



2009 Moratorium On Minimum Required Distributions Includes A Trap For The Unwary And A Plan Administration Issue

In the last quarter of 2008 many retirees received a minimum required distribution from a qualified defined contribution retirement plan (“DC Plan”) or an individual retirement account (“IRA”), based on a December 31, 2007 account value which was an inflated (or excessive) amount based on the value of the retiree’s account at the time of the required distribution. This problem was addressed by the Worker, Retiree and Employer Recovery Act of 2008 (the “Act”), which President Bush signed on December 23, 2008, by amending Section 401(a)(9) of the Internal Revenue Code (the “Code”) to provide that no minimum distributions will be required **for** 2009.

This provision in the Act waives minimum required distributions for 2009 from (i) a qualified employer defined contribution plan maintained under Code Section 401(a), 403(a) or 403(b) or (ii) an eligible deferred compensation plan maintained under Code Section 457(b) by a state or local government agency or instrumentality.

The Act’s solution to this problem seems rather simple—no minimum required distributions need to be made **for** 2009.

Trap for the Unwary

The trap for the unwary relates to an initial 2009 minimum required distribution that must be made on or before an April 1, 2009 “required beginning date” by an individual who did not receive such an initial required distribution in 2008.

“Required beginning date” is defined as April 1 of the calendar year immediately following the calendar year in which:

- an IRA participant attains age 70-1/2;
- a DC Plan participant, who is a five percent or greater owner of the Plan sponsor, attains age 70-1/2; or
- A DC Plan participant, who is not a five percent owner of the Plan sponsor, attains age 70-1/2 or retires, whichever occurs later.

The regulations under Code Section 401(a)(9) provide that an April 1 “required beginning date” distribution is **for** the immediately preceding calendar year. Consequently, an April 1, 2009

required beginning date distribution is **for** 2008 and, therefore, must be made by April 1, 2009 (unless the required distribution was made in 2008).

The effective date of the minimum required distribution provisions in the Act is “**for** calendar years beginning after December 31, 2008”. The Technical Explanation of the Act by the Joint Committee on Taxation states that the Act “does not apply to any required minimum distribution **for** 2008 that is **permitted** to be made in 2009 by reason of an individual’s required beginning date being April 1, 2009.” In other words, the Act does not waive an initial required beginning date distribution which must be made by April 1, 2009; even though the distribution is made **in** 2009, it is **for** 2008.

If a minimum required distribution is not made, the individual is subject to a 50 percent federal excise tax, unless the excise tax is waived by the Internal Revenue Service because it is due to a reasonable error and reasonable corrective actions have been taken. Furthermore, the minimum required distribution must be included in the individual’s gross income for federal income tax purposes.

For example, if a minimum required distribution for an April 1, 2009 required beginning date in the amount of \$30,000 is not made in a timely manner by an individual in the 33% tax bracket, there would be a \$15,000 federal excise tax and a \$10,000 federal income tax, resulting in only \$5,000 of the required distribution remaining after federal taxes.

The good news for an individual with an April 1, 2009 required beginning date is that a second 2009 minimum required distribution will not need to be made by December 31, 2009 because of the 2009 minimum required distribution moratorium in the Act.

When these same new rules are applied to an April 1, 2010 required beginning date distribution, the result is the reverse. In 2010, no minimum required distribution must be made by April 1, 2010 (because such a distribution would be **for** 2009), but a minimum required distribution **for** 2010 must be made by no later than December 31, 2010.

Required Beginning Dates After 2009

The Act also provides that “the required beginning date of an individual after 2009 shall be determined without regard to the 2009 minimum required distribution moratorium.”

Plan Administration Issue

The plan administration issue only applies to DC Plans. A minimum required distribution is not an “eligible rollover distribution.” However for 2009, there are no minimum required distributions and, therefore, any distribution for 2009 that is not required because of the moratorium, but is made anyway, will be an eligible rollover distribution. The Act provides that the following requirements will not apply to a distribution for 2009 if part or all of the distribution would have been a minimum required distribution, but for the Act:

- the direct rollover requirement in Code Section 401(a)(31);

- the special tax notice requirement in Code Section 402(f); and
- the mandatory 20 percent income tax withholding requirement in Code Section 3405(c).

We understand this special plan administration rule is included in the Act so DC Plan and IRA distributions can be processed for 2009 with minimal disruption to current procedures and electronic benefit payment systems.ⁱ

However, the Technical Explanation of the Joint Committee on Taxation provides that with respect to distributions made for 2009, the plan administrator is permitted (but not required) to allow a participant to elect a direct rollover. Furthermore, the plan administrator is permitted (but not required) to provide a special tax notice that has been revised to explain the 2009 moratorium. The plan administrator is presumably also permitted to allow participants to elect to voluntarily withhold amounts from a distribution for 2009 that, but for the Act, would be a minimum required distribution. Even if the plan administrator does not permit direct rollovers or provide special tax notices with an explanation of the 2009 minimum required distributions moratorium, the individual can, nonetheless, rollover part or all of a distribution for 2009 to an IRA or an eligible retirement plan within 60 days of the individual's receipt of the distribution.

The plan administration issue, therefore, is whether a plan administrator should permit direct rollovers, provide a special tax notice (with an explanation of the 2009 moratorium) and permit voluntary federal income tax withholding for 2009 distributions that are not required because of the moratorium, but are being made anyway.

Post-Death Minimum Required Distributions

The Act also includes a 2009 rule relating to minimum required distributions that are made due to the death of an individual who died before his or her required beginning date. If the post-death minimum required distribution is being made under the "five year rule", 2009 is not counted in determining the five year period. The Technical Explanation of the Joint Tax Committee provides the following example of this rule: ... for an account with respect to an individual who died in 2007, the five year period ends in 2013, instead of 2012.

Employer Actions

- Employers need to determine soon whether any required beginning date distributions will need to be made from their DC Plans by April 1, 2009 and make the distributions in a timely manner.
- A decision needs to be made soon with respect to whether direct rollovers and voluntary federal income tax withholding will be permitted to be made from distributions for 2009 that would be minimum required distributions, but for the Act.
- A decision also needs to be made soon with respect to whether Code Section 402(f) special tax notice(s) will be revised to describe the 2009 moratorium rules and will be provided to individuals who receive or elect distributions for 2009 even though such distributions are not required.

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ⁱ On January 9, 2009, the IRS issued Notice 2009-9, which states that financial institutions that report distributions from IRAs on *IRS Form 5498, IRA Contribution Information*, should not put a check in box 11 for IRA distributions made for 2009 which are not minimum required distributions ("RMD"). Box 11 of form 5498 reads as follows: "Check if RMD for 2009. If an IRS Form 5498 has been sent with respect to a distribution for 2009 with box 11 checked, the financial institution must notify the recipient by March 31, 2009, that no RMD is required for 2009."