July 23, 2019

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Re: Revenue Ruling 2018-17; Withholding and Reporting with Respect to Payments from IRAs to State Unclaimed Property Funds

Dear Ms. Judson, Mr. Evans and Ms. Van Bogaert,

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates your willingness to continue to discuss Revenue Ruling 2018-17 (the "Ruling") with us and hear our recommendations to ensure smooth compliance while reducing any potential negative impacts on savers. We furthermore appreciate the additional time the Internal Revenue Service ("IRS") and the

[1] SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly 1 million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

U.S. Treasury Department provided to comply with the Ruling, which imposes withholding and reporting requirements when our members transfer a shareholder's traditional Individual Retirement Account ("IRA") to a state, pursuant to that state's unclaimed property law. As a follow up to our meeting on February 25, 2019, outlined in this letter are a number of recommendations and clarifications that we believe would help ensure easier compliance with the new reporting and withholding requirements, while at the same time protecting investors' sensitive information and making it more likely that they will be reunited with their unclaimed property.

1. Inclusion of a New Distribution Code on Form 1099-R

Form 1099-R is required to be provided to the taxpayer and the IRS when a distribution is made from an IRA, and the 2019 instructions clarify that transfers of IRAs to state unclaimed property departments under escheat laws must be reported on Form 1099-R. SIFMA recommends the IRS add a new Distribution Code to Box 7 on Form 1099-R to clarify that IRA assets escheated to states are IRA distributions includable in gross income. Adding this new code will allow for better information tracking of escheated IRA assets for both the custodians of these assets and the IRS. Moreover, the code will better facilitate the ability of investors to reclaim their assets from the states. Given the upcoming January 1, 2020 effective date of the Ruling and the time that would be required both for the IRS and holders to update the form and systems to capture the new distribution code, SIFMA proposes that this change be effective on the first of a business year with at least a one-year notice (e.g., January 1, 2021).

2. Relief for Sending Sensitive Information to a Known Bad Address

As you are aware, Form 1099-R contains sensitive investor information, including the investor's taxpayer identification number ("TIN"), account number, and address, among other private financial information. And while some firms may truncate TINs on tax documents and account statements, an informal survey of SIFMA's membership found that almost no firms truncate account numbers. The circumstances under which an investor's IRA assets are being escheated to a state as unclaimed property are such that the individual could have been inactive with respect to the account and/or moved from the address of record for a potentially long period of time, sometimes years or even decades. While not every abandoned IRA is due to a returned-mail event, in those instances in which that is the case, the requirement to mail the form to a known bad address could put sensitive personal and financial information at risk with respect to data protection and privacy concerns. We understand that the concern associated with sending sensitive personal and financial information to a known bad address is not unique to the Form 1099-R; however, we believe it is of greater significance due to the fact that the individual could have been inactive with respect to his/her account and/or have changed addresses for a much longer period of time than in the case of an investor-initiated distribution. This is because much of the activity in retirement account products is generally contributions, and those may not occur on an annual basis. This is in contrast to other forms that may be impacted by investor inactivity; for example, the longest an individual receiving a Form W-2 could be inactive or have moved is likely to only be 365 days or less.

Moreover, the creation and transmission of a Form 1099-R with a known incorrect address exposes the filer to IRS penalties for issuing tax forms with consequential errors. Under Treas. Reg. 301.6722-1, a filer is subject to failure to file penalties for each Form 1099-R issued with consequential errors or omissions. This includes the payee's address. Under escheatment procedures applied by most filers, there are cases where an address provided by an investor is updated on the filer's books and records to reflect updates received from the United States Postal Service National Change of Address ("NCOA") database. Reliance on the database is critical to efforts designed to locate unresponsive investors. However, the language of Treas. Reg. 301.6722-1 suggests that the issuance of a Form 1099-R that reports the NCOA address would subject the filer to tax penalties.

For these reasons, SIFMA requests that the IRS clarify that firms are not required to mail a Form 1099-R to known bad addresses (i.e., an address where mail has been returned undeliverable). To ensure that this relief is granted only when absolutely necessary, SIFMA further recommends that this apply in those instances where the accountholder is considered lost as defined under the Securities and Exchange Commission ("SEC") Exchange Act Rule 17Ad-17 regarding "Lost Securityholders."[2] Moreover, in such instances, firms would still generate the form and comply with all required reporting to the IRS, but would be granted relief from sending sensitive information when there is evidence that the form would not reach its intended destination and could furthermore expose the shareholder to potential fraud (e.g., if such mail falls into the hands of nefarious individuals). While we appreciate the need to furnish reporting documents to individuals, we believe under these specific circumstances it is in the best interests of all stakeholders to shield investors from potential harm.

3. Penalty Relief for De Minimis Discrepancies

The IRAs offered by SIFMA members typically contain securities, which will require liquidation in order to cover the withholding amount due upon escheatment. Applicable SEC requirements utilize a two-day settlement cycle for most broker-dealer securities transactions (hereinafter "T+2"). At the same time, current IRS regulations require that the valuation used to determine withholding tax be based on the account's fair market value "as of the last preceding valuation date prior to the date of distribution."[3] Due to normal market fluctuations, there could be discrepancies between the account's value on liquidation date and the T+2 settlement date, resulting in over- or under-withholding. SIFMA is requesting that the IRS grant penalty relief in

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[2] 17 CFR § 240.17Ad-17 - Lost securityholders and unresponsive payees.
Lost securityholder means a securityholder: (i) To whom an item of correspondence that was sent to the securityholder at the address contained in the transfer agent's master securityholder file or customer security account records of the broker or dealer has been returned as undeliverable; provided, however, that if such item is re-sent within one month to the lost securityholder, the transfer agent, broker, or dealer may deem the securityholder to be a lost securityholder as of the day the resent item is returned as undeliverable; and (ii) For whom the transfer agent, broker, or dealer has not received information regarding the securityholder's new address.

[3] Treas. Reg. §35.3405-1T, Q. F-1.

those instances where there are de minimis discrepancies in withholding because of differences in the liquidation date and settlement date due to market fluctuations. We suggest that the IRS stipulate that for this purpose, a de minimis amount is less than or equal to 5 percent of the amount that was required to be withheld.

4. Exempting Illiquid Securities from Withholding Requirement

SIFMA requests the IRS clarify that illiquid securities are not includible in a designated distribution for purposes of calculating the withholding tax amount on abandoned IRA assets that are escheated to state unclaimed property funds. There may be instances when an IRA holds positions that are thinly traded securities, physical certificates, interval funds that do not liquidate on demand, or other illiquid securities where it can be challenging or impossible to liquidate and thus not possible to collect the full withholding tax amount for the abandoned IRA assets that are escheated to state unclaimed property funds. Notably, many states no longer require or even permit the escheatment of non-freely transferrable securities which does in fact reduce the number of instances in which this could arise; however, there have been instances when certain states, such as New York, ask that the firm create a separate account in the name of the state, transfer the illiquid securities into that account, and hold those escheated assets on behalf of the state. The challenge of withholding in these situations is manifest as the ability to redeem the assets may not be possible and therefore withholding could not occur, absent the IRS' allowing transferal of non-cash assets to satisfy the withholding obligation. There still may be other instances in which a presumed abandoned IRA includes illiquid securities and insufficient cash to satisfy a withholding obligation, as illustrated by the following examples:

- Restricted Securities – Generally, it is noted on the certificate that the security is restricted. In order to have the restriction removed, a letter must be received from the issuer's counsel stating that the restriction can be lifted. This is done after other conditions (i.e., holding period) have been met.
- Delisted Securities – Generally, these are no longer traded on an exchange or over the counter and there is no market on which they can be sold.
- Security without a transfer agent – Generally, this occurs after a security has been delisted (although it can occur simultaneously). In these instances, the company no longer utilizes a transfer agent to handle the recordkeeping of its stock records.

5. Restoring Assets to an IRA

We recognize that the intended goal of this Ruling is not only to collect withholding tax due that might otherwise go permanently unpaid, but also to ultimately reunite investors with their abandoned property. To that end, and to help those IRA owners and their beneficiaries seeking to reclaim their assets and restore the money into an IRA, SIFMA requests that the IRS provide specific rollover relief by adding "The distribution was escheated to a state agency" to the list of approved self-certification reasons for missing the 60-day rollover deadline in Revenue Procedure 2016-47.

Assuming the IRA owner is eligible to reclaim the funds, adding this allowable scenario to the 60-day late rollover certification would help mitigate the negative results of the escheatment.

Furthermore, SIFMA requests that a rollover under these unique circumstances be excluded from the one-rollover-per-year rule. SIFMA believes the conditions of a distribution caused by the escheatment of the assets are similar to that of other involuntary distributions, as described within a May 31, 2017 letter from the Treasury to the Federal Deposit Insurance Corporation ("FDIC"). In that letter, the Treasury highlights an excerpt noting that the legislative history of the Employee Retirement Income Security Act ("ERISA") indicates the 12-month restriction on multiple rollovers was intended to "prevent abuse of a system permitting voluntary transfers."[4]

At our February meeting, the concern was raised by the IRS and Treasury that this could be used as an RMD avoidance scheme, a concern which SIFMA appreciates and would not want to facilitate. In an effort to balance the ability of investors to restore their assets with the prevention of tax avoidance, SIFMA suggests that any accumulated RMDs (based on the originally escheated amount) be excluded from the allowable rollover amount. In other words, individuals would only be able to roll back into an IRA those assets that would not have been an RMD. In order to facilitate this, SIFMA notes that firms would need relief from the provisions under Publication 590-A, which requires that the same property distributed must be the same property rolled over.[5]

Continuing the theme of helping individuals find, reclaim and restore their assets following escheatment, there will be other instances in which a non-spouse beneficiary may want to restore the escheated assets from a deceased owner's IRA to an inherited IRA. However, because inherited IRAs are not currently eligible to be rolled over, they could not benefit from the same relief requested above. In such instances of an involuntary distribution triggered by escheatment, it is our belief that the restriction should not apply. Similarly, as concluded in the May 31, 2017 letter referenced above, we believe the IRS could issue guidance providing the same flexibility to instances of non-spouse beneficiaries seeking to restore the assets to an inherited IRA.

Finally, SIFMA seeks guidance on how to reclaim the federal and state taxes withheld at the time the IRA was escheated. Specifically, can the investor use their personal non-IRA funds to replace only the tax withholding amounts that cannot be reclaimed?

6. Reporting and Withholding in the Case of Deceased IRA Owners

We understand the IRS' concerns relating to lost beneficiaries and we would very much like to work through these issues with the IRS. The short term problem, occasioned by the Revenue Ruling, however, is that where the beneficiaries are unknown, our members cannot report and withhold based on anyone other than the decedent. SIFMA requests the IRS confirm that reporting

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[4] Letter from the Treasury Department to the FDIC, May 31, 2017, regarding the income tax consequences of IRA distributions made from a failed financial institution, https://www.fdic.gov/bank/individual/failed/firstnbc-ira-rollovers-irs-letter-to-fdic.pdf

[5] IRS Publication 590-A, Contributions to Individual Retirement Arrangements (IRAs), p. 24. "The same property must be rolled over. If property is distributed to you from an IRA and you complete the rollover by contributing property to an IRA, your rollover is tax free only if the property you contribute is the same property that was distributed to you."

and withholding occur in the name of the decedent when IRA assets are escheated to states, assuming that the firm either does not know who the beneficiaries are or does not know their address after reasonable attempts to locate them.

We also respectfully request clarification where we have the name of a beneficiary in the account's documentation, but no information on the beneficiary after reasonable attempts to obtain that information. Even where the name of the beneficiary is listed on the account, there is no requirement under current law to collect or keep updated information on that beneficiary where the beneficiary is not a client of the firm. While some firms have practices in place for collecting and maintaining address and TIN information on beneficiaries, we believe that the majority of IRA custodians do not keep that data up to date, because of the expense to the account of doing so, especially where beneficiaries move frequently.

Therefore, under the presumption of the Ruling that any escheatment is a designated distribution from an IRA, SIFMA requests confirmation that Form 1099-R reporting and withholding should occur in the name of the decedent where the IRA custodian, after reasonable diligence, does not have the current address or TIN of the beneficiary. The use of the decedent's name for withholding and reporting will make it relatively easy for beneficiaries, once found, to reclaim the assets from the states, and seek a refund from the IRS. Furthermore, the later found beneficiary would have a much more difficult time attempting to reclaim the taxes withheld where the withholding and reporting occurred in the name of the beneficiary of record since the tax reporting would not match the registration information used to transfer the account assets to the state. Finally, if withholding and reporting occurred in the name of the beneficiary with incomplete information such as a missing TIN, this could result in an increase of penalty notices (e.g. 972CG) for mismatched TINs.

Conclusion

SIFMA greatly appreciates your continued consideration of our questions and requests. We would welcome another opportunity to discuss these issues with you if it would be helpful in your efforts. Please do not hesitate to contact me with any questions at (202) 962-7329 or lbleier@sifma.org, or my colleague Jillian Enoch at (202) 962-7339 or jenoch@sifma.org.

Sincerely,

Lisa J Bleier

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