens

Special tax withholding rules apply to TSP payments made to beneficiaries of nonresident aliens. For a detailed explanation of how these rules apply to you, please read the TSP tax notice “Tax Treatment of Thrift Savings Plan Payments to Non-resident Aliens and Their Beneficiaries.” You can obtain a copy of the notice from the TSP Web site (www.tsp.gov) or by calling or writing to the TSP Service Office.

² If you are receiving a death benefit payment from both a civilian TSP account and a uniformed services TSP account, you must submit a separate IRS Form W-4P for each account.

A **nonresident alien** is an individual who is neither a U.S. citizen nor a resident alien in the United States.³ A **resident alien** is a non-citizen who is or was a lawful permanent resident of the United States during any part of a calendar year. An alien may also be considered a U.S. resident if the individual meets the IRS “substantial presence” test for a calendar year.⁴ For information on residency status and the tests for residency, you may obtain IRS Publication 515, *Withholding of Tax on Nonresident Aliens and Foreign Entities*, or IRS Publication 519, *U.S. Tax Guide for Aliens*.

Other Tax Withholding Information

If you do not have enough Federal income tax withheld from your payment, you may be responsible for paying estimated tax. You may also incur penalties under the IRS estimated tax rules if your withholding and estimated tax payments are not sufficient.

You can request additional withholding by completing Line 3 of IRS Form W-4P. If you complete Line 3 of IRS Form W-4P and the total amount of the withholding equals or exceeds the amount of your payment, your entire payment will be withheld.

The TSP does not withhold for state, city, county, or other local income tax. Therefore, you should consult your tax advisor or relevant state or local taxing authorities regarding any potential tax obligations to them.

2. Transferring or Rolling Over a TSP Payment Made to a Surviving Spouse

If you are a surviving spouse receiving a TSP death benefit payment, all or any part of it can either be transferred or rolled over to a traditional IRA or an eligible employer plan. This permits you to postpone paying tax on that amount until you withdraw the money from the IRA or plan. However, distributions from the IRA or plan to which the transfer or rollover is made may be subject to different plan rules and tax consequences from those that apply to distributions from the TSP. Before making the transfer or rollover, you should consult with the administrator of the IRA or plan that is to receive your payment.

³ The “United States” includes the 50 States and the District of Columbia.

⁴ This is commonly referred to as the “green card” test.

If you are also currently a TSP participant (active or separated), your death benefit payment may be transferred into your TSP account. If you are separated from service, however, you must not be receiving monthly payments from your account.

A **transfer** occurs when you instruct the TSP to send all or part of your payment to a traditional IRA or to an eligible employer plan instead of issuing it directly to you. Mandatory 20% Federal income tax withholding does not apply to an amount that the TSP transfers to a traditional IRA or an eligible employer plan; **however, it does apply to any payment made directly to you (or to your personal checking or savings account via EFT), even if you then roll it over.**

A **rollover** occurs when the TSP makes a distribution to you (which includes the amount of the payment you receive plus the amount of tax withheld) and you deposit any part of that distribution into a traditional IRA or eligible employer plan within 60 days of the date you receive it.

In deciding whether to choose a transfer or a rollover, you should consider the following:

- You must pay Federal income tax on any part of the payment that you do not transfer or roll over.
- Because all eligible rollover distributions of \$200 or more made directly to you (or to your personal checking or savings account via EFT) are subject to mandatory 20% withholding, you must pay Federal income tax on the amount withheld for taxes — even if you roll over the amount you receive — unless you deposit personal funds equal to the amount withheld into your traditional IRA or eligible employer plan. (If you do this, you may receive a refund of taxes withheld, but you cannot wait until you receive a refund of the withheld amount to complete a rollover.)

Therefore, if you do not want to use personal funds to make up the amount withheld, you should choose to have the TSP transfer the death benefit payment to your traditional IRA or eligible employer plan directly, instead of rolling it over to your IRA or plan yourself.

If you are not the surviving spouse of the deceased participant, you cannot transfer or roll over your TSP death benefit payment.

Special Note for Uniformed Services Accounts

Tax-exempt balances (i.e., contributions from pay earned in a combat zone) may be transferred or rolled over into a traditional IRA or transferred into certain eligible employer plans, but only if the IRA or plan accepts tax-exempt balances. Although a death benefit payment will be distributed to you based on the proportion of taxable and tax-exempt balances in your account, if you choose to transfer a portion of the payment, the taxable balance will be transferred to your IRA or plan first. Tax-exempt money will be transferred only if the taxable portion of your payment does not satisfy the percentage that you elect to transfer to your IRA or plan. Any tax-exempt money in your payment that cannot be transferred will be paid directly to you (or to your checking or savings account, if you so elect).

As a surviving spouse, you may transfer (but not roll over) the deceased participant's tax-exempt balance only to certain eligible employer plans. The types of eligible employer plans that are permitted to accept a transfer of tax-exempt balances from the TSP are plans qualified under I.R.C. § 401(a) and I.R.C. § 403(a) annuity plans; however, a plan is not legally required to accept such a transfer.

You cannot first transfer or roll over a tax-exempt balance into a traditional IRA and later transfer or roll over that amount into an employer plan. If you transfer or roll over a tax-exempt balance into a traditional IRA, it is your responsibility to keep track of the amount of these contributions and report that amount to the IRS on the appropriate form so that the nontaxable amount of any future distribution(s) can be determined.

Tax-exempt balances in a uniformed services TSP account may not be transferred into your own civilian TSP account if you have one.

3. Tax Reporting

The TSP will report to the IRS all death benefit payments, as well as all amounts transferred to traditional IRAs or to eligible employer plans. The TSP will also report TSP payments and transfers to the state in which our records show the beneficiary resides at the time the payments are made, if that state imposes an income tax.

In January of the year that follows a TSP payment, the TSP will send each beneficiary Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. You should include the taxable amount reported on Form 1099-R as income on your individual income tax return for the year in which payment is made. **You should keep the TSP Service Office informed of any changes in your address until you receive this tax information.**

The TSP must provide the correct Taxpayer Identification Number (TIN) to the IRS on Form 1099-R. In the case of payments to individual beneficiaries, the beneficiaries' Social Security numbers will be used. For payments to a trust or estate, an executor, administrator, or trustee must furnish to the TSP a TIN for the estate or trust before payment will be made to that entity. (An individual who applies to the TSP for a payment as a representative of the estate using a state's small estate procedure must also furnish a TIN for the estate.) A TIN must be furnished for a trust or estate even though there may be no need to file IRS Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return.

4. Ten-Year Tax Option

If the payment you receive from the TSP qualifies as an **eligible lump sum distribution**, you may be able to lower the income tax you pay by using the **10-year tax option**.

An **eligible lump sum distribution** is one in which the participant's total TSP account balance (if the participant had two accounts, his or her civilian and uniformed services TSP accounts, including tax-exempt balances, if any) is distributed within one tax year (the calendar year, for most taxpayers), regardless of whether this occurs in one or more payments to a single beneficiary or to multiple beneficiaries. With the **10-year tax option**, your eligible lump sum distribution is taxed as if it were paid to you over 10 tax years.

The following rules apply to the 10-year tax option:

- The 10-year tax option is available only if the participant was age 50 before January 1, 1986.
- You must use the 10-year tax option for all eligible lump sum distributions that you receive in the same tax year. This includes an eligible lump sum distribution from any plan described in I.R.C. § 401(a) or § 403(a) which is maintained by another employer of the participant.
- You must use the tax rates in effect in 1986.
- If you transfer or roll over all or any part of your distribution, you cannot use the 10-year tax option.

You can elect the 10-year tax option by filing IRS Form 4972, Tax on Lump Sum Distributions (From Qualified Plans of Participants Born Before 1936), with your annual income tax return.

5. TSP Service Office Information

If you have any questions regarding this notice, please contact the TSP Service Office at (504) 255-8777 (TDD: (504) 255-5113), or write to:

TSP Service Office
National Finance Center
P.O. Box 61500
New Orleans, LA 70161-1500

If contacting the Service Office in writing, include both your name and Social Security number and the name and Social Security number of the deceased TSP participant. The Social Security numbers are important in identifying the TSP account to which the payment relates.