TO BE PUBLISHED IN THE OFFICIAL REPORTS

OFFICE OF THE ATTORNEY GENERAL
State of California

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| OPINION | : | No. 80-219 |
| of | : | July 22, 1980 |
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SUBJECT: REPORTING OF ACCUMULATED CONTRIBUTIONS—The California Public Employees' Retirement System (PERS) is required to report a refund to a member of accumulated contributions totalling $600 or more on IRS Form 1099R.

The Honorable Carl J. Blechinger, Executive Officer, Board of Administration of the California Public Employees' Retirement System (PERS), has requested an opinion on the following question:

When PERS pays to a member a refund of accumulated contributions (which includes interest) credited to the member's account, is the System obligated to report the payment to the United States Internal Revenue Service, and if so, is it to be reported on IRS Form 1099–INT or 1099R?

CONCLUSION

PERS is required to report a refund to a member of accumulated contributions totalling $600 or more on IRS Form 1099R.

## ANALYSIS

The Public Employees' Retirement Law (Gov. Code, tit. 2, div. 5, Pt. 3, § 20000 *et seq.*)[1] is designed to provide a comprehensive retirement system consisting of retirement compensation (pt. 3, ch. 9, art. 2, § 21250 *et seq.*), disability benefits (pt. 3, ch. 9, art. 3, § 21290 *et seq.*), and death benefits (pt. 3, ch. 9, art. 5, § 21360 et.seq.) "whereby employees who become superannuated or otherwise incapacitated may, without hardship or prejudice, be replaced by more capable employees. . . ." (§ 20001; *Cf.* § 20036.) Its pension system "serves as an inducement to enter and continue in [public] service (*Phillipson v. Board of Administration* (1970) 3 Cal. 3d 32, [49]) and [its] provisions for disability retirement are also designed to prevent the hardship which might result when an employee who, for reasons of survival, is forced to attempt performance of his duties when physically unable to do so." (*Quintana v. Board of Administration* (1976) 54 Cal. App. 3d 1018, 1021.)

The management and control of the System is vested in a Board of Administration which presently consists of 11 members (§§ 20100, 20103).

PERS members (e.g., employees of the state or local public agencies (§§ 20012, 20013, 20450, 20580)) have a portion of their monthly compensation placed in a Public Employees' Retirement Fund, according to an applicable rate established by the Board in accordance with chapter 5 of part 3. (§§ 20600, 20680–20684.) The state and other public employers also make a monthly contribution according to formulae. (Pt. 3, ch. 6, § 20740 *et seq*.) The Board has "exclusive control of the administration and investment of the [Public Employees'] Retirement Fund." (§ 20201.) The Board is charged to "credit all contributions . . . with interest at the current annual interest rate, compounded at each June 30th" (§ 20131) and to post each member's contribution together with that interest to the individual account of the member (§ 20684, *Cf.* § 20026).

When a person's membership in PERS is discontinued, as for example on a state employee's resignation or involuntary termination, he may either elect to leave his accumulated contributions on deposit in the Retirement Fund, or he may "terminate his membership or resign from [the] system . . . [and demand that he] be paid his accumulated contributions. . . ." (§ 20652[2]; see also § 20393.) Since "accumulated contributions" is

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[1] All preliminary statutory references herein are to the Government Code.

[2] Section 20652 reads in full as follows:

"If the state service or membership herein, of a member is discontinued except by death on account of which a basic, a limited, or a special death benefit is payable or by retirement, or his membership is terminated or he elects to terminate his membership or resign from this system pursuant to this part, he shall, six months after date of

defined to mean the "accumulated normal contributions plus any additional contributions standing to the credit of a member's account" (§ 20031) and since "accumulated normal contributions" includes the interest thereon (§ 20029) as does "accumulated additional contributions" (§ 20030), the sum to be refunded consists of all monies that the member contributed to PERS during his tenure, together with the appropriate interest. This refund of accumulated contributions is an integral "benefit" of PERS. (§ 20036.)

Since section 6049 of the Internal Revenue Code of 1954[3], which requires the reporting of payments of interest[4], does not apply to a state or its agencies or instrumentalities (26 C.F.R. § 1.6049–1 (a) (2); *Cf.* Rev. Rul. 75–133, 1975–1 C.B. 21, 23)[5], question has arisen as to whether PERS, which is embraced within that exclusion as part of the state government (*Cf.* 53 Ops. Cal. Atty. Gen. 4, 5 (1970)), is required to report refund payments at all. We conclude that reporting is required by another section of the Code.

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discontinuance, termination, or resignation, be paid his accumulated contributions upon his demand, except that if he is credited with less than five years of state service, or is credited with five years or more of state service and has not elected to allow it to remain in the retirement fund, and, in the opinion of the board, is permanently separated from state service by reason of such discontinuance, he shall be paid forthwith all of his accumulated contributions."

[3] All further statutory reterences are to the United States Internal Revenue Code of 1954 which constitutes title 26 to the United States Code and likewise title 26, U.S.C.A. under the same arrangement and section numbering.

[4] Section 6049 provides as follows:

"(a) Requirement of reporting.—

(1) In general.—Every person—

(A) who makes payment of interest (as defined in subsection (h)) aggregating 510 or more to any other person during any calendar year,

(B) . . . , or

(C) . . .

shall make a return according to the forms or regulations prescribed by the Secretary, setting forth the aggregate amount of such payments and such aggregate amount includible in the gross income of any holder and the name and address of the person to whom paid or such holder."

[5] "The federal tax regulations appear in title 26 or the Code of Federal Regulations. In *Helvering v. Winmill* (1938) US. 79, 83, the Supreme Court said: "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially re-enacted statutes, are deemed to have received congressional approval and have the effect of law." (Footnote omitted.) The interpretations referred to of course are the Revenue Rulings.

Section 6041 of the Code provides that all persons engaged in a trade or business and making certain payments in the course thereof, must report those payments as provided for by the federal tax regulations. The section reads in pertinent part as follows:

> "(a) Payments of $600 or more. All *persons* engaged in a trade or *business and making payment* in the course of such trade or business to another person, of rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, *or other fixed or determinable gains*, profits, and *income* (other than payments to which section 6042 (a) (1), 6044(a) (1), or 6049(a) (1) applies, and other than payments with respect to which a statement is required under the authority of sections 6042(a)(2), 6044(a)(2), 6045, 6049(a)(2), or 6049(a)(3)), of $600 or more in any taxable year, or, in the case of such payments made by the United States, the officers or employees of the United States having information as to such payments and required to make returns in regard thereto by the regulations hereinafter provided for, shall render a true and accurate return to the Secretary or his delegate, under such regulations and in such form and manner and to such extent as may be be prescribed by the Secretary of his delegate, setting forth the amount of such gains, profits, and income, and the name and address of the recipient of such payment." (Emphasis added.)

Section 1.6041 (a) (1) (ii) of the regulations provides that payments of fixed or determinable interest comes within the embrace of section 6041 of the Code,[6] and section 1.6041–1 (b) in conjunction with section 1.6041–1(g) of the regulations provide that the phrase "all persons engaged in a trade or business" used in the Code does include a state, and its instrumentalities such as PERS.[7]

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[6] Section l.6041–1(a)(1) of the regulations provides:

> "(a) General rule. (1) Except as provided in § 1.6041–3, every person engaged in a trade or business shall make an information return for each calendar year with respect to payments made by him during the calendar year in the course of his trade or business to another person of fixed or determinable—
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> "(i) . . .
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> "(ii) Interest . . . and other income aggregating 5600 or more: or
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> "(iii) . . .
>
> [T]he term 'interest', as used in subdivision (ii) of this subparagraph, includes all interest other than that coming within the definition of interest provided in § 1.6049–2."

[7] 2l C.F.R. section 1.6041–1(b) reads in part:

> "(b) Persons engaged in trade or business. The term 'all persons engaged in a trade or business', as used in section 6041(a), includes not only those so engaged for gain or

The types of payments excepted from the operation of section 6041 (a) do not apply to the situation before us. Section 6042 (a) (1) provides for the reporting of dividends aggregating more than $10; section 6044(a) (1), for the reporting of payments by cooperatives of patronage dividends aggregating more than $10; section 6042(a) (2), for the reporting of dividends aggregating less than $10; section 6044(a) (2), for payments by cooperatives of patronage dividends aggregating less than $10; and section 6045, for the reporting by brokers of transactions with customers. Lastly, as we have seen, while section 6049 (a) (1) (A) does impose a requirement of reporting on "every person . . . who makes payments of interest . . . aggregating $10 or more to any other person during any calendar year," the states and their agencies and instrumentalities are excluded from the term "person" as it is used in that section. (26 C.F.R. § 1.6049–1 (a) (2).) Since "interest paid by . . . one of these entitles need not be reported" under section 6049(a) (1) of the Code (*Ibid*.), the section 6049 exemptions from section 6041(a)'s general requirements does not apply to the situation with which we are faced. (See also 26 C.F.R. § 1.6041–1 (a) (1) quoted *supra* at fn. 6.)

We therefore must return to section 6041 (a) to answer the question before us. Here section 1.6041–1 (c) of the implementing regulations defines "fixed or determinable income" as follows:

> "Income is fixed when it is to be paid in amounts definitely predetermined. Income is determinable whenever there is a basis of calculation by which the amount to be paid may be ascertained."

and section 1.6041–1 (f), of those regulations provides:

> "When payment deemed made. For purposes of a return of

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profit, but also Organizations the activities of which are not for the purpose of gain or profit. 'Thus, the term includes the organizations referred to . . . in paragraph (g) of this section." paragraph (g) reads:

"(g) Payments made by the United States or a State. Information returns on—

"(1) Forms 1096 and 1099 and

"(2) Forms W-3 and W-2 (when made under the provisions of § 1.6041–2) of payments made by the United States or a State, or political subdivision thereof, or the District of Columbia, *or any agency or instrumentality of any one or more of the foregoing*, shall be made by the officer or employee of the United States, or of such State, or political subdivision, or of the District of Columbia, or of such agency or instrumentality, as the case may be, having control of such payments or by the officer or employee appropriately designated to make such returns." (Emphasis added.)

> information, an amount is deemed to have been paid when it is credited or set apart to a person without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made, and is made available to him so that it may be drawn at any time, and its receipt brought within his own control and disposition."

Thus, pursuant to section 6041 (a) and its accompanying regulations, PERS is required to report the interest on contributions paid to a member when it becomes fixed or determinable, i.e., when it is paid to the member as part of PERS' refund of his accumulated contributions.

The $600 threshold requirement for the reporting applies to the total payment made of refunded accumulated contributions and not just to the interest portion thereof. In this regard it must be noted that since a member's normal and additional contributions would have previously been taxed in the year they were made to PERS when they were considered part of the member's income from wages and reported as such on the W2 Form (see Rev. Rul. 58–141, 1958–1 G.B. 101, 102–103; Rev. Rul. 56–473, 1956–2 C.B. 22; *Cf. Miller v. Commission of Internal Revenue* (4th Cir. 1944) 144 F.2d 287, 289–290), they are not taxed again when refunded and only the interest portion of the accumulated contributions is subject to tax on its distribution in the refund.

Section 1.6041–1 (a) (2) provides that the information return for such distributions (under 26 U.S.C.A. § 6041 and tit. 26 C.F.R. § 1.6041 (a) (1)), be made on Forms 1096 and 1099. Form 1096 is an Annual Summary and Transmittal Form, Form 1099 covers the actual payments. There are at least a dozen different 1099 forms depending on the type payment made (1099–BCD, 1 (1099–DIV, 1099–F, 1099–INT, 1099–L, 1099–MED, 1099–MISC, 1099–NEC, 1099–OID, 1099–DATR, 1099R, and 1099–UC). It would appear that Form 1099R—which is entitled "Statements For Recipients of Lump-Sum Distributions . . . From Retirement Plans"—is the appropriate form so use to report PERS' refund of a member's accumulated contributions of the $600 or more.[8] Form 1099–INT

[8] Again we note that the 5600 threshold amount for the reporting requirement under section 6041 applies to the entire distribution and not just to the interest portion of it, even though only the latter is subject to tax on a return by PERS of a member's accumulated contributions. Although not reported as income on Form 1099R (in Box 1). PERS' return of a member's normal and additional contributions—which were already taxed and which are not taxed again-must nonetheless be reported (in Box 5), since a distribution of them is now being made. This of course means that a second reporting of those contributions takes place, the first having been when the contributions were taxed as income from wages and reported as such on the W2 Form for the member in the year(s) they were paid to PERS. Such duplicate reporting on different forms and at different times is not unusual because of the deferred nature of an employees trust such as PERS.

The 1099R is actually an informational statement for the member showing the nature of monies

would not be appropriate for reporting of refunds of accumulated contributions since it is designed to accommodate reporting of payments of interest under section 6049, which, as we have mentioned, does not apply to the state or its instrumentalities. The Internal Revenue Service agrees with this conclusion. (Letter of the District Director's representative to this office dated April 9, 1980.)

It is important to note that Form 1099R accommodates reporting payments thereon both as ordinary income (in Box 3) and as a capital gain (in Box 2). In this regard, section 402 (a) (2) provides as follows:

> "(2) Capital gains treatment for portion of lump sum distributions.—In the case of any employee trust described in section 401(a), which is exempt from tax under section 501(a), so much of the total taxable amount (as defined in subparagraph (D) of subsection (e) (4) of a lump sum distribution as is equal to the product of such total taxable amount multiplied by a fraction—
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> "(A) the numerator of which is the number of calendar years of active participation by the employee in such plan before January 1, 1974, and
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> "(B) the denominator of which is the number of calendar years of active participation by the employee in such plan, shall be treated as again from the sale or exchange of a capital asset held for more than 1 year."

For the purpose of section 402(a) (2), the "governmental plan" (§ 414(d)) established by PERS should be treated as a "qualified" pension plan under section 401 with the payment of interest as part of a refund of accumulated contributions from it, being treated as if it was from an "employee's trust" described section 401 (a) which is exempt from tax under section 501 (a).[9] Pursuant to section 402 (a) (2) then, that percentage of the interest distributed equal to the proportion of the member's employment (i.e., participation in PERS) preceding 1974, should be report on Form 1099R as a capital gain (in Box 2). The

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he is receiving in the current year. As such, it shows that his personal contributions, which appear in Box 5 (employee contributions), are not being reported as income or perforce taxed again, since only the interest being paid of them is being reported (in Box 1) as income currently received which is subject to tax. (Compare Its Form 1099, Box 1 ("amount ineludible as income") with Box 5 ("employee contributions") and see Department of the Treasury, Internal Revenue Service, Instructions for Form 1096, p. 4.

[9] It is not necessary for the purposes of this opinion to determine whether the income earned by the Retirement System, an agency of the State of California, on its investments, is exempt from federal taxation on constitutional grounds.

remainder should be reported as ordinary income (in Box 3). (See *Instruction for Form 1096, supra,* at p. 4.)

We therefore conclude that PERS is required to report its refund to a member of accumulated contributions totalling $600 or more, and that such should be accomplished on Internal Revenue Service Form(s) 1096 and 1099R.

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