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PENSION ANALYST COMPLIANCE BULLETIN



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IRS provides new safe harbors for validating rollover contributions

On April 3, 2014, the IRS released Revenue Ruling 2014-9, which provides two simplified safe harbor processes that a plan administrator may use to confirm that a potential rollover contribution is a valid rollover contribution.

Valid rollover contributions

Only eligible rollover distributions may be rolled over tax-free into qualified plans, including 401(a)-qualified plans, 403(b) plans and governmental section 457(b) plans. A distribution must meet two requirements to be an "eligible rollover distribution:"

1. It must be made from an eligible plan or traditional IRA. For this purpose, an "eligible plan" is a 401(a)-qualified plan (401(k), profit sharing, money purchase pension, or defined benefit), a 403(b) plan, or a governmental section 457(b) plan.
2. It must not be an ineligible distribution. Ineligible distributions include: required minimum distributions (RMDs), any payment that is one of a series of substantially equal periodic payments over the lifetime of the participant or the lifetime of the participant and his spouse, and hardship distributions.

When accepting a rollover contribution from an employee or on behalf of an employee, the plan administrator of the receiving plan must reasonably conclude that the contribution is a "valid rollover contribution." If the plan administrator makes such a conclusion but later determines that the contribution is an invalid rollover contribution, the plan will not be disqualified as long as the amount of the invalid rollover and related earnings are distributed as soon as possible.

Existing safe harbor processes for determining validity

In previous guidance, the IRS had indicated that the following actions will result in a "reasonable conclusion" that the rollover contribution is a valid rollover contribution:

- The plan administrator of the distributing plan provides a letter to the administrator of the receiving plan stating that the distributing plan has received a favorable IRS determination letter. *This option is available only if the distributing plan is a 401(a)-qualified plan that is eligible to receive a determination letter. It is not available if the qualified plan uses a prototype document or if the plan is a 403(b) plan or governmental section 457(b) plan.*
- The plan administrator of the distributing plan provides a letter to the administrator of the receiving plan stating that the distributing plan satisfies the 401(a) requirements or is intended to satisfy those requirements and the distributing plan administrator is not aware of any plan provision or operation that would result in disqualification.
- In the situation where a participant makes a 60-day rollover rather than a direct rollover, the participant certifies that to the best of his knowledge: he is entitled to the distribution as an employee and not as a beneficiary; the distribution is not one of a series of substantially equal periodic payments; the distribution was received by the employee not more than 60 days before the date of the rollover; and the entire amount of the contribution would be taxable to the employee if not rolled over. The employee also provides a letter from the administrator of the distributing plan stating that the plan has received a favorable IRS determination letter, as well as a distribution statement that accompanied the check and indicates the gross amount being distributed from the plan to the employee and that 20% was withheld for federal income taxes.

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New safe harbor options

In its most recent guidance, the IRS offers two additional safe harbors for exercising the necessary due diligence to make the reasonable conclusion that a rollover contribution is a valid rollover contribution.

In a situation where the check stub accompanying the direct rollover distribution check identifies the distributing plan and the participant identifies the name of the prior employer, the plan administrator of the receiving plan may access the EFAST2 database and search for the most recently filed Form 5500 for the distributing plan. If line 8a of that Form 5500 does not include code 3C, which would indicate that the plan is not intended to be qualified under Code section 401, 403 or 408, the plan administrator may reasonably conclude that this is a valid rollover contribution.

The second situation involves an employee who delivers to a plan administrator a check from the trustee of his traditional IRA made payable to the trustee of the receiving plan for the benefit of that employee and a check stub that identifies "IRA of Employee" as the source of the funds. The administrator of the receiving plan may reasonably conclude that this is a valid rollover contribution if the participant also certifies that the distribution does not include any after tax amounts and that he will not have reached age 70½ by the end of the year in which the check is issued.

Important Notes:

- A check stub identifying the source of the funds is not necessary if this information is indicated on the check itself.
- Rollovers made electronically will qualify for either of the new safe harbors as long as the distributing plan administrator or IRA trustee provides the required information regarding the source of funds to the administrator for the receiving plan.
- If the distributing plan is not required to file Form 5500 (e.g., SIMPLE IRA, SEP, governmental plan, non-electing church plan, traditional IRA) the EFAST2 records will not be an option for confirming plan status.

These new safe harbors are simply IRS-approved options available to plan administrators. Plan administrators may develop other processes for making reasonable conclusions that a potential rollover contribution is a valid rollover contribution.

Impact on plan administration

This guidance should not have any impact on plan documents or require plan amendments since the process of determining the validity of a rollover contribution is an administrative function that is typically not described in detail in plan documents, including summary plan descriptions (SPDs). However, plan administrators who want to follow this safe harbor guidance when determining whether to accept rollover contributions should update their written procedures, including any procedures used by a third party to make such determinations. In addition, all plan administrators should consider revising paperwork that accompanies eligible rollover distributions to provide the information a receiving plan administrator would look for when applying the new safe harbor rules to validate a rollover contribution.

Eligible rollover distributions processed by Prudential Retirement are accompanied by information identifying the distributing plan. The Outsourced Rollover-In Service provided by Prudential for some plans has acceptable procedures already in place to validate rollovers following existing safe harbor standards. However, we are looking into providing the additional flexibility offered by this new guidance.

Plan sponsors should also be aware that IRS Form 5310, used to request a determination for a terminating plan, was revised in December 2013 to require proof that all rollover contributions received in the year of termination and five previous plan years were received from a qualified plan or IRA. Prudential's Outsourced Rollover-In Service retains supporting documentation for all rollovers that are processed by that service for as long as legally required.

Compliance Bulletin by Prudential Retirement

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