Special Tax Notice

Regarding TRSL Payments

There are tax implications for receiving a payment from TRSL.

All payments from TRSL, including refunds of member contributions, withdrawals from Deferred Retirement Option Plan (DROP) and Initial Lump-Sum Benefit (ILSB) accounts, and certain death benefits, are subject to applicable Internal Revenue Service (IRS) rules and regulations.

It is important to consider all the tax implications of any refund or withdrawal you may request from TRSL. This notice contains important information you will need before you decide how to receive your distribution from TRSL.

Eligible rollover distributions

Some payments from TRSL are "eligible rollover distributions." This means that they can be rolled over to a traditional IRA, Roth IRA, a 403(b) tax-sheltered annuity, a governmental 457(b) plan, or another eligible employer retirement plan that accepts rollovers. Payments from TRSL cannot be rolled over to a SIMPLE IRA or a Coverdell Education Savings Account. Your plan administrator should be able to tell you what portion of your payment is a rollover-eligible distribution.

Payments eligible for rollover

- All refunds of sheltered member contributions
- Most DROP and ILSB account withdrawals scheduled over a period of less than 10 years
- Most Option 1 death benefits paid to spouses of deceased members

If you choose a direct rollover of all or any part of your payment that is an eligible rollover distribution, you are not taxed on a payment until you later take it out of the traditional IRA or other eligible retirement plan. Additionally, no income tax withholding is required for any taxable portion of your plan benefits for which you choose a direct rollover.

Special tax rules apply to rollovers to a Roth IRA. The plan administrator is not responsible for assuring your eligibility to make a rollover to a Roth IRA (IRS Notice 2008-30). You should consult a qualified tax advisor if you are interested in rolling over your distribution to a Roth IRA.

Rollover-eligible payments

Direct rollover to a traditional IRA

To have your payment made directly to a traditional IRA (not a SIMPLE IRA or Coverdell Education Savings Account), contact an IRA sponsor (usually a financial institution).

If you are unsure of how to invest your money, you can temporarily establish a traditional IRA to receive the payment. However, in choosing a traditional IRA, you may wish to make sure that the traditional IRA you choose will allow you to move all or a part of your payment to another traditional IRA at a later date, without penalties or other limitations.

For more information on traditional IRAs, see *IRS Publication 590, Individual Retirement Arrangements*, at *www.irs.gov/pub*.

You should consult a tax advisor regarding the payment of an eligible rollover distribution.

Direct rollover to a plan

If your new employer has an eligible employer plan, a 403(b) tax-sheltered annuity, or a governmental 457(b) plan, and you want a direct rollover to that plan, ask the employer's plan administrator whether your rollover will be accepted. An eligible employer plan is not legally required to accept a rollover. If your new employer's plan does not accept a rollover, you can still choose a direct rollover to a traditional IRA. If the employer plan accepts your rollover, the plan may provide restrictions on the circumstances under which you may later receive a distribution of the rollover amount or may require spousal consent for any subsequent distribution. Check with the employer's plan administrator before making your decision.

Direct rollover of a series of payments

If you receive a payment that can be rolled over to a traditional IRA or an eligible employer plan that will accept it, and it is paid in a series of payments covering less than 10 years, your choice to make or not make a direct rollover for a payment will apply to all later payments in the series until you change your election. You are free to change your election for any later payment in the series.

- Distributions of less than $200 will not be rolled over directly by TRSL. If only a portion of the distribution is rolled over, the portion rolled over must be equal to at least $500.
- Distributions of $200 or more can be rolled over by TRSL, but to only one IRA or eligible retirement plan.

Other types of payments that can and cannot be rolled over

After-tax contributions

After-tax contributions made to the plan can be rolled into either a traditional IRA or to certain employer plans that accept rollovers of the after-tax contributions. The following rules apply:

- You can roll over your after-tax contributions to a traditional IRA either directly or indirectly. Your plan administrator should be able to tell you how much of your payment is the taxable portion and how much is the after-tax portion.
    - » If you roll over after-tax contributions to a traditional IRA, it is your responsibility to keep track of, and report to the IRS on the applicable forms, the amount of these after-tax contributions. This will enable the nontaxable amount of any future distributions from the traditional IRA to be determined.
- You can roll over after-tax contributions from an employer plan that is qualified under Internal Revenue Code section 401(a) to another such plan using a direct rollover if the other plan provides separate accounting for amounts rolled over, including separate accounting for the after-tax employee contributions and earnings on those contributions.
- You cannot roll over after-tax contributions to a governmental 457(b) plan. If you want to roll over

What if a rollover-eligible payment is made directly to me?

Rollover-eligible payments made to you are subject to a mandatory 20% income tax withholding. However, distributions of less than $200 will not be subject to the mandatory 20% withholding.

- The payment is taxed in the year you receive it, unless you roll it over to a traditional IRA or eligible retirement plan that accepts rollovers within 60 days of receiving the payment.
- If you do not roll it over, special tax rules may apply.
- In order to roll over 100% of the payment made to you into a traditional IRA or an eligible retirement plan, you must find other money to replace the 20% that was withheld.
- If you roll over only the 80% that you received, you will be taxed on the 20% that was withheld and that is not rolled over.

EXAMPLE: *Your eligible rollover distribution is $10,000, and you choose to have it paid directly to you. You will receive $8,000, and $2,000 will be sent to the IRS as income tax withholding. Within 60 days after receiving the $8,000, you can roll over the entire $10,000 to a traditional IRA or eligible retirement plan. To do this, you roll over the $8,000 you received from TRSL, and you will have to find $2,000 from other sources (your savings, a loan, etc.). In this case, the entire $10,000 is not taxed until you take it out of the traditional IRA or eligible retirement plan.*

When you file your taxes:

If you roll over the entire $10,000, when you file your income tax return you may get a refund of the $2,000 withheld. If, on the other hand, you roll over only $8,000, the $2,000 you did not roll over is taxed in the year it was withheld. When you file your income tax return you may get a refund of part of the $2,000 withheld. (However, any refund is likely to be larger if you roll over the entire $10,000.)

your after-tax contributions to an employer plan that accepts these rollovers, you cannot have the after-tax contributions paid to you first. You must instruct the plan administrator of this plan to make a direct rollover on your behalf.

- ***Once you roll over your after-tax contributions to a traditional IRA, those amounts cannot later be rolled over to an employer plan.***

Payments spread over long periods

You cannot roll over a payment if it is part of a series of equal (or almost equal) payments that are made at least once a year and that will last for your lifetime (or your life expectancy), or your lifetime and your beneficiary's lifetime (or life expectancies), or a period of 10 years or more.

Required minimum payments

For payments beginning in the year you reach age 70½, a certain portion of your payment cannot be rolled over because it is a "required minimum payment" that must be paid to you.

Additional 10% early withdrawal penalty

If you receive a rollover-eligible payment before you reach age 59½ and you do not roll it over, you may have to pay an early withdrawal penalty equal to 10% of the taxable portion of the payment, in addition to the regular income tax.

The 10% early withdrawal penalty does not apply to:

- Payments that are paid after you separate from service with your employer during or after the year you reach age 55.
- Payments that are paid because you retire due to disability.
- Payments that are paid as equal (or almost equal) payments over your life or life expectancy (or your and your beneficiary's lives or life expectancies).
- Payments that are paid directly to the government to satisfy a federal tax levy.
- Payments that are paid to an alternate payee under a qualified domestic relations order (an order issued by a court, usually in connection with a divorce or legal separation).
- Payments that do not exceed the amount of your deductible medical expenses.

For more information on the additional 10% tax, see *IRS Form 5329, Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts* available at *www.irs.gov/pub*.

Special tax treatment for those born before January 1, 1936

If your "eligible rollover distribution" is not rolled over, it will be taxed in the year you receive it. However, if it qualifies as a "lump-sum distribution," it may be eligible for special tax treatment. DROP/ILSB account withdrawals do not qualify as lump-sum distributions. A lump-sum distribution is a payment, within one year, of your entire balance in TRSL that is payable to you because you have reached age 59½ or have separated from service with your employer. For a payment to be treated as a lump-sum distribution, you must have been a participant in TRSL for at least five years before the year in which you received the distribution.

The special tax treatment for lump-sum distributions that may be available to you is described below:

- **10-year averaging:** If you receive a lump-sum distribution and you were born before January 1, 1936, you can make a one-time election to figure the tax on the payment by using "10-year

Federal income tax withholding

MANDATORY withholding

- If any portion of the payment to you is an eligible rollover distribution, TRSL is required by law to withhold 20% of the taxable amount. This amount is sent to the IRS as federal income tax withholding. For example, if you roll over a taxable payment of $10,000, only $8,000 will be paid to you because TRSL must withhold $2,000 as income tax.
- However, when you prepare your income tax return for the year, unless you make a rollover within 60 days (see "60-day rollover option" section on page 2), you must report the full $10,000 as a taxable payment. You must report the $2,000 as tax withheld, and it will be credited against any income tax you owe for the year. There will be no income tax withholding if your payments for the year are less than $200.

VOLUNTARY withholding

If any portion of your payment is taxable but cannot be rolled over, the mandatory withholding rules described to the left do not apply. In this case, you may elect not to have withholding apply to that portion. To elect out of withholding, ask TRSL for the election form and related information.

averaging" (using 1986 tax rates). This often reduces the tax you owe. DROP/ILSB withdrawals are not eligible for 10-year averaging.

- **Capital gain treatment:** In addition, if you receive a lump-sum distribution and you were born before January 1, 1936, and you were a TRSL participant before 1974, you can elect to have the part of your payment that is attributable to your pre-1974 participation in TRSL (if any) taxed as long-term capital gain at a rate of 20%. DROP/ILSB withdrawals are not eligible for capital gain treatment.

There are other limits on the special tax treatment for lump-sum distributions. For example:

- You can generally elect this special tax treatment only once in your lifetime, and the election applies to all lump-sum distributions that you receive in that same year.
- If you have previously rolled over a payment from TRSL, you cannot use this special tax treatment for later payments from TRSL.
- If you roll over your payment to a traditional IRA, you will not be able to use this special tax treatment for later payments from that IRA.
- If you roll over only a portion of your payment to a traditional IRA, this special tax treatment is not available for the rest of the payment.

Additional restrictions are described in *IRS Form 4972, Tax on Lump-Sum Distributions*, which has more information on lump-sum distributions and how you elect the special tax treatment, available at the IRS publication webpage, *www.irs.gov/pub*.

Surviving spouses, alternate payees, and other beneficiaries

In general, the rules summarized in this brochure also apply to surviving spouses and spouses or former spouses who are "alternate payees." You are an alternate payee if your interest in TRSL results from a "qualified domestic relations order," which is an order issued by a court, usually in connection with a divorce or legal separation.

Some of the rules summarized also apply to a deceased member's beneficiary who is not a spouse. However, there are certain exceptions for payments to surviving spouses, alternate payees, and other beneficiaries that should be mentioned.

Exceptions for payments to surviving spouses, alternate payees, and other beneficiaries:

Surviving spouses and alternate payees:

- You have the same distribution choices as the member. Thus, you can have the payment made as a direct rollover or paid to you. If directly paid to you, you can keep it or roll it over yourself to a traditional IRA, Roth IRA, or to another eligible retirement plan that accepts rollovers.

Other beneficiaries:

- You can choose a direct rollover to an IRA that is established to receive the distribution as an inherited IRA.

Surviving spouses, alternate payees, and other beneficiaries:

- Your payment is not subject to the additional 10% tax, even if you are younger than age 59½.
- You may be eligible for the special tax treatment for lump-sum distributions. If you receive a payment because of the member's death, you may be able to treat the payment as a lump-sum distribution if the member met the appropriate age requirements, regardless of whether the member had five years of participation in TRSL. Refer to "Special tax treatment" section.

For additional information

The rules described in this brochure are complex and contain many conditions and exceptions that are not included here. Therefore, you may want to consult a professional tax advisor before you take a payment of your benefits from TRSL. This notice summarizes only the federal tax rules that might apply to your payment. It does not address any applicable state tax rules.

You can find more specific information on the tax treatment of payments from qualified retirement plans in *IRS Publication 575, Pension and Annuity Income*, and *IRS Publication 590, Individual Retirement Arrangements* available at the IRS publication webpage, *www.irs.gov/pub*.

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