

**ESTIMATING LEAKAGE FROM RETIREMENT
SAVINGS ACCOUNTS**

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION



April 26, 2021
JCX-20-21

CONTENTS

	<u>Page</u>
OVERVIEW	1
I. BACKGROUND ON THE U.S. RETIREMENT SAVINGS SYSTEM.....	2
A. Tax-Preferred Retirement Savings Accounts.....	2
II. OVERCOMING TAX REPORTING LIMITATIONS.....	3
A. Brief Data Description.....	3
B. Estimating the Account Type Generating a Form 1099-R.....	3
III. FLOWS BETWEEN RETIREMENT ACCOUNTS AND INDIVIDUALS.....	5
A. Aggregate Flows by Age and Account Type.....	5
B. Estimates of Leakage.....	7
IV. LIFE EVENTS CORRELATED WITH LEAKAGE.....	11
A. Estimating the Effect of Life Events on Leakage.....	11
APPENDIX A.....	16
APPENDIX B.....	17

OVERVIEW

One of the responsibilities of the staff of the Joint Committee on Taxation (“Joint Committee staff”) is to provide Congress with estimates of the revenue effects of proposed tax legislation. This begins with an economic analysis of the proposal.

Designated retirement savings accounts generally receive favorable tax treatment under the Internal Revenue Code. Contributions to traditional individual retirement accounts (“IRAs”) or employer-sponsored defined contribution plans (“DCs”) are generally accorded tax deferral until funds are withdrawn, while contributions to Roth IRAs or Roth DC plans are made after-tax and subsequent income and gain are generally not subject to income taxation. These tax subsidies are intended to encourage taxpayers to save more for retirement. However, pre-retirement withdrawals are allowed under certain circumstances, subject to certain penalties or additional taxes. Pre-retirement withdrawals from retirement accounts are often referred to as “leakage” from the retirement accounts.

This document¹ summarizes recent work by the Joint Committee staff to better understand contributions to and distributions from retirement accounts, with a particular emphasis on distributions from retirement accounts to pre-retirement age individuals (*i.e.*, leakage).² The base data underlying this analysis were constructed by the Joint Committee staff using 16 years of tax returns and information returns. These data are a new and unique set of nationally representative data on flows between individuals and retirement accounts.³ In this document, the Joint Committee staff reports estimates of leakage among working-age individuals and analyzes the extent to which certain common life events contribute to leakage. The staff estimates that roughly 22 percent of net contributions made by those 50 or younger leaks out of the retirement savings system in a given year and finds that the most prominent factor associated with leakage from retirement accounts is job separation.

¹ This document may be cited as follows: Joint Committee on Taxation, *Estimating Leakage from Retirement Savings Accounts* (JCX-20-21), April 26, 2021. This document is available on the Joint Committee on Taxation website at www.jct.gov.

² The staff of the Joint Committee on Taxation welcomes comments from interested readers who have studied modeling of the Federal individual income tax. Direct comments to Chief of Staff, Thomas A. Barthold, and Deputy Chief of Staff, Robert P. Harvey, Joint Committee on Taxation, 502 Ford House Office Building, Washington, D.C. 20515-6453.

³ For more details, see Lucas Goodman, Kathleen Mackie, Jacob Mortenson, and Heidi Schramm, “Leakage from Retirement Savings Accounts in the U.S.” *National Tax Journal*, forthcoming 2021.

I. BACKGROUND ON THE U.S. RETIREMENT SAVINGS SYSTEM

A. Tax-Preferred Retirement Savings Accounts

Generally, contributions to a qualified employer-sponsored defined contribution plan (*e.g.*, a 401(k) plan) are excludable from income and certain contributions to IRAs are deductible from income, subject to income and contribution limits. Under present law, elective deferrals made to 401(k) or 403(b) plans may not exceed \$19,500 for calendar year 2021. The overall limit for contributions to a DC plan is the lesser of 100% of compensation or \$58,000 (\$64,500 including catch-up contributions) for 2021. Contributions to IRAs are deductible for individuals not covered (and whose spouses are not covered) by a retirement plan at work, up to \$6,000. For individuals covered by a retirement plan at work, IRA contributions are at least partially deductible for individuals in tax units with income below \$76,000 (\$125,000 for married filers). An additional \$1,000 in catch-up contributions are allowed for those age 50 or older. Contributions to Roth accounts, whether employer-sponsored plans or IRAs, are made after-tax.

Distributions from traditional accounts are taxable as ordinary income when withdrawn, while distributions from Roth accounts are generally not taxed upon withdrawal. Both types of accounts are subject to early withdrawal penalties for distributions prior to age 59½, though the basis of Roth accounts can be distributed penalty-free at any age.⁴

⁴ Internal Revenue Code of 1986 (the “Code”) secs. 72, 219, 401-420, and 4973-4975.

II. OVERCOMING TAX REPORTING LIMITATIONS

A. Brief Data Description

The Joint Committee staff maintains a multi-year data set of individuals and their tax data for use in revenue estimates and research on taxpayer behavior. This data set consists of a random sample of five percent of all individuals in the United States age 20 and older from 2003 to 2018 (approximately 140 million individual-year observations). Using the taxpayer's tax identification number, the Joint Committee staff links information from Form 1099-R (Distributions from Pensions, Annuities, Retirement, or Profit-Sharing Plans), Form 5498 (IRA Contribution Information), Form W-2 (Wage and Tax Statement), and Form 1040 (U.S. Individual Income Tax Return). These data provide a picture of individual retirement savings behavior and underly the analysis described in this document.

B. Estimating the Account Type Generating a Form 1099-R

Form 1099-R reports distributions from tax-preferred retirement savings accounts. However, the form does not specify the type of account, beyond indicating whether a distribution is from a traditional IRA (or not). Because proposals to modify the Code related to retirement savings vehicles often differ based on type of account, the unspecified account types on Form 1099-R are a serious shortcoming in the data. To improve the accuracy of revenue estimates for retirement savings proposals, the Joint Committee staff developed an algorithm to use available data to classify 1099-Rs as being generated by an employer-sponsored defined benefit ("DB") or DC plan. (IRAs are readily classified using the check boxes and distribution codes).

The algorithm generates predictions in an "hierarchical" manner. The data used to make a prediction are ordered from those that (if available for a given taxpayer-account pair) would generate a prediction with a high degree of certainty, followed by pieces of information that generate less certain predictions. First, several of the distribution codes reported in Box 7 of Form 1099-R indicate whether the distribution came from a DC plan. This step classifies approximately three percent of 1099-Rs as issued by a DC plan. Second, the "payer name" field occasionally explicitly refers to the type of plan. These might include "defined benefit plan," "401(k) plan," or "cash balance plan." This step classifies approximately three percent of 1099-Rs as being issued by a DC plan and 42 percent by a DB plan. Third, the age distribution of 1099-R recipients for a given plan may reveal the presence of a "required minimum distribution" ("RMD") effect. Such an effect might manifest as a discontinuous increase in withdrawals around age 70½, the age (during this time period) at which taxpayers were required to begin taking RMDs. The Joint Committee staff use the Bee-Mitchell method, a regression-based approach to flag an RMD response by participants of a plan, for the third step.⁵ This step classifies approximately 11 percent of 1099-Rs as issued by a DC plan. The last step involves a machine learning method known as a "cluster analysis." The analysis uses several payer and individual characteristics to categorize a given payer-individual pair as either a DC plan or DB plan. The inputs for the algorithm include the statistic produced as part of the Bee-Mitchell exercise, the share of years with a positive distribution from a given payer, the share of years

⁵ See Adam Bee and Joshua Mitchell, "Do Older Americans Have More Income Than We Think?," SESHD Working Paper No. 2017-39, July 25, 2017.

with a positive rollover, the age of first distribution, the total number of individuals receiving a distribution from the payer, and whether individuals have a partially-taxable distribution in any year. This step results in a classification for all remaining 1099-Rs and, as a fraction of all 1099-Rs, classifies nine percent as reporting distributions from DC plans and 31 percent from DB plans.

III. FLOWS BETWEEN RETIREMENT ACCOUNTS AND INDIVIDUALS

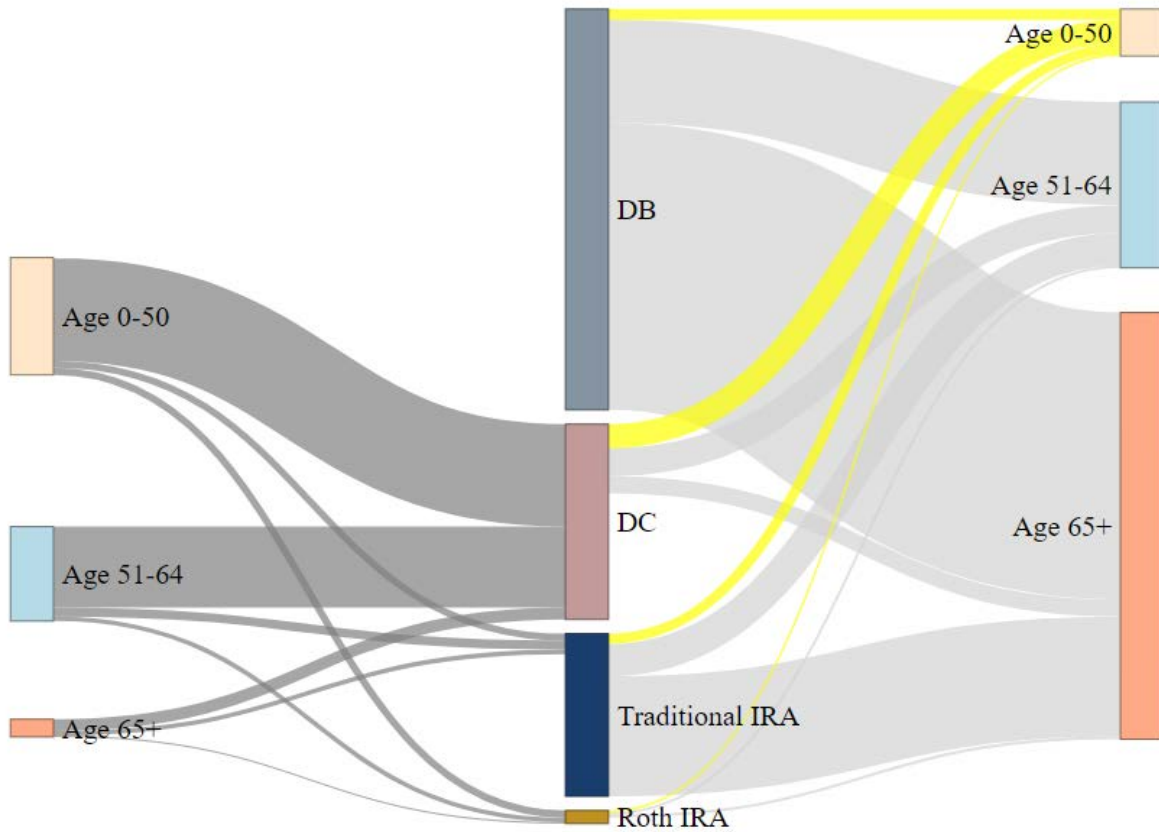
A. Aggregate Flows by Age and Account Type

Using the data set described above, the Joint Committee staff estimates aggregate contributions to and distributions from different types of retirement accounts. These new series of population-level flows of retirement assets are displayed in Figure 1 for tax year 2015 (see Appendix Table A1 for the magnitudes in billions of dollars). Flows are represented by gray areas connecting different origins and destinations (*i.e.*, age groups of individuals or account types). The left half of the chart contains contributions by individuals to different account types; the right half contains distributions from retirement accounts to individuals. Rollovers between accounts are not displayed here but are substantial. For example, most assets in IRAs are rolled in from employer-sponsored plans.⁶ The size of the gray areas is proportional to the magnitude of the flow.

Moving from left to right within the figure, the tax system observes large contributions from individuals age 64 and younger to DC plans, and much smaller contributions directly to IRAs. Notably, the tax system does not observe individual-level employer contributions to employer-sponsored plans, and these are absent from the figure. Despite the noted relative rise of DC plans and decline in DB plans, a higher proportion of retirement distributions to individuals age 51 and older (and 65 and older) are from DB accounts, relative to DC plans and IRAs. The areas connecting DB, DC, Traditional IRA, and Roth IRA boxes with the “Age 0-50” box on the right-hand side (displayed in yellow) are considered leakage for the purposes of the analysis presented here. These distributions are the focus of Section III.B. and Section IV of this document.

⁶ For more details on the magnitude of flows between accounts, see Lucas Goodman, Kathleen Mackie, Jacob Mortenson, and Heidi Schramm, “Leakage from Retirement Savings Accounts in the U.S.” *National Tax Journal*, forthcoming 2021.

Figure 1.—Contributions to and Distributions from Retirement Accounts in 2015



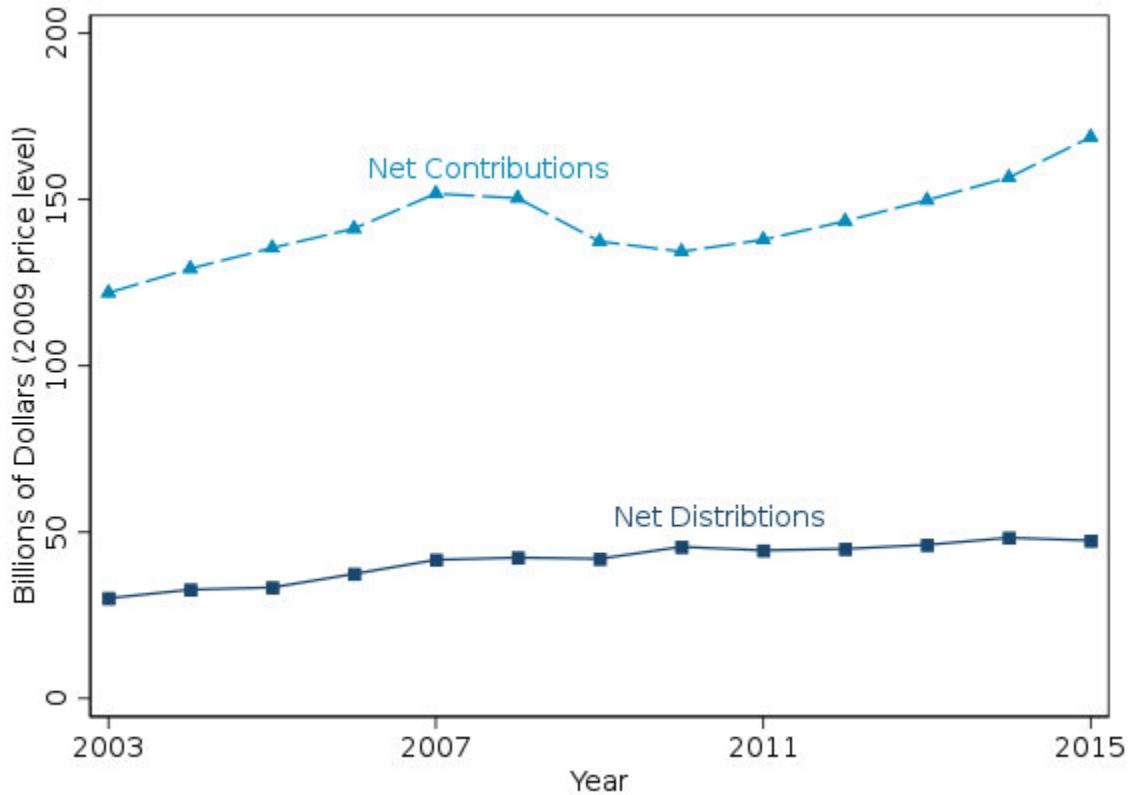
Note: This figure displays flows between retirement accounts and individuals in 2015, as measured in tax records. The magnitude of the lines corresponds with the magnitude of the dollars, which are inflation-adjusted to 2009 price levels. See Appendix Table A1 for the dollar values.

B. Estimates of Leakage

Policymakers are interested in distributions from retirement accounts to pre-retirement age individuals, often referred to as “leakage.” Leakage (as defined in this document) occurs when an individual age 20 to 50 takes DC or IRA distributions that exceed contributions the individual makes to those accounts in the same year. If an individual age 20 to 50 makes more contributions than distributions, his or her net contributions are positive, and his or her net distributions are zero. If an individual age 20 to 50 takes more distributions than contributions, his or her net contributions are zero and his or her net distributions are positive. The population-wide “leakage ratio” each year is the ratio of total net distributions to total net contributions and is expressed in percentage point terms. For example, a leakage ratio of 10 percentage points would imply that for every \$1,000 in net contributions to qualified plans (*i.e.*, \$1,000 more in contributions than distributions) by individuals age 20 to 50 or younger, there are other participants in that age range taking \$100 in net withdrawals.

Figure 2 separately displays annual estimates of total net contributions (for individuals with more contributions than distributions) and total net distributions (for individuals with more distributions than contributions) to and from DC accounts or IRAs. Net contributions are represented by triangles connected by dashed lines, net distributions are represented by squares connected by solid lines. The data used in this graph are restricted to individuals between ages 20 and 50. Total net contributions dipped in 2009-2010 relative to the pre-Great Recession trend and did not regain their 2007 inflation-adjusted level until 2014. Total net distributions, on the other hand, remained relatively on-trend.

Figure 2.—Net Contributions and Net Distributions from 2003 to 2015



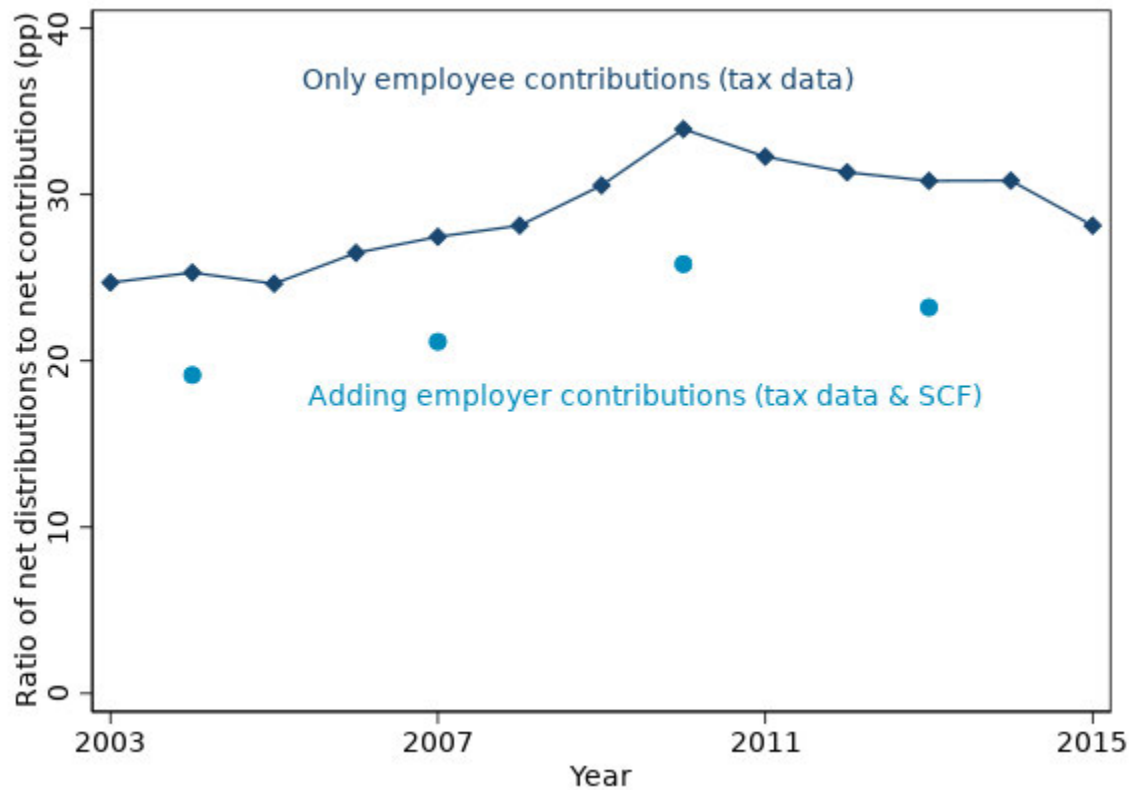
Note: This figure displays net distributions and net contributions from 2003 to 2015. The dashed line is net contributions and the solid line is net distributions. Dollars are adjusted to 2009 price levels.

Figure 3 displays the leakage ratio for the same period as a series of diamonds connected by a solid line. The decline in net contributions and corresponding relative non-response in net distributions caused the leakage ratio (the dashed line series in Figure 2 divided by the solid line series) to increase in 2009-2010 relative to the period immediately preceding the Great Recession. Figure 3 also displays a second series that includes estimates of contributions from employers. No tax filing records individual-level employer contributions to defined contribution plans (employee contributions are reported on Form W-2). To incorporate this source of contributions to DC accounts in measures of leakage, the Joint Committee staff imputes employer contributions using the Survey of Consumer Finance (“SCF”).⁷ This series is displayed as four circles, but without connecting lines, as the SCF is only conducted once every three years (in these data: 2004, 2007, 2010, and 2013). Including estimated employer contributions causes

⁷ See Neil Bhutta, Jesse Bricker, Andrew C. Chang, Lisa J. Dettling, Sarena Goodman, Joanne W. Hsu, Kevin B. Moore, Sarah Reber, Alice Henriques Volz, and Richard A. Windle, “Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances,” *Federal Reserve Bulletin*, vol. 106, no. 5, September 2020.

the denominator (net contributions) of the ratio to increase, lowering the leakage ratio. However, this is mostly a level shift, and both series indicate the leakage ratio increased following the Great Recession.

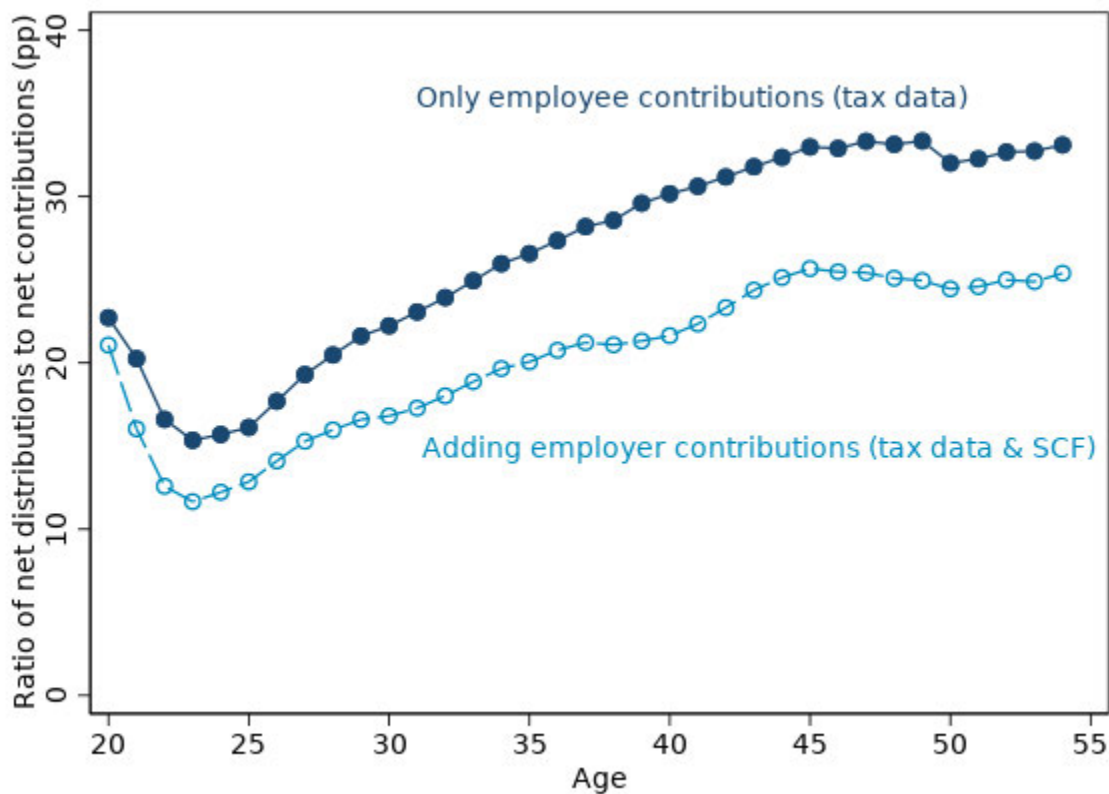
Figure 3.—Leakage Ratio from 2003 to 2015



Note: This figure displays the leakage ratio – the ratio of net contribution to net distributions – from 2003 to 2015. The ratio is expressed in percentage points. The series with diamonds connected by solid lines is constructed using employee contributions found on tax filings for the denominator. The series with dots that is not connected by a line is constructed from contributions found on tax filings augmented with imputed employer contributions from the Survey of Consumer Finance.

Figure 4 displays the leakage ratio – the ratio of net distributions to net contributions – by age, separately for the base series estimated using tax data (solid circles and line) and a series including imputed employer contributions (hollow circles and dashed line). Both series display an initial decline in the leakage ratio for individuals in their early 20s, before steadily increasing for individuals age 25 and above.

Figure 4.–Leakage Ratio by Age



Note: This figure displays the leakage ratio – the ratio of total net distributions to total net contributions – for different age groups. The data underlying this figure are tax records from 2003 to 2015, and data imputed from the SCF for 2004, 2007, 2010, and 2013. The SCF data are imputed for the years they do not cover using a local linear regression, and the resulting series are averages across all individuals in every year from 2003 to 2015.

IV. LIFE EVENTS CORRELATED WITH LEAKAGE

A. Estimating the Effect of Life Events on Leakage

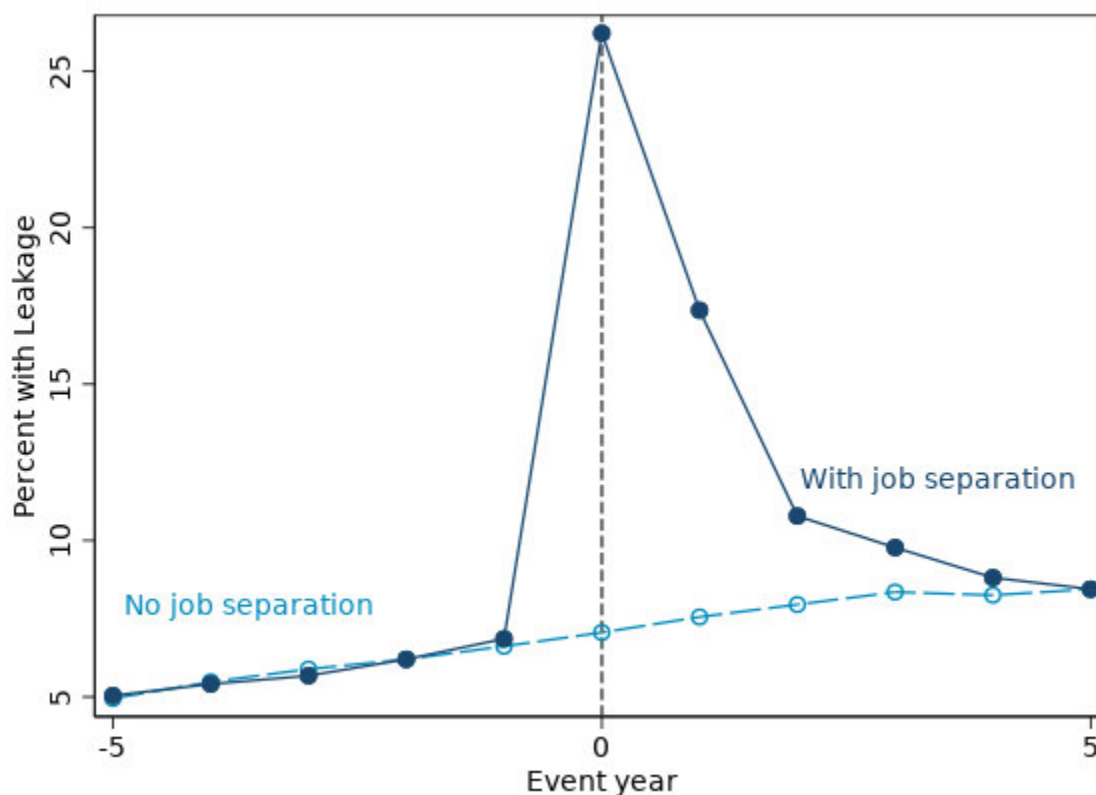
To estimate the correlation between various life events and leakage, the Joint Committee staff uses an event study research design.⁸ This design compares the average levels of an outcome variable for those that experience a given event at time zero to those that do not. In this case, the outcome variable is a binary variable indicating whether a leakage event occurred or not. This approach relies on panel data, as leakage is measured for everyone included in the regression in the years leading up to the life event and the years following.

Leakage for individuals separating from their employer

Figure 5 displays the leakage ratio for individuals changing jobs (solid line and filled circles) along with the leakage ratio for individuals not changing jobs (dashed line and hollow circles). Job separations are determined by examining the W-2s of individuals and recording when most of an individual's wages comes from a different employer from one year to the next. The data in these series are limited to those age 20 to 50. The two series are close to one another until the event time (zero), when the leakage ratio increases discontinuously for those with job separations. The leakage ratio in the year of a job separation is roughly 26 percentage points, relative to a baseline leakage ratio of seven. This difference of 19 percentage points translates to a roughly 270 percent increase in the fraction of individuals experiencing a leakage event. This effect diminishes somewhat the year following a job separation, before returning toward the baseline as years following a job separation pass.

⁸ For an overview of event study designs, see Craig A. MacKinlay, "Event Studies in Economics and Finance." *Journal of Economic Literature*, vol. 35, no. 1, 1997, pp. 13–39.

Figure 5.—Job Separation and Leakage



Note: This figure displays the leakage ratio for those experiencing a job separation (solid line) in year zero to those not experiencing job separations.

The strong correlation between leakage and job separation is consistent with prior research, and with many features of tax-preferred retirement savings in the United States.⁹ Most tax-preferred retirement savings occur in employer-sponsored accounts because retirement savings tax deferral benefits are most generous through employer-sponsored plans (*e.g.*, larger contribution limits), and because employers frequently offer matching contributions. When an employee with one of these accounts separates from an employer, employers can force separating employees with small DC balances (\$1,000 or less) to distribute the balance of their account. While these employees have 60 days to roll this amount into an IRA or other eligible retirement plan, this likely causes some leakage. Regardless of account balance size, a job separation often prompts employees to make an active decision regarding their retirement assets. This can result in individuals deciding to move some of their assets outside of retirement

⁹ See Gene Amromin and Paul Smith, “What explains early withdrawals from retirement accounts? Evidence from a panel of taxpayers,” *National Tax Journal*, Vol. 56, no. 3, September 2003, pp. 3-50; and Robert Argento, Victoria L. Bryant, and John Sabelhaus, “Early withdrawals from retirement accounts during the Great Recession,” *Contemporary Economic Policy*, vol. 33, no. 1, January 2015, pp. 1-16.

accounts. Job separations can also result in reduced income, leading to pre-retirement distributions as a source of consumption smoothing. This may be more likely in the case of unexpected job separations.

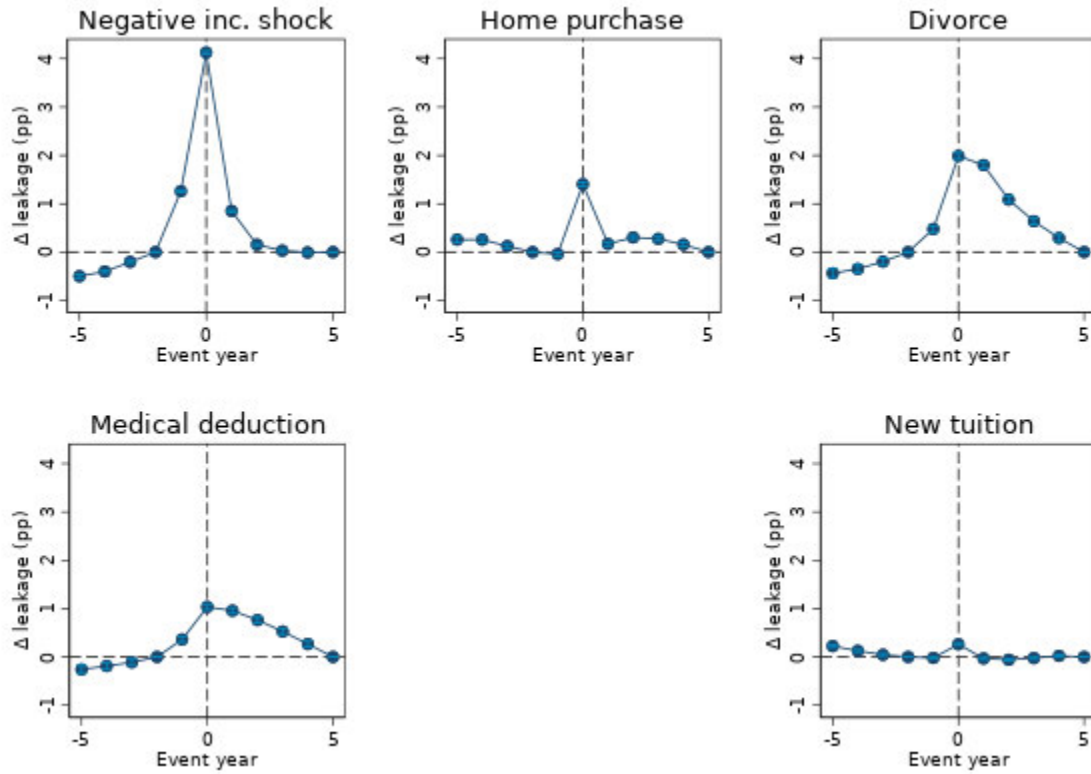
Leakage for other selected life events

Figure 6 is analogous to Figure 5, with a slight variation to allow for a cleaner portrayal of multiple events: instead of separate “event” and “no event” series, Figure 6 displays the difference between the “life event” series and the “no life event” series for five different life events: negative income shocks, home purchase, divorce or separation, medical expense deduction, or new tuition.¹⁰ Each of these can be measured on information returns or tax returns. Of these, the negative income shock, defined here as a reduction in income of at least 40 percent, has the largest effect on leakage. While this event is likely correlated with job separations, the effect is much smaller (four percentage points relative to about 19 percentage points), indicating that job separations are distinctly more likely to lead to leakage.

The other four life events have relatively small effects, and many of them persist after the event. This makes sense to the extent, for example, that a home purchase or new tuition payments leads to longer-term increases in debt payments. In the case of the medical expense deduction, the elevated leakage in years after the event may reflect persistent reductions in health-necessitating drawdowns from (or reduced contributions to) tax-preferred retirement savings vehicles. Finally, many of the events feature a “year before” increase in leakage, consistent with the “shock” spanning multiple years or some amount of anticipation by the taxpayer.

¹⁰ Note that the “no life event” data is comprised of individuals who experience one of these events, but not in that year.

Figure 6.—Other Life Events and the Probability of Leakage



Note: This figure displays the change in the probability – expressed in percentage points – that an individual takes an early withdrawal (exceeding contributions made by the individual in that year) if they experience one of five life events.

IMPLICATIONS OF LEAKAGE FROM RETIREMENT ACCOUNTS FOR JOINT COMMITTEE REVENUE ESTIMATES

The Joint Committee staff's work to identify leakage from retirement accounts permits the staff to separately estimate flows from individual retirement accounts and employer-sponsored defined contribution plans and defined benefit plans. Separately classifying withdrawals by the type of account from which they are distributed directly improves the precision of the Joint Committee staff revenue estimates for proposals affecting tax-preferred retirement savings vehicles.

This analysis has also yielded several pieces of information useful to the Joint Committee staff revenue estimates and to retirement policymakers. First, during the Great Recession, retirement distributions did not meaningfully increase for those under 50, but contributions dipped well below the pre-Great Recession trend. Second, while not visible in the tax system, employer contributions are a non-trivial source of saving for those under 50. Third, job separations are strongly correlated with leakage of assets from designated retirement accounts. This correlation is much stronger than those between leakage and negative income shocks, home purchases, divorce, large medical expenses, or new tuition payments. The evidence emphasizing the role of job separations in leakage suggests that rules related to forced distributions and portability of plans likely affect leakage from retirement savings accounts.

APPENDIX A

Table A-1 summarizes contributions made by individuals or employers to defined contribution accounts, rollovers between different types of retirement savings accounts, and distributions from these accounts to individuals (broken out by the age of the individual). These data underly Figure 1.

Table A-1.—Flows Between Individuals and the Retirement Saving System, 2015

From:	D.B.	D.C.	Trad'l IRA	Roth IRA	Individuals			Employers
					Age 0-50	Age 51-64	Age 65+	
To:								
D.B.	—	—	—	—	—	—	—	—
D.C.	—	—	7.63	—	141.24	111.66	16.34	89.89
Trad'l IRA	32.55	316.70	—	—	9.61	12.14	3.34	—
Roth IRA	0.49	2.36	7.52	—	9.91	6.36	1.64	—
<i>Individuals</i>								
Age 0-50	14.74	33.16	14.01	2.70	—	—	—	—
Age 51-64	141.87	38.74	44.66	3.25	—	—	—	—
Age 65+	395.90	23.18	165.25	3.76	—	—	—	—

Notes: All dollars are values are in billions, and are inflation adjusted to 2009 levels. Blank entries are either unobserved by the tax system or are repeated elsewhere in the table.

APPENDIX B

This appendix contains the Form 1099-R, and its instructions.

☐ CORRECTED (if checked)

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.			1 Gross distribution \$ _____ 2a Taxable amount \$ _____ 2b Taxable amount not determined ☐ Total distribution ☐		OMB No. 1545-0119 2021 Form 1099-R	Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.	
PAYER'S TIN	RECIPIENT'S TIN	3 Capital gain (included in box 2a) \$ _____	4 Federal income tax withheld \$ _____		Copy B Report this income on your federal tax return. If this form shows federal income tax withheld in box 4, attach this copy to your return. This information is being furnished to the IRS.		
RECIPIENT'S name Street address (including apt. no.) City or town, state or province, country, and ZIP or foreign postal code		5 Employee contributions/ Designated Roth contributions or insurance premiums \$ _____	6 Net unrealized appreciation in employer's securities \$ _____				
10 Amount allocable to IRR within 5 years \$ _____		11 1st year of desig. Roth contrib.	12 FATCA filing requirement ☐	14 State tax withheld \$ _____		15 State/Payer's state no.	16 State distribution \$ _____
Account number (see instructions)		13 Date of payment	17 Local tax withheld \$ _____	18 Name of locality		19 Local distribution \$ _____	

Form **1099-R**
www.irs.gov/Form1099R
Department of the Treasury - Internal Revenue Service

Instructions for Recipient

Generally, distributions from retirement plans (IRAs, qualified plans, section 403(b) plans, and governmental section 457(b) plans), insurance contracts, etc., are reported to recipients on Form 1099-R.

Qualified plans and section 403(b) plans. If your annuity starting date is after 1997, you must use the simplified method to figure your taxable amount if your payer didn't show the taxable amount in box 2a. See the instructions for your tax return.

IRAs. For distributions from a traditional individual retirement arrangement (IRA), simplified employee pension (SEP), or savings incentive match plan for employees (SIMPLE), generally the payer isn't required to compute the taxable amount. See the instructions for your tax return to determine the taxable amount. If you're at least age 72, you must take minimum distributions from your IRA (other than a Roth IRA). If you don't, you're subject to a 50% excise tax on the amount that should've been distributed. See Pub. 590-A and Pub. 590-B for more information on IRAs.

Roth IRAs. For distributions from a Roth IRA, generally the payer isn't required to compute the taxable amount. You must compute any taxable amount on Form 8606. An amount shown in box 2a may be taxable earnings on an excess contribution.

Loans treated as distributions. If you borrow money from a qualified plan, section 403(b) plan, or governmental section 457(b) plan, you may have to treat the loan as a distribution and include all or part of the amount borrowed in your income. There are exceptions to this rule. If your loan is taxable, code L will be shown in box 7. See Pub. 575.

Recipient's taxpayer identification number (TIN). For your protection, this form may show only the last four digits of your TIN (SSN, ITIN, ATIN, or EIN). However, the payer has reported your complete TIN to the IRS.

Account number. May show an account, policy, or other unique number the payer assigned to distinguish your account.

Box 1. Shows the total amount distributed this year. The amount may have been a direct rollover, a transfer or conversion to a Roth IRA, a recharacterized IRA contribution; or you may have received it

as periodic payments, nonperiodic payments, or a total distribution. Report the amount on Form 1040, 1040-SR, or 1040-NR on the line for "IRA distributions" or "Pensions and annuities" (or the line for "Taxable amount") and on Form 8606, as applicable. However, if this is a lump-sum distribution, see Form 4972. If you haven't reached minimum retirement age, report your disability payments on the line for "Wages, salaries, tips, etc." on your tax return. Also report on that line permissible withdrawals from eligible automatic contribution arrangements and corrective distributions of excess deferrals, excess contributions, or excess aggregate contributions except if the distribution is of designated Roth contributions or your after-tax contributions or if you're self-employed.

If a life insurance, annuity, qualified long-term care, or endowment contract was transferred tax free to another trustee or contract issuer, an amount will be shown in this box and code 6 will be shown in box 7. If a charge or payment was made against the cash value of an annuity contract or the cash surrender value of a life insurance contract for the purchase of qualified long-term care insurance, an amount will be shown in this box and code W will be shown in box 7. You need not report these amounts on your tax return. If code C is shown in box 7, the amount shown in box 1 is a receipt of reportable death benefits that is taxable in part.

Box 2a. This part of the distribution is generally taxable. If there is no entry in this box, the payer may not have all the facts needed to figure the taxable amount. In that case, the first box in box 2b should be checked. You may want to get one of the free publications from the IRS to help you figure the taxable amount. See *Additional information* on the back of Copy 2. For an IRA distribution, see *IRAs and Roth IRAs*, earlier. For a direct rollover, other than from a qualified plan, section 403(b) plan, or governmental section 457(b) plan to a designated Roth account in the same plan or to a Roth IRA, zero should be shown and you must enter zero (-0-) on the "Taxable amount" line of your tax return. If you roll over a distribution (other than a distribution from a designated Roth account) from a qualified plan, section 403(b) plan, or governmental section 457(b) plan to a designated Roth account in the same plan or to

(Continued on the back of Copy C)

Instructions for Recipient (continued)

a Roth IRA, you must include on the "Taxable amount" line of your tax return the amount shown in this box plus the amount in box 6, if any.

If this is a total distribution from a qualified plan and you were born before January 2, 1936 (or you're the beneficiary of someone born before January 2, 1936), you may be eligible for the 10-year tax option. See the Form 4972 instructions for more information.

If you're an eligible retired public safety officer who elected to exclude from income distributions from your eligible plan used to pay certain insurance premiums, the amount shown in box 2a hasn't been reduced by the exclusion amount. See the instructions for your tax return for more information.

Box 2b. If the first box is checked, the payer was unable to determine the taxable amount and box 2a should be blank, except for an IRA. It's your responsibility to determine the taxable amount. If the second box is checked, the distribution was a total distribution that closed out your account.

Box 3. If you received a lump-sum distribution from a qualified plan and were born before January 2, 1936 (or you're the beneficiary of someone born before January 2, 1936), you may be able to elect to treat this amount as a capital gain on Form 4972 (not on Schedule D (Form 1040)). See the Form 4972 instructions. For a charitable gift annuity, report as a long-term capital gain as explained in the Instructions for Form 8949.

Box 4. Shows federal income tax withheld. Include this amount on your income tax return as tax withheld, and if box 4 shows an amount (other than zero), attach Copy B to your return. Generally, if you receive payments that aren't eligible rollover distributions, you can change your withholding or elect not to have income tax withheld by giving the payer Form W-4P.

Box 5. Generally, this shows the employee's investment in the contract (after-tax contributions), if any, recovered tax free this year; the portion that's your basis in a designated Roth account; the part of premiums paid on commercial annuities or insurance contracts recovered tax free; the nontaxable part of a charitable gift annuity; or the investment in a life insurance contract reportable under section 6050Y. This box doesn't show any IRA contributions. If the amount shown is your basis in a designated Roth account, the year you first made contributions to that account may be entered in box 11.

Box 6. If you received a lump-sum distribution from a qualified plan that includes securities of the employer's company, the net unrealized appreciation (NUA) (any increase in value of such securities while in the trust) is taxed only when you sell the securities unless you choose to include it in your gross income this year. See Pub. 575 and Form 4972. If you roll over the distribution to a designated Roth account in the same plan or to a Roth IRA, see the instructions for box 2a. For a direct rollover to a designated Roth account in the same plan or to a Roth IRA, the NUA is included in box 2a. If you didn't receive a lump-sum distribution, the amount shown is the NUA attributable to employee contributions, which isn't taxed until you sell the securities.

Box 7. The following codes identify the distribution you received. For more information on these distributions, see the instructions for your tax return. Also, certain distributions may be subject to an additional 10% tax. See the Instructions for Form 5329.

- 1—Early distribution, no known exception (in most cases, under age 59½).
 - 2—Early distribution, exception applies (under age 59½).
 - 3—Disability.
 - 4—Death.
 - 5—Prohibited transaction.
 - 6—Section 1035 exchange (a tax-free exchange of life insurance, annuity, qualified long-term care insurance, or endowment contracts).
 - 7—Normal distribution.
 - 8—Excess contributions plus earnings/excess deferrals (and/or earnings) taxable in 2021.
 - 9—Cost of current life insurance protection.
 - A—May be eligible for 10-year tax option (see Form 4972).
 - B—Designated Roth account distribution.
- Note:** If code B is in box 7 and an amount is reported in box 11, see the Instructions for Form 5329.
- C—Reportable death benefits under section 6050Y.
- D—Annuity payments from nonqualified annuities that may be subject to tax under section 1411.
- E—Distributions under Employee Plans Compliance Resolution System (EPCRS).

(Continued on the back of Copy 2)

Instructions for Recipient (continued)

F—Charitable gift annuity.

G—Direct rollover of a distribution to a qualified plan, a section 403(b) plan, a governmental section 457(b) plan, or an IRA.

H—Direct rollover of a designated Roth account distribution to a Roth IRA.

J—Early distribution from a Roth IRA, no known exception (in most cases, under age 59½).

K—Distribution of traditional IRA assets not having a readily available FMV.

L—Loans treated as distributions.

M—Qualified plan loan offset.

N—Recharacterized IRA contribution made for 2021 and recharacterized in 2021.

P—Excess contributions plus earnings/excess deferrals (and/or earnings) taxable in 2020.

Q—Qualified distribution from a Roth IRA.

R—Recharacterized IRA contribution made for 2020 and recharacterized in 2021.

S—Early distribution from a SIMPLE IRA in first 2 years, no known exception (under age 59½).

T—Roth IRA distribution, exception applies.

U—Dividend distribution from ESOP under section 404(k).

Note: This distribution isn't eligible for rollover.

W—Charges or payments for purchasing qualified long-term care insurance contracts under combined arrangements.

If the IRA/SEP/SIMPLE box is checked, you've received a traditional IRA, SEP, or SIMPLE distribution.

Box 8. If you received an annuity contract as part of a distribution, the value of the contract is shown. It isn't taxable when you receive it and shouldn't be included in boxes 1 and 2a. When you receive periodic payments from the annuity contract, they're taxable at that time. If the distribution is made to more than one person, the percentage of the annuity contract distributed to you is also shown. You'll need this information if you use the 10-year tax option (Form 4972). If charges

were made for qualified long-term care insurance contracts under combined arrangements, the amount of the reduction in the investment (but not below zero) in the annuity or life insurance contract is reported here.

Box 9a. If a total distribution was made to more than one person, the percentage you received is shown.

Box 9b. For a life annuity from a qualified plan or from a section 403(b) plan (with after-tax contributions), an amount may be shown for the employee's total investment in the contract. It is used to compute the taxable part of the distribution. See Pub. 575.

Box 10. If an amount is reported in this box, see the Instructions for Form 5329 and Pub. 575.

Box 11. The first year you made a contribution to the designated Roth account reported on this form is shown in this box.

Box 12. If checked, the payer is reporting on this Form 1099 to satisfy its Internal Revenue Code chapter 4 account reporting requirement under FATCA. You may also have a filing requirement. See the Instructions for Form 8938.

Box 13. Shows the date of payment for reportable death benefits under section 6050Y.

Boxes 14–19. If state or local income tax was withheld from the distribution, boxes 16 and 19 may show the part of the distribution subject to state and/or local tax.

Additional information. You may want to see:
Form W-4P, Form 4972, Form 5329, Form 8606

Pub. 525, Taxable and Nontaxable Income
Pub. 560, Retirement Plans for Small Business
Pub. 571, Tax-Sheltered Annuity Plans
Pub. 575, Pension and Annuity Income
Pub. 590-A, Contributions to IRAs
Pub. 590-B, Distributions from IRAs
Pub. 721, U.S. Civil Service Retirement Benefits
Pub. 939, General Rule for Pensions and Annuities
Pub. 969, HSAs and Other Tax-Favored Health Plans