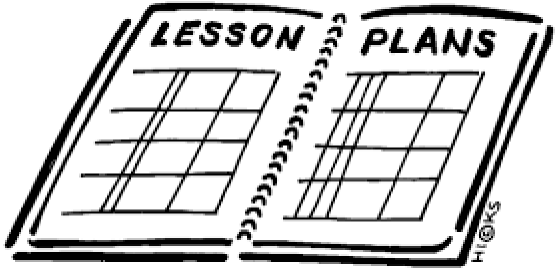
The Potential Liabilities of Loans

2019 Annual Delegates Meeting

Today's Lesson Plan

- Loan Eligibility Requirements
- Benefits of Taking a Loan
- Potential Tax Consequences
- Proposed Change for Tier 6 Loans



Loan Eligibility Requirements

- Have at least one year of member service credit.
- Have a minimum of $1,334 in your Required Contributions Fund (Tiers 3-6).
- Generally, you can borrow up to 75% of the contributions in your Required Contributions Fund.
- Borrow once per calendar year (Tiers 3-6).
- Not have an outstanding System loan more than two months delinquent, in default or in a non-performing status.

Default vs. Non-Performing

- Default status – Loan is four months delinquent. Once a loan is in default status, it remains so until the entire defaulted loan amount is repaid. If payments are received consistently each month, your loan will not move into non-performing status.

- Non-performing – Loan became four months delinquent, and we are not receiving payments consistently each month. The loan may be reportable as income for federal tax purposes.

Benefits of Taking a Loan

- You'll have money needed for the necessary expense.
- Submit your loan online and you may select the direct deposit feature.
- We do not report to any credit agencies or check credit scores.
- Automatic Payroll Deduction
- Payments are not required for the months of July and August.

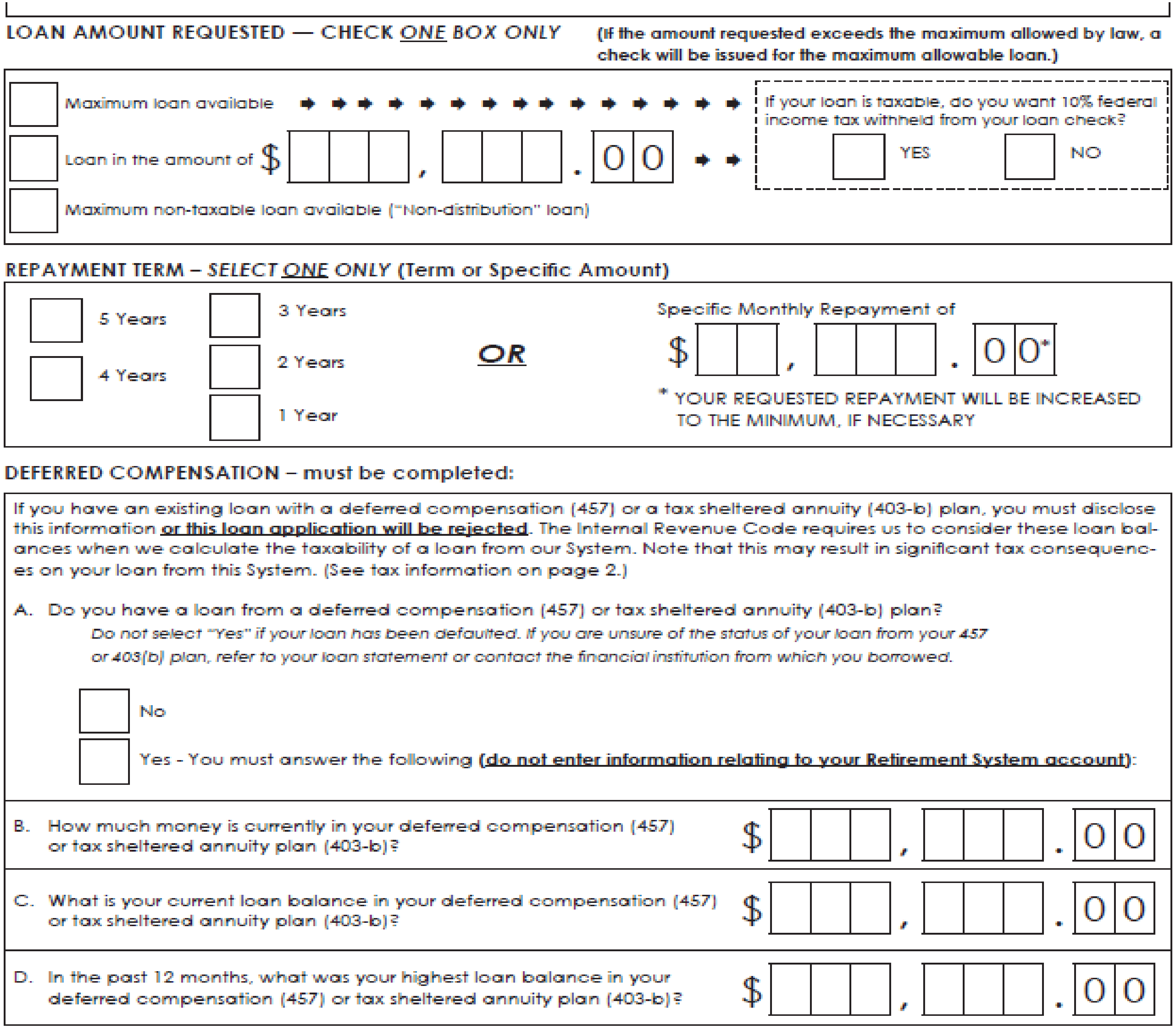
Other Loan Considerations

- Service charge of $30
- Your loan is fully insured beginning 31 days from the date of issuance, with an annual insurance charge of .10%
- Interest Rate – currently 6.25%

Potential Tax Implications

- A loan may be taxable if the total amount borrowed exceeds the limits allowed by the IRS.
- To avoid taxability, your total loan debt must be paid within five years of the date the **original** loan was issued.

Loan Application



LOAN AMOUNT REQUESTED — CHECK *ONE* BOX ONLY (If the amount requested exceeds the maximum allowed by law, a check will be issued for the maximum allowable loan.)

- ☐ Maximum loan available ➔ ➔ ➔ ➔ ➔ ➔ ➔ ➔ ➔ ➔ ➔ ➔ ➔ ➔ ➔
- ☐ Loan in the amount of $ ___ , ___ . 00 ➔ ➔
- ☐ Maximum non-taxable loan available ("Non-distribution" loan)

If your loan is taxable, do you want 10% federal income tax withheld from your loan check? ☐ YES ☐ NO

REPAYMENT TERM – *SELECT ONE ONLY* (Term or Specific Amount)

- ☐ 5 Years
- ☐ 4 Years
- ☐ 3 Years
- ☐ 2 Years
- ☐ 1 Year

OR

Specific Monthly Repayment of $ __ , ___ . 00*

* YOUR REQUESTED REPAYMENT WILL BE INCREASED TO THE MINIMUM, IF NECESSARY

DEFERRED COMPENSATION – must be completed:

If you have an existing loan with a deferred compensation (457) or a tax sheltered annuity (403-b) plan, you must disclose this information **or this loan application will be rejected**. The Internal Revenue Code requires us to consider these loan balances when we calculate the taxability of a loan from our System. Note that this may result in significant tax consequences on your loan from this System. (See tax information on page 2.)

A. Do you have a loan from a deferred compensation (457) or tax sheltered annuity (403-b) plan?

Do not select "Yes" if your loan has been defaulted. If you are unsure of the status of your loan from your 457 or 403(b) plan, refer to your loan statement or contact the financial institution from which you borrowed.

- ☐ No
- ☐ Yes - You must answer the following **(do not enter information relating to your Retirement System account)**:

B. How much money is currently in your deferred compensation (457) or tax sheltered annuity plan (403-b)? $ ___ , ___ . 00

C. What is your current loan balance in your deferred compensation (457) or tax sheltered annuity plan (403-b)? $ ___ , ___ . 00

D. In the past 12 months, what was your highest loan balance in your deferred compensation (457) or tax sheltered annuity plan (403-b)? $ ___ , ___ . 00

Potential Tax Implications

- A loan may be taxable if the total amount borrowed exceeds the limits allowed by the IRS.

- To avoid taxability, your total loan debt must be paid within five years of the date the **original** loan was issued.

Taxability Calculation for a New 5-year Combined Loan

Current loan balance	$ 9,000	(to be paid in full by 12/1/2023)
New loan	+ $ 2,000	
	$11,000	Total combined loan
Service Charge	+ 30	

To test for taxability

Current + New	$ 11,030	
Current balance	+ $ 9,000	Balance of previous loan not paid within original 5-year term (e.g., 12/1/2023)
	$20,030	Total considered when calculating taxability

$ 10,030 Taxable at Issuance

Taxability Calculation for a New 4-year Combined Loan

Current loan balance $ 9,000 (to be paid in full by 12/1/2023)

New loan + $ 2,000

$ 11,000 Total combined loan

Service Charge + 30

To test for taxability

Current + New $ 11,030

+ 0 Balance of previous loan not repaid within original 5-year term (e.g., 12/1/2023)

$ 11,030 Total considered when calculating taxability

$ 1,030 Taxable at Issuance

Taxability Significantly Reduced!

- By changing the term of her new loan from five years to four years, this member was able to reduce the taxable amount by **$9,000**.

- **The trade off:** Because the term is shorter, the monthly payment is higher. Generally, a loan of $11,000 will cost approximately $260 per month for five years. The same loan will cost approximately $310 per month for four years.

Selecting a Specific Monthly Payment

- You have two options when choosing repayment terms:
  - Choosing a fixed term of 1, 2, 3, 4 or 5 years. **OR**
  - Selecting a specific monthly payment amount. By choosing a specific monthly payment, you can control the term length and pay off the loan in the number of months you choose.

How to Arrive at a Monthly Payment Amount that Limits Taxability

- Look for this on the Loan Estimate page in MyNYSTRS.

- Try various scenarios, both for term and specific repayment amount. It is worth the time and effort to explore different options to avoid a large tax liability.

Don't want to pay federal income tax on your loan?
It may be possible to reduce or eliminate the taxability of your loan by choosing a smaller loan amount or a shorter repayment term. For the maximum loan amount that is non-taxable at the time of issuance, try the Maximum Non-Distribution Loan option.

‹ Start Over and Choose Different Options

Taxability Calculation Using a Specific Monthly Payment for a Combined Loan

Member applies for an additional loan in the amount of $ 2,500

Monthly repayment amount:	$ 325
Taxable at issuance:	$ 3,667

OR

Monthly repayment amount:	$ 350
Taxable at issuance:	$ 0

Outstanding Loan in Retirement

- Retiring with an outstanding loan balance will permanently reduce your pension (Tiers 3-6) and create a taxable occurrence.
- Members default if they do not repay the loan within 30 days after their service retirement date.
- All or a portion of the unpaid balance may become subject to federal tax.

Recap: What to Consider When Borrowing from Your Contributions

- When taking a new (combined) loan, the taxable amount is directly impacted by the original loan repayment date.
- Changing the “Repayment Term” or “Monthly Repayment Amount” on your estimates can help limit loan taxability.
- Requesting a smaller loan can also reduce taxability.
- Do multiple loan estimates before deciding on a loan term.
- Consider paying off your loan before you retire.

Loans

- Call for an estimate before you borrow, or use NYSTRS' online loan estimator to see if a loan is taxable, and to test various loan amounts and repayment periods.

- Video on Website (NYSTRS.org):

  Loan Truths…And Consequences

Loans

For eligibility restrictions and other important information, view the *Borrowing From Your Contributions* brochure on NYSTRS.org. Questions? Call (800) 348-7298, Ext. 6080.

Program Bill

- NYSTRS has proposed to limit the amount a Tier 6 member who joins on or after July 1, 2020 can take from their contributions.
- This proposed law would cap the limit at the greater of $10,000 or 50% of the member's total contribution balance OR $50,000, whichever is less.
- This proposed bill was introduced to mirror legislation already passed by the NYSLRS.

Program Bill

Example 1

- Member’s contribution balance = $70,000
  50% of member’s total contribution balance = $35,000

- Member is eligible to borrow $35,000

Program Bill

Example 2

- Member's contribution balance = $150,000
  50% of member's total contribution balance = $75,000
- Member is eligible to borrow $50,000


THANK
YOU!