New Rules Concerning Required Minimum Distributions for 2009

OCTOBER 15, 2009

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The 2008 Worker, Retiree, and Employer recovery Act (WRERA) waived required minimum distributions for 2009 for employer-provided defined contribution qualified retirement plans, IRAs, and individual retirement annuities that are subject to the Required Minimum Distribution (RMD) rules.

RMDs must generally begin by April 1st of the calendar year following the later of the calendar year in which the taxpayer (employee or IRA owner) reaches age 70 ½. For employer-provided qualified retirement plans, taxpayers who own less than 5% in the company have a delayed date of April 1st of the year following their retirement. And for IRAs and defined contribution plans the RMD for each year 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 IRS regulations.

Since the waiver was passed late in 2008 some taxpayers received their RMDs unnecessarily unless they needed the payments for cash flow or many of the financial institutions and retirement plans began processing checks in 2009 for RMDs before they could be altered to reflect the late-2008 change. However, in the recently issued IRS notice 2009-82 the IRS has given taxpayers the opportunity to correct the mistake that otherwise would increase their taxable income, since qualified plan and IRA distributions are generally fully taxable, unless nondeductible contributions had been previously made to the plan or IRA.

THE IRS HAS ISSUED GUIDANCE THAT RELAXES RULES FOR TAXPAYERS WHO PREVIOUSLY TOOK 2009 REQUIRED MINIMUM DISTRIBUTIONS.

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The notice issued by the IRS provides the taxpayer until the later of 60 days from the date the RMD was received or November 30th, 2009 to roll over the distribution. For lump sum distributions, since all the funds were received on the same date it is considered one distribution, the total amount can be rolled over into another retirement plan. For distributions received monthly or quarterly, these distributions go against the rule of only one rollover per year. The notice allows taxpayers to rollover one of the distributions received and taking the remaining amount and rolling that amount into a ROTH IRA. Since the taxpayer is already paying the tax on that amount, when they do start taking distributions from that account all of the money they receive will be tax-free.

In addition, the notice provides guidance for retirement plan sponsors. It outlines two sample plan amendments that plan sponsors may choose from to amend their plans to either stop or continue 2009 required minimum distributions. Both sample amendments provide that participants and beneficiaries can choose to receive or not to receive 2009 RMDs and allow the employer to offer direct rollover options of certain 2009 RMDs. This notice provides new tax planning opportunities for taxpayers who are subject to RMDs, but as with any tax ruling there can be costly traps as well.

#353

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