

Pension Act Waives Required Minimum Distribution For Calendar Year 2009

DECEMBER 17, 2008

BE IN A POSITION OF STRENGTH

The stock market's decline has been cruel to all investors, but doubly so for the millions of people who are required to receive required minimum distributions (RMDs) from qualified retirement plans and IRAs that are invested heavily in stocks or mutual funds. Because of the way in which RMDs are calculated (i.e., based on the previous year's closing value), the law has forced these individuals to receive a disproportionately large portion of their remaining account balance. And they have been forced to sell stock or mutual fund shares at exceptionally depressed values. This double hit affects not only retirees but also beneficiaries of qualified plan accounts and IRAs who must take minimum distributions from the accounts they inherited. The Pension Act (H.R. 7327, the "Worker Retiree and Employer Recovery Act," passed by Congress and ready for the President's expected signature) helps out, but for next year only. More specifically, for calendar year 2009 only, plan account participants and IRA owners don't have to make otherwise required lifetime RMDs; likewise, their beneficiaries also don't have to make minimum distributions.

...Observation: Unfortunately, the Pension Act doesn't help taxpayers with 2008 RMDs. Additionally, it doesn't change the way in which an RMD is calculated, namely based on the retirement account's previous year's closing value.

Background on RMDs under Code 401(a)(9). Employer-provided defined contribution qualified retirement plans, IRAs and individual retirement annuities are subject to RMD rules. Generally, RMDs must begin by the required beginning date (RBD), which usually is April 1 of the calendar year in which the individual (employee or IRA owner) reaches age 70 1/2; however, for employer-provided qualified retirement plans, the RBD for non-5% company owners is delayed to April 1 of the year following the year in which the individual retires. For IRAs and defined contribution plans, the RMD for each year generally is determined by dividing the account balance as of the end of the prior year by a distribution period carried in a uniform table in the regs. Special rules apply to annuity payments from an insurance contract.

2009 RMD RELIEF

Questions or comments?

E-mail us at taxbriefs@withum.com



WithumSmith+Brown, PC
Certified Public Accountants and Consultants
New Jersey, New York, Pennsylvania, Maryland, Florida, Colorado

Pension Act Waives Required Minimum Distribution For Calendar Year 2009

DECEMBER 17, 2008

BE IN A POSITION OF STRENGTH

Minimum distributions after the date of death of the qualified plan participant or IRA owner depend on whether he died before or after his RMD:

...If he dies on or after his RBD, the RMD is determined by dividing the account balance as of the end of the prior year by a distribution period equal to the remaining years of the beneficiary's life expectancy or, if there is no designated beneficiary, a distribution period equal to the remaining years of the deceased individual's single life expectancy, using the age of the deceased individual in the year of death.

..If he dies before his RMD, there are two methods for satisfying the after death RMD rules. Under the life expectancy method, annual RMDs must begin no later than December 31 of the calendar year in which the individual died. This method is only available if the designated beneficiary is an individual (e.g., not the individual's estate or a charity). If the designated beneficiary is the individual's spouse, commencement of distributions can be delayed until December 31 of the calendar year in which the deceased individual would have attained age 70 1/2. The RMD for each year is also determined by dividing the account balance as of the end of the prior year by a distribution period, which is determined by reference to the beneficiary's life expectancy. Under the five-year method, the individual's entire account must be distributed no later than December 31 of the calendar year containing the fifth anniversary of his death. (A special after-death rule applies for an IRA if the beneficiary of the IRA is the surviving spouse. Here, the surviving spouse may choose to calculate RMDs while the spouse is alive, and after the spouse's death, as though the spouse is the IRA owner, rather than a beneficiary).

Roth IRAs. Roth IRAs are not subject to RMD rules during the IRA owner's lifetime, but they are subject to the post-death RMD rules that apply to traditional IRAs. For Roth IRAs, the IRA owner is treated as having died before his RBD. Thus only the life expectancy or five year method apply.

Questions or comments?

E-mail us at taxbriefs@withum.com



WithumSmith+Brown, PC
Certified Public Accountants and Consultants
New Jersey, New York, Pennsylvania, Maryland, Florida, Colorado

Pension Act Waives Required Minimum Distribution For Calendar Year 2009

DECEMBER 17, 2008

BE IN A POSITION OF STRENGTH

Penalty for failure to make RMDs. Failure to take an RMD triggers a 50% excise tax under Code Sec. 4974, payable by the qualified plan participant or IRA owner or his beneficiary. The tax is imposed during the tax year that begins with or within the calendar year during which the distribution was required. The tax may be waived if the distribution did not occur because of reasonable error and reasonable steps are taken to remedy the violation.

Eligible rollover distributions. In general, under Code Sec. 402(c)(4), distributions from an employer-qualified retirement plan may be rolled over tax free into another employer-provided qualified retirement plan or an IRA. This can be done by contributing the amount of the distribution to the other plan or IRA within 60 days of the distribution, or by a direct payment by the plan to the other plan or IRA (direct roll-over). Distributions that are not eligible for rollover include (1) any distribution that is one of a series of periodic payments generally for a period of 10 years or more (or, if a shorter period, certain life expectancies) and (2) any distribution to the extent that the distribution is an RMD.

For any distribution that is eligible for rollover, an employer-provided tax-qualified retirement plan must offer the right to have the distribution made in a direct rollover and, before making the distribution, the plan administrator must provide the distributee with a written explanation of the direct rollover right and related tax consequences. If a distributee does not choose to have the distribution made in a direct rollover, the distribution is generally subject to mandatory 20% income tax withholding.

New law. Under the Act, no RMD is required for calendar year 2009 from individual retirement plans and employer-provided qualified retirement plans that are defined contribution plans (within the meaning of Code Sec. 414(i)). (Code Sec. 401(a)(9)(H), as amended by Pension Act 201(a)) applies to:

Questions or comments?

E-mail us at taxbriefs@withum.com



WithumSmith+Brown, PC
Certified Public Accountants and Consultants
New Jersey, New York, Pennsylvania, Maryland, Florida, Colorado

Pension Act Waives Required Minimum Distribution For Calendar Year 2009

DECEMBER 17, 2008

BE IN A POSITION OF STRENGTH

...a defined contribution plan described in Code Sec. 401(a), or in Code Sec. 403(a) or Code Sec. 403(b),

...a defined contribution plan which is an eligible deferred compensation plan described in Code Sec. 457(b), but only if the plan is maintained by an employer described in Code Sec. 457(e)(1)(A), or

...an individual retirement plan. (Code Sec. 401(a)(9)(H)(i))

Thus any RMD for 2009 from these plans required under pre-Pension Act law, otherwise determined by dividing the account balances by a distribution period, does not have to be made. The next RMD will be for calendar year 2010.. The Committee Report makes it clear the new relief applies to otherwise-required lifetime distributions to employees and IRA owners and after-death distributions to beneficiaries.

The RBD is determined without regard to the new temporary waiver rule for RMDs for purposes of applying the RMD rules after 2009. (Code Sec. 401(a)(9)(H)(ii)(I)).

Illustration: IRA owner Jack Able attains age 70 1/2 in 2009 and this his RBD is April 1, 2010. Under Pension Act law, the first year for which Able would have to take an RMD from his IRA would be 2009. Under the Pension Act, no RMD is required for 2009 and, thus, no distribution will be required to be made by Apr. 1, 2010. However, because the Pension Act does not change the RBD for purposes of determining the RMD for calendar years after 2009, Able's RMD for 2010 must be made no later than the last day of the calendar year 2010. Should Able die on or after Apr. 1, 2010, the RMD for Able's beneficiary will be determined using the rules that apply where an IRA owner dies on or after the RBD. (Committee Report)

Questions or comments?

E-mail us at taxbriefs@withum.com



WithumSmith+Brown, PC
Certified Public Accountants and Consultants
New Jersey, New York, Pennsylvania, Maryland, Florida, Colorado

Pension Act Waives Required Minimum Distribution For Calendar Year 2009

DECEMBER 17, 2008

BE IN A POSITION OF STRENGTH

Caution: The Committee Report specifically says that the Pension Act's relief provision would not help a taxpayer who attained age 70 1/2 in 2008 but chose to wait until Apr. 1, 2009 to receive his first RMD (for 2008). He would still have to make that first RMD by Apr. 1, 2009. However, he would not have to make the otherwise-required RMD for 2009.

If the 5-year payout rule applies to an account with respect to any decedent, the 5-year period is determined without regard to calendar year 2009. (Code Sec. 401(a)(9)(H)(II)(II)). Thus, for example, for an account with respect to an individual who dies in 2007, the five year period ends in 2013 instead of 2012 (Committee Report)

If all or a portion of a distribution during 2009 is an eligible rollover distribution because it is no longer an RMD under the Pension Act change, the distribution won't be treated as an eligible rollover distribution for purposes of the direct rollover requirement and notice and written explanation of the direct rollover requirement, as well as the mandatory 20% income tax withholding for eligible rollover distributions, to the extent the distribution would have been an RMD for 2009 absent the Pension Act change (Code Sec. 402(c)(4))

Thus, for example, if an employer-provided retirement plan distributes an amount to an individual during 2009 that is an eligible rollover distribution but would have been an RMD for 2009, the plan may but is not required to offer the employee a direct rollover of that amount and provide him with a written explanation of the requirement. If the employee receives the distribution, the distribution is not subject to mandatory 20% income tax withholding, and the employee can roll over the distribution by contributing it to an eligible retirement plan within 60 days of the distribution. (Committee Report)

Questions or comments?

E-mail us at taxbriefs@withum.com



WithumSmith+Brown, PC
Certified Public Accountants and Consultants
New Jersey, New York, Pennsylvania, Maryland, Florida, Colorado

Pension Act Waives Required Minimum Distribution For Calendar Year 2009

DECEMBER 17, 2008

BE IN A POSITION OF STRENGTH

Who benefits from the RMD suspension? The pension Act's suspension of RMDs for 2009 helps retired taxpayers who are well-to-do and do not need to rely on their RMDs for living expenses. By not making the RMD for 2009 (or withdrawing less than the RMD) they will wind up with less taxable income for 2009, and, possibly, avoid (or mitigate the effect of) AGI-based phase-outs of tax breaks. They will also have more tax-sheltered amounts to leave to their beneficiaries. Those retired, wealthy taxpayers who are well on in years will stand to benefit the most, because their (short) table-life expectancy factors would otherwise compel them to take large RMD payouts in 2009.

The non-tax advantage to not making the 2009 RMD is that those taxpayers who have retirement funds invested in beaten down assets, and can afford to wait, will have an opportunity to (hopefully) watch their investments recover before having to sell assets in order to make withdrawals.

Observation: There's no need to show that a retirement plan account or IRA is "in distress" because of stock market conditions in order to qualify for the 2009 RMD suspension. Thus, for example, the RMD suspension applies equally to IRAs invested entirely in FDIC-insured bank-CDs as well as to IRAs invested in depressed in value stocks or mutual funds.

The Pension Act's suspension of RMDs for 2009 also helps taxpayers who don't need to take required beneficiary distributions from qualified plan accounts or IRAs during 2009. They, too, can keep down their AGI, keep more funds within the tax-shelter of the retirement account, and avoid having to sell depressed in value assets in order to make required distributions from their qualified plan accounts.

Questions or comments?

E-mail us at taxbriefs@withum.com



WithumSmith+Brown, PC
Certified Public Accountants and Consultants
New Jersey, New York, Pennsylvania, Maryland, Florida, Colorado

Pension Act Waives Required Minimum Distribution For Calendar Year 2009

DECEMBER 17, 2008

BE IN A POSITION OF STRENGTH

Who doesn't benefit from the RMD suspension? The Pension Act's suspension of RMDs for 2009 means nothing to many, many elderly taxpayers who must make regular withdrawals (sometimes in excess of the RMD) from their retirement plan accounts and IRAs in order to get by each month. For the past year or so, those with a substantial portion of their retirement funds invested in stocks or mutual funds have been forced to take payouts from constantly dwindling account balances. They are likely to continue along that difficult pattern in 2009, barring a dramatic market turnaround. order to make withdrawals.

Questions or comments?

E-mail us at taxbriefs@withum.com

If you have any questions, please contact the WS+B tax department.

#287



WithumSmith+Brown, PC
Certified Public Accountants and Consultants
New Jersey, New York, Pennsylvania, Maryland, Florida, Colorado