April 26, 2021

<u>Via Electronic Mail</u>

Mark Mazur
Deputy Assistant Secretary (Tax Policy)
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Re: <u>2022 Draft Forms W-4P and W-4R</u>

Dear Mr. Mazur,

We are writing on behalf of the undersigned organizations to comment on the early release drafts of IRS Forms W-4P and W-4R for the 2022 tax year. These forms are to be used by individuals in connection with income tax withholding from periodic payments and nonperiodic distributions from their retirement plans, IRAs, and commercial annuities. We urge you to make the following changes to the forms:

- *Simplicity* – The draft Form W-4P should be simplified considerably. The draft is very complicated for individuals to use, many of whom are seniors. We are concerned that they will have tremendous difficulty understanding and completing the form.
- *Payor obligations* – The draft Form W-4P imposes significant new administrative burdens that appear to be inconsistent with long-standing regulations. The form should be revised to eliminate the inconsistency and reduce burdens.
- *Elections out* – The draft Forms W-4P and W-4R obscure individuals' statutory rights to elect out of withholding. A check-box should be restored to appropriately reflect the importance that Congress has assigned to these rights.
- *Flexibility* – Payors should have more flexibility to develop user-friendly electronic interfaces as substitutes to the paper forms.
- *Guidance on Form W-4R* – Guidance is needed on certain issues involving Form W-4R, regarding how to handle earlier withholding elections for nonperiodic distributions on Form W-4P and certain issues relating to escheated distributions.
- *Effective date and penalty relief* – The effective date of the new forms should be delayed until the 2023 tax year in order to provide at least one full calendar year for implementation, and penalty relief should be provided for inadvertent errors that payors may make after the established deadline if they act in good faith to comply by then.

We believe these changes can be made while furthering the goal of accurate withholding. Our comments are discussed further below.

(1) <u>Simplify the Form W-4P for Individuals</u>

The Treasury Department and IRS should adopt a simpler approach to Form W-4P for withholding from periodic payments. The early release draft would require individuals to input a significant amount of personal financial information and perform numerous calculations that are not required on the prior versions of the form. Although much of that information is relevant to worksheets that have been included in the instructions to prior versions of the form, completing those worksheets has been voluntary and the individual – not the payor – retained any completed worksheets in their records.[1] We are concerned that mandating the inclusion of this information on the form will confuse individuals and encourage them to either not complete the form at all or to elect out of withholding, neither of which is preferable to a completed form if accurate withholding is the goal. Indeed, the regulations provide a much easier path for seniors to take – simply elect out of withholding in any manner that demonstrates their intent to do so.[2] Electing out could result in under-withholding and penalties, while ignoring the form and thus triggering the default withholding rule could result in unnecessary withholding of money that seniors need. These outcomes can be expected if the only way to avoid them is to deal with a complicated IRS form.

In that regard, in our collective experience recipients of periodic payments often are elderly retirees who have difficulty dealing with complicated IRS forms. They often find the current and prior versions of the form confusing. Adding requirements and steps to the form will only exacerbate this. Seniors may ask their payors for advice on how to complete the forms, but payors cannot provide such advice and generally can help only by explaining the general rules and directing them to the proper forms. We urge the Treasury Department and IRS to take these points into account and simplify the form.

This could be accomplished in a way that encourages withholding, for example by allowing individuals to choose to withhold from periodic payments at a specified alternative rate, or at a rate corresponding to their expected income from a table of marginal tax rates like the table already set forth in the draft Form W-4R for nonperiodic distributions. In our experience, retirees who are receiving periodic payments typically possess a fundamental sense as to which tax bracket they fall into, so this approach could both simplify the process and encourage adequate withholding. Simplifying the form also would be consistent with recent congressional efforts to simplify tax filings for seniors.[3]

(2) <u>Reduce Burdens on Payors and Ensure Consistency with Current Regulations</u>

The early release draft Form W-4P would require payors of pensions and other periodic payments to make complex withholding calculations that reflect the individual's other sources of income. This would be a sea change in the obligations placed on payors, requiring in some cases extensive and costly changes to existing systems, procedures, and personnel training. The approach also appears to be inconsistent with a Treasury Department regulation that has been on the books for almost 40 years. Specifically, Treas. Reg. section 35.3405-1T, B-1, asks whether "the payor of periodic payments [is] required to aggregate such payments with a payee's compensation to determine the amount of tax to be withheld under section 3405(a)(1)?" The regulation answers "no," as follows:

> Although the payor must withhold from any periodic payment the amount that has to be withheld if the payment were a payment of wages by an employer to an employee for a payroll period, <u>the amount to be withheld</u>

[1] Requiring individuals to share personal financial information with a payor could raise serious privacy concerns. The instructions to the draft Form W-4P acknowledge this by directing individuals to an online tool if they have such concerns. Still, many seniors may be uncomfortable using the online tool.

[2] *See*, *e.g.*, Treas. Reg. section 35.3405-1T, D-22.

[3] *See*, *e.g.*, Pub. L. No. 115-123 § 41106 (2018) (directing Treasury to develop a new Form 1040SR for seniors, including to provide them with a simpler way to reflect retirement distributions on their tax returns).

> under section 3405(a)(1) is calculated separately of any amounts that actually are wages to the payee for the same period. (Emphasis added.)

In other words, the regulation suggests that payors are required to calculate withholding for periodic payments based only on the amount of the periodic payments they make. At a minimum, the regulation means that if an employer is paying two types of income (wages and periodic retirement payments) to the same individual, and thus has independent knowledge of both types, the payor nonetheless is not required to aggregate those two types to determine the amount to withhold from the retirement payments. If a payor that independently knows about two sources of income for a particular payee is not required to aggregate those sources, it seems incongruous to require payors who do not have such independent knowledge to do so.

Unfortunately, the draft Form W-4P and accompanying payor worksheet would do exactly that. For the first time, payors would be required to undertake calculations that aggregate a payee's multiple sources of income when determining how much to withhold from the periodic payments the payor actually makes. Although the instructions to the current and prior versions of the form included worksheets that *individuals* could use to assess whether *they* should reduce their number of withholding allowances or request additional withholding as a result of their other sources of income, those worksheets *did not require the payor to do any aggregating of income sources*. Thus, the current and prior versions of the form have not been inconsistent with the regulations. The new draft suffers from this inconsistency and should be revised to eliminate it, along with the associated new and substantial burdens it would place on payors.

(3) Do Not Obscure Individuals' Statutory Right to Elect Out

Congress explicitly gave individuals the statutory right to elect out of withholding for periodic payments and nonperiodic distributions under Code sections 3405(a)(2) and (b)(2), respectively. The current and prior versions of Form W-4P appropriately recognized this by including a check-box on the form for individuals to exercise their statutory right. The check-box has been placed at the beginning of the form, which makes perfect sense because the rest of the form is irrelevant for individuals invoking this right.

In contrast, the new draft Forms W-4P and W-4R omit a dedicated space on the form for the election. If an individual wants to elect out of withholding for periodic payments, they would be required to hand-write "no withholding" on the bottom of Form W-4P in a place that is not identified in any way as an input field. Similarly, if an individual wants to elect out of withholding for a nonperiodic distribution, they would be required to write "0%" as the withholding percentage rather than being able to check a simple box, and the form itself does not make it obvious that this is how an individual elects out of withholding.[4]

These proposed changes to the forms would obscure the statutory right that Congress gave individuals to elect out of withholding. In our view, de-emphasizing this right is inconsistent with congressional intent. Congress thought the right was so important that *payors are required to notify payees of the right and are penalized if they fail to do so*. The IRS forms should devote similar

---

[4] The new draft Form W-4R allows individuals who receive a nonperiodic or eligible rollover distribution simply to select an alternate percentage for withholding (subject, of course, to the minimum 20% in the case of an eligible rollover distribution). As noted earlier, in our experience taxpayers have a fundamental sense as to which tax bracket will apply to their distribution. Accordingly, we strongly support the decision to allow individuals to specify a withholding percentage on Form W-4R.

importance to this statutory right by restoring the check-box, which should appear at the beginning of each form to make it clear that the rest of the form is irrelevant for any individual who has decided to elect out. We also observe that the long-standing Treasury regulations state that payees may elect out of withholding "in any manner that clearly shows the payee's intent."[5] As an example of this permissive standard, the regulations indicate that marking a check box on a payor's notice of the right to elect out will suffice. Thus, a payee need not use Form W-4P at all to elect out. This makes it even stranger that the draft form obscures the right to elect out.

(4) Allow More Flexibility for Electronic Systems

The cover pages for the latest early release drafts of Forms W-4P and W-4R state that any web-based or other electronic system that payors develop as a substitute for the paper form must "exactly replicate" the text and instructions from the face of the paper form. This requirement appears to be more stringent than long-standing guidance on electronic substitutes for Form W-4P.[6] As such, it would inhibit the ability of retirement plans and financial institutions to develop interfaces that are substantively identical to the paper form but more user-friendly. For example, it would help the user if the online interface could start by asking if the individual wants taxes withheld and by explaining the potential implications of answering no. If the individual answers no and thus invokes their statutory right to elect out, the online interface would not seek any further information that is not necessary for the election out.

If the online interface must "exactly replicate" the paper form, and the paper Form W-4P relegates the election out to the end of the form, individuals presumably would need to work through the entire online interface before getting to the place where they can exercise their right to elect out. This makes little sense, is inconsistent with the regulatory withholding notice requirements mentioned above, and is bound to confuse individuals or force them to undertake complex steps that ultimately are unnecessary to execute their intended withholding election. A better standard would be to require that electronic systems provide the same information to the payor even if formatted or ordered differently. Such a standard would be consistent with long-standing guidance and facilitate an approach such as the one outlined above, thus potentially improving the user experience and helping reduce the risk of confusion. It also would avoid forcing payors to modify their electronic systems each time the IRS and Treasury Department make minor changes to the paper forms.

(5) Clarifications for Form W-4R

Guidance is needed on how payors should handle withholding elections for nonperiodic distributions that individuals previously provided on a Form W-4P that remains in effect after the new Form W-4R is finalized. There should be a way for such elections – including an election of a flat dollar amount of additional withholding – to remain in effect unless and until the individual provides a Form W-4R to the payor; otherwise, they may be subject to the default withholding rule despite their intent to elect additional withholding. If the IRS plans to offer an optional "computational bridge" for Form W-4R as with Form W-4P, that guidance also should be issued as soon as possible. Finally, guidance is needed with respect to the withholding requirements when an individual has elected

---

[5] *See*, *e.g.*, Treas. Reg. section 35.3405-1T, D-22.

[6] *See* Announcement 99-6, 1999-1 C.B. 352 (stating that the electronic substitute "must provide the payer with exactly the same information as the paper Forms W-4P" but that any hard copies the payor is required to provide to the IRS "need not be a facsimile of" the paper form). Thus, the focus is on the information that the electronic substitute collects for the payor, not on the formatting, ordering, or other details of the substitute form.

withholding on Form W-4R at a rate of less than 10% and an amount is subsequently escheated to a state unclaimed property fund.

(6) Effective Date and Penalty Relief

Our organizations have serious concerns regarding the effective date for the new forms. In many ways, the new forms reflect an entirely new withholding regime for periodic payments and nonperiodic distributions under section 3405. Implementing the new regime will be complex, time consuming, and costly for many payors. They will need to make substantial modifications to systems, practices, procedures, documents, and training. In some cases, state regulatory approval may be needed for changes. Payors will need significant lead-time to complete these tasks before they can reasonably be expected to implement the new forms. For these reasons, the effective date of the new forms should be delayed until the 2023 tax year in order to provide at least one full calendar year for implementation. In addition, temporary penalty relief (such as through 2024) should be provided for inadvertent errors that payors may make in implementing the new withholding regime, if they act in good faith to comply by the established deadline.

* * * * *

Thank you for considering these issues. Please do not hesitate to contact any of the undersigned organizations if you have any questions.

American Benefits Council
American Council of Life Insurers
American Retirement Association
Committee of Annuity Insurers
Insured Retirement Institute
Investment Company Institute
The SPARK Institute

cc: Kimberly Clausing, Treasury Department
Edith Brashares, Treasury Department
Amber Salotto, Treasury Department
Adam Isben, Treasury Department
Adam Cole, Treasury Department
Lauson Green, IRS
Jennifer Mitchell, IRS
Kara Soderstrom, IRS
Michael Ecker, IRS
Diane McGowan, IRS
Alan Plumley, IRS
Tuawana Pinkston, IRS
Wendy Jing, IRS
Maria Staggers, IRS
Angela Jones, IRS