

Tax Information for TSP Participants Receiving Installment Payments

All taxable portions¹ of TSP installment payments are subject to federal tax withholding unless you transfer your eligible payments to an IRA or eligible employer plan. This tax notice explains the IRS rules governing federal tax withholding on installment payments and eligibility to transfer these payments. The table on page 3 provides a summary. Please see the TSP tax notice *Important Tax Information About Payments From Your TSP Account* for information about other TSP tax matters.

We do not withhold for state or local income tax. However, we report all TSP distributions on IRS Form 1099-R to your state of residence. Since we do not address state and local tax withholding in this tax notice, you should also seek information from your state and municipality.

We cannot give tax advice; we are providing this tax notice to ensure you have the facts you need to make informed decisions about installment payments. Because tax rules are complex, you may wish to speak with a tax advisor.

¹ The taxable portions of your payments include contributions made to your traditional balance except for any contributions made from tax-exempt pay earned while serving in a combat zone; the earnings on all contributions in your traditional balance, including earnings on tax-exempt contributions; and non-qualified earnings on all contributions made to your Roth balance. See the TSP tax notice *Important Tax Information About Payments From Your TSP Account* for more information.

Federal Tax Withholding Rules for Installment Payments²

The main factor in determining which IRS tax withholding requirements apply to the taxable portion of your installment payments is how long those payments are expected to last. When you start installment payments you choose to receive a fixed dollar amount (minimum \$25) or to have us calculate an amount based on life expectancy. Payments based on life expectancy and fixed-dollar-amount payments expected to last 10 years or more fall into one tax category; fixed-dollar-amount payments expected to last less than ten years fall into another.

Payments Expected to Last 10 Years or More or Based on Life Expectancy

- The IRS categorizes these as periodic payments.
- All installment payments based on life expectancy are included in this category, regardless of your age.

² While you're receiving installment payments, you may also choose to receive single withdrawals from your account or to use money from your account to purchase an annuity. These withdrawals could affect withholding on your installment payments, as described in the following section. However, the withholding rules for single withdrawals and annuity purchases are often different from those for installment payments. See the TSP tax notice *Important Tax Information About Payments From Your TSP Account* for details.

- You're not allowed to transfer any part of these payments to an IRA or employer plan.
- We're required to withhold for federal taxes from any taxable amount as if you are married with three dependents unless you elect a different option.
- You can choose to have an increase or decrease in the withholding amount or to have withholding waived.
- Any installment payment of this type—and any portion of such payment—that goes toward satisfying a **required minimum distribution (RMD)**³ is subject to the rules described here. This is an exception to the usual RMD withholding rules.

Payments Expected to Last Less Than 10 Years

- The IRS categorizes these as eligible rollover distributions.
- You're allowed to transfer all or part of these payments to an IRA or eligible employer plan. We are not required to withhold for federal taxes from money you transfer directly to your other plan or IRA unless you're transferring from your traditional balance to a Roth IRA.

³ The IRS requires separated and beneficiary participants to receive a portion of their TSP accounts within certain deadlines. See either *Important Tax Information About Your TSP Withdrawal and Required Minimum Distributions* or *Tax Information About TSP Withdrawals and Required Minimum Distributions for Beneficiary Participants* for more information about RMDs.



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- We're required to withhold at least 20% of any taxable part of your payments that you do not directly transfer. You may still roll over all or part of such payments to an IRA or eligible employer plan. Generally, you have 60 days after receiving payment to do the rollover. If you want to roll over the full amount of the payment, you must use other funds to make up for the amount withheld.
- You can choose to have us withhold more than 20%, but you cannot request that we withhold less or waive withholding.
- Any installment payment of this type—and any portion of such payment—that goes toward satisfying a **required minimum distribution (RMD)**⁴ is subject to a different set of tax rules:
 - The IRS categorizes these as non-periodic payments.
 - You're not allowed to transfer RMDs to an IRA or employer plan.
 - We're required to withhold 10% of any taxable amount for federal taxes unless you elect a different option.
 - You can elect to have us withhold more than 10% or to waive withholding, but you cannot elect to have an amount less than 10% withheld.

Calculating How Long Your Payments Will Last

To determine the expected duration of your fixed-dollar-amount installment payments,⁵ we simply divide your total TSP account balance by the dollar amount of your payment and then see how many years it would take for you to receive that many payments:

For annual payments: $\text{Balance} \div \text{Payment Amount}$

For quarterly payments: $(\text{Balance} \div \text{Payment Amount}) \div 4$

For monthly payments: $(\text{Balance} \div \text{Payment Amount}) \div 12$

For example, if you have a total account balance of \$100,000 and you receive quarterly payments of \$2,000, you are expected to receive 50 payments. You receive four each year since they're quarterly, so your expected payment duration is 12.5 years:

$$(\$100,000 \div \$2,000) \div 4 \text{ payments per year} = 12.5 \text{ expected years of payments}$$

Since 12.5 is greater than 10, we would use the rules for payments expected to last 10 years or more.

Note that we do not consider potential earnings or losses when we calculate your payment duration.

*Recalculating Payment Duration*⁶

We do the calculation just described when you first establish your fixed-dollar-amount TSP installment payments. That happens when you first start your payments **or**, if your installment payments were initially based on life expectancy, if you change to a fixed dollar amount. Once your fixed-dollar-amount payments have begun, we don't recalculate unless you make certain transactions. For example, if we originally calculated your expected payment duration to be 12.5 years and you don't make any of the transactions described later in this section, your payments stay in the 10-years-or-more category even if your balance drops to a level that would result in payments expected to last less than 10 years. This could be the result of market losses or simply from your having received your installment payments over time.

The following events do, however, trigger a recalculation of your payment duration:

- You **withdraw money** from your account in addition to your regular installment payments.
- You use part of your TSP account balance to **purchase an annuity** through our annuity vendor.
- You **transfer \$1,000 or more into your TSP account** from an IRA or eligible employer plan.
- You **change the dollar amount** of your installment payments.
- You **change the frequency** of your installment payments.

The result of the recalculation, which takes place at the time you take the action, will determine which set of rules we must follow for the taxable portion of your installment payments from that point on, until you make another transaction that causes a recalculation.

Remember that changing the amount or frequency of your installment payments could have tax consequences. Consider talking to a tax advisor before making such a change.

⁴ The IRS requires separated and beneficiary participants to receive a portion of their TSP accounts within certain deadlines. See either *Important Tax Information About Your TSP Withdrawal and Required Minimum Distributions* or *Tax Information About TSP Withdrawals and Required Minimum Distributions for Beneficiary Participants* for more information about RMDs.

⁵ Remember, this calculation of payment duration only applies to payments of a fixed dollar amount. We must treat all life-expectancy-based payments the same as payments expected to last 10 years or more, regardless of your age. We recalculate life expectancy each January, but this only affects the amount of your payments and does not change which tax rules apply.

⁶ See the TSP booklet *Withdrawing From Your TSP Account for Separated and Beneficiary Participants*, available at tsp.gov, for information about these options.

Early Withdrawal Tax Penalty

Participants who separate from service before the age of 55 and choose to receive installment payments may be subject to a 10% early withdrawal penalty. Installment payments based on life expectancy are an exception to the rule. But the penalty can be applied retroactively if you do any of the following within five years of beginning your payments or before you reach age 59½:

- stop your life-expectancy-based payments
- switch them to payments of a fixed dollar amount
- withdraw money in addition to your life-expectancy-based payments

Doing any of those things in that period of time will make you liable for the penalty tax on the payments you previously received.

Resources

You can obtain other information about the TSP from tsp.gov or by calling us toll free at 1-877-968-3778 (TDD: 1-877-847-4385). Outside the U.S. and Canada, please call 404-233-4400 (not toll free).

Tax Treatment for TSP Installment Payments

Type of TSP Payment	Type of Payment for IRS Purposes	May I Transfer or Roll Over the Payment?	What Is the Withholding Rate?	May I Increase Withholding?	May I Decrease Withholding?	May I Waive Withholding?
Fixed-dollar-amount installment payments expected to last less than 10 years*	Eligible rollover distribution	Yes	20%	Yes—complete the withholding section of your withdrawal request.	No	No
Fixed-dollar-amount installment payments expected to last less than 10 years when used to satisfy a required minimum distribution (See page 2.)	Non-periodic payments	No	10%	Yes—complete line 3 of IRS Form W4-P.	No	Yes—complete line 1 of IRS Form W4-P.
Fixed-dollar-amount installment payments expected to last more than 10 years**	Periodic payments	No	As if married with 3 dependents	Yes—complete the withholding section of your withdrawal request.	Yes—complete the withholding section of your withdrawal request.	Yes—complete the withholding section of your withdrawal request.
Life-expectancy-based installment payments**						

* See the second row of this table for treatment of these payments when used to meet a required minimum distribution.

** The rules described for fixed-dollar-amount payments expected to last 10 years or more and payments based on life expectancy apply to the entire payment, including any part of such payment that is used to satisfy a required minimum distribution.

