

Can You Terminate a 403(b) Plan and Distribute the Assets?

403(b)

The answer to the title question seems simple since the passage of the final 403(b) regulations in July 2007. The regulations clearly allow an employer to terminate a 403(b) plan by following the procedures under the final regulations, as long as the employer-level plan document has a provision allowing for plan termination. Additionally, the 403(b) plan document must provide that plan termination will be considered a distribution-triggering event. When a plan is terminated under these conditions, accumulated benefits can now be distributed, rather than having to wait for another triggering event, such as age 59½ or separation from service, as was the case before the final regulations became effective.

A 403(b) employer must fully understand the requirements for a 403(b) plan to be properly terminated. As outlined below, the process includes an employer resolution, employee notifications, and, possibly, an amendment to the employer-level plan document. But problems will likely arise when the employer attempts to distribute the plan assets in the time frame defined under the final 403(b) regulations.

Start Termination Process

The process of terminating a 403(b) plan is, for the most part, the same process that is required to properly terminate a qualified defined contribution plan. Some of the basic steps include formalizing the termination date in writing, maintaining an up-to-date plan document, distributing all plan assets as soon as administratively feasible, and, if the plan is subject to ERISA, filing a final Form 5500, *Annual Return/Report of Employee Benefit Plan*, with the appropriate schedules.

Employers should note that certain 403(b) contracts or accounts are not considered to be held under the 403(b) plan of the employer and would not need to be distributed under a valid plan termination. These contracts/accounts include grandfathered 90-24 transfers, and contracts or accounts held by an unapproved investment provider as long as such accounts/contracts were established prior to 2005 and no direct 403(b) plan contributions were made to any contract or account under the employer's plan to that investment provider after December 31, 2004. (i.e., the investment provider has not had a "payroll slot" under the plan on any date after December 31, 2004).

Formalize Termination

Formalizing the termination means documenting the decision to terminate the plan. The employer's board or governing body should execute a resolution authorizing the plan termination and establishing an effective

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We on this continent should never forget that men first crossed the Atlantic not to find soil for their ploughs but to secure liberty for their souls.

—Robert J. McCracken


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termination date. The employer should formally notify plan participants of the details of the pending termination, and—before distributions occur—must provide IRC Sec. 402(f) notices that detail the tax consequences associated with the various distribution options.

Amend Plan

The IRS has long held the opinion that a plan must be up-to-date with current law as of the termination date. A plan that terminates after the effective date of a law change, but before the date that amendments are otherwise required for that law change, must be amended to comply with the applicable provisions of law from the date on which such provisions become effective with respect to the plan. Because such a terminated plan would no longer exist on the required amendment date and, therefore, could not be amended on that date, the plan must be amended before it is terminated. Consequently, employers with existing 403(b) documents will want to contact their plan providers (e.g., Ascensus) to determine if they must amend their plan to bring the document up to date.

Terminating in 2009

Because the deadline for an employer to adopt a 403(b) plan document was extended until December 31, 2009, by Notice 2009-3, an employer may not yet have a written plan document in place. The question then is whether the employer will need to have a plan document in place before terminating in 2009.

The answer to this question is unclear at this time. Although it may be sufficient for an employer who terminates its plan in 2009 to have an up-to-date plan document in place by December 31, 2009, the conservative and safest approach is to have an up-to-date written plan document in place no later than the termination date of the plan.

Distribute Assets

If a plan includes plan termination as one of the distribution triggers and is subsequently terminated, any accumulated benefits under the plan must be distributed as soon as administratively feasible, as defined under the final 403(b) regulations. The final regulations follow the qualified plan termination rules, which require, among other things, for assets generally to be distributed within one year of the stated plan termination date. This requirement makes it problematic—if not impossible—for a 403(b) plan to terminate if the employees maintain individual accounts. The employer may not be able to ensure that all assets are distributed from all individual accounts within the required time frame. The inability of the employer to ensure that all plan assets be distributed timely could occur for a number of reasons. First, as a result of plan assets being moved to outside 403(b) investment providers using 90-24 transfers, employers may not know where all 403(b) plan assets are currently held. Second, for individual account plans, the 403(b) individual annuity contract and custodial account agreements will likely have been drafted so that the employer is not a party to the agreements. As a result, the employer cannot force a distribution without the individual participant's consent.

In some cases, terminating a 403(b) plan may be easier when the plan assets are held in annuity contracts. This is especially true when plan assets have been held under a group annuity contract arrangement. In such cases, the employer is more likely to know where all plan assets are housed. Plan termination under 403(b) annuity arrangements, however, could also prove to be problematic if the language under the contract or contracts does not allow for distribution as a result of plan termination. Such contracts also may require participant consent before making a distribution. The final 403(b) regulations state that the distribution of a fully paid individual annuity contract would meet the plan termination distribution requirement.

Successor-plan rules similar to those that apply to 401(k) plans also apply to 403(b) plans. Consequently, distributions as a result of plan termination will not be allowed if the employer contributes to another 403(b) plan within 12 months after the termination date (the day that the last dollar is paid out of the plan). This rule does not restrict eligible employers from establishing a 401(k) plan in lieu of a successor 403(b) plan.

File Form 5500

Finally, filing Form 5500, *Annual Return/Report of Employee Benefit Plan*, is new to employers offering 403(b) plans. Consequently, few of them will be familiar with the final Form 5500 filing requirement for terminating plans. The final Form 5500 following a plan termination is due at the end of the seventh month following the month in which all plan assets are distributed. All 403(b) plans subject to ERISA must file a final Form 5500, even if the employer has never filed one before. ♦

Let's Talk Basic Roth IRAs: The "Ins and Outs" of Transfers and Rollovers

ROTH IRA

Our coverage of Roth IRA basics continues with this article examining the two most common methods for moving assets to and from Roth IRAs: transfers and rollovers. Financial organizations must know the characteristics of each method and how those methods differ. Once IRA administrators gain a clear understanding of the rules, they will be able to better assist customers when processing these transactions.

Transfers

Transfers only apply to the movement of money between *like IRAs* and are, perhaps, the simplest way of moving assets between two Roth IRAs. When an IRA holder wants to take money from one IRA and deposit it directly into another IRA that he owns, he generally can do so through a transfer. The key component of a transfer is that there is no distribution to the IRA holder. The check from the sending organization is made payable to the receiving organization; therefore, the IRA holder does not take constructive receipt of the assets. For that reason, transfers are tax-free, nonreportable transactions. The IRS does not require Form 1099-R, *Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*, or Form 5498, *IRA Contribution Information*, for transfers. The amount of the transfer will, however, be part of the fair market value of the receiving IRA, shown in Box 5 of Form 5498.

The IRS does not limit the number of transfers allowed to each IRA holder or the amount of money transferred during a year. The IRA holder can decide whether to transfer his entire IRA or just a portion of it, subject to financial organization policy.

When it comes to transfers involving decedents' Roth IRAs, the rules pertaining to beneficiaries are slightly different. Spouse beneficiaries are allowed to move the assets of their deceased spouses' IRAs into their own IRAs or inherited IRAs through a transfer. Nonspouse beneficiaries, on the other hand, are limited to transfers to inherited IRAs (IRAs set up and maintained in the name of the deceased IRA holder for the beneficiaries' benefit, according to Publication 590, *Individual Retirement Arrangements (IRAs)*).

Although the IRS does not require reporting for transfers, industry sources recommend that financial organizations document the transfer and obtain the IRA holder's (or beneficiary's) signature. Documentation can be accomplished by using forms, such as a transfer request form, withdrawal statement, or contribution form, to more easily facilitate the transaction. No matter what documentation a financial organization uses, it should include the name of the IRA holder, name of the transferring financial organization, name of the receiving financial organization, instructions that the check be made payable to the receiving organization, and instructions that indicate which investments or what portion of the IRA is to be transferred.

Rollovers

By definition, a rollover is generally a tax-free, reportable movement of assets from one retirement savings vehicle to another. When it comes to Roth IRAs, there are three categories of rollovers:

- ◆ Roth IRA-to-Roth IRA,
- ◆ retirement plan-to-Roth IRA, and
- ◆ designated Roth account-to-Roth IRA.

Roth IRA-to-Roth IRA Rollover

A rollover between two Roth IRAs is similar to a transfer, with one major distinction: the IRA holder *does* take constructive receipt of the assets before depositing the money into another Roth IRA. In other words, the check is made payable to the IRA holder instead of the financial organization. Thus, a distribution has occurred and must be reported to the IRS on Form 1099-R, despite the IRA holder's intent to roll over the money to another IRA. Once the distribution is rolled over to the receiving IRA, thereby completing the rollover, it is reported on Form 5498 as a rollover contribution.

Rollovers between two Roth IRAs have specific rules that the IRA holder must follow.

- ◆ No more than one distribution per IRA can be rolled over in a 12-month period, beginning with the date of the distribution. Also, an IRA holder may not roll over the same IRA assets more than once in a 12-month period.
- ◆ The IRA holder must complete the rollover within 60 days of distribution. The 60-day period starts with the day after the day the IRA holder receives the distribution.
- ◆ The IRA holder must irrevocably designate in writing with the receiving organization at the time of the rollover that the deposit is to be treated as a rollover contribution.

Final regulations clarify that a spouse beneficiary, even if she is not the sole beneficiary, may take a distribution and roll over the amount to her own IRA, as long as it is within 60 days. Nonspouse beneficiaries do not have the option of rolling over their inherited Roth IRA assets to another Roth IRA. As mentioned earlier, however, the IRS allows them to transfer the assets from one organization to another, as long as the new account is kept in the name of the deceased IRA holder for the nonspouse beneficiaries' benefit.

As stated earlier, all rollovers are reportable to the IRS. In the case of a rollover between two Roth IRAs, the sending organization will use Form 1099-R to report the amount of the distribution in Box 1, *Gross distribution*, and enter the appropriate distribution code (J, Q, or T) in Box 7, *Distribution code(s)*. The receiving organization will report the rollover amount on Form 5498 in Box 2, *Rollover contributions*.

Retirement Plan-to-Roth IRA Rollover

Rollovers from employer-sponsored retirement plans to Roth IRAs were allowed beginning January 1, 2008, as a result of the Pension Protection Act of 2006 (PPA). Retirement plan participants and their beneficiaries can roll over eligible assets from retirement plans qualified under IRC Sec. 401(a), annuity plans qualified under 403(a), 403(b) plans, and governmental 457(b) plans to Roth IRAs (IRC Sec. 408A(d)(3)). Rollovers from Federal Thrift Savings Plan (TSP) accounts to Roth IRAs are also allowed. Roth IRA-to-employer-sponsored retirement plan rollovers, however, are not permitted.

These types of rollovers must follow the general rollover rules (and may be subject to specific rules set by the employer plan).

- ◆ Assets in the retirement plan must meet the plan's definition of "eligible rollover distributions" to be eligible to roll to a Roth IRA.
- ◆ A written irrevocable election is required at the time of the rollover contribution.
- ◆ Rollovers of retirement plan assets may be direct or indirect. A direct rollover occurs when the check is made payable to the receiving organization. An indirect rollover occurs when the check is made payable to the plan participant and he rolls it over within 60 days.
- ◆ Both pretax and after-tax assets from retirement plans can be rolled over to a Roth IRA. Any rolled over amount that consists of pretax assets must be included in the IRA holder's income for the year of the rollover because a Roth IRA may hold only after-tax assets (plus earnings). To avoid paying tax on the entire rollover amount in the year it is rolled over, an IRA holder may first indirectly roll only the pretax portion to a Traditional IRA. Next, the IRA holder may roll over the after-tax portion to the Roth IRA. (These are two separate rollover procedures.)
- ◆ Until January 1, 2010, plan participants or beneficiaries of plan participants must be eligible to convert assets to a Roth IRA before rolling over money into a Roth IRA: they cannot have a modified adjusted gross income (MAGI) of more than \$100,000 or be married and filing separate income tax returns.
- ◆ Spouse beneficiaries can roll over retirement plan assets either to their own Roth IRAs or inherited Roth IRAs.
- ◆ Nonspouse beneficiaries are allowed to roll over retirement plan assets only to inherited Roth IRAs and only through direct rollovers. Note that the inherited IRAs must be kept in the name of the decedent for the nonspouse beneficiary's benefit.

When reporting a rollover contribution from a retirement plan, enter the total rollover amount in Box 2 of Form 5498.

Designated Roth Account-to-Roth IRA Rollover

Since January 1, 2006, 401(k) and 403(b) plans may allow participants to designate all or a portion of their elective deferrals as after-tax Roth contributions. Like other retirement plan assets, these assets can be rolled over to Roth IRAs. Because these assets are after-tax assets and share other Roth characteristics, however, their portability rules differ slightly from the rules for the retirement plan assets discussed previously. Financial organizations should recognize the differences, as noted below.

- ◆ For a distribution that is not directly rolled over, upon the plan participant's request, the plan administrator must provide a statement either indicating that the distribution is a qualified distribution or stating the amount of the distribution that represents basis (Roth contributions).
- ◆ The designated Roth account five-year period under the 401(k) or 403(b) plan does not carry over to the Roth IRA. Rather, the designated Roth account assets become subject to the IRA holder's existing Roth IRA five-year status.
- ◆ The entire amount of any qualified distribution of the designated Roth account is treated as Roth IRA contributions (basis) when rolled over. If a distribution from a designated Roth account is nonqualified, the designated Roth account contributions are treated as Roth IRA contributions, and the designated Roth account earnings are treated as earnings in the Roth IRA.
- ◆ If upon rollover to the Roth IRA, the designated Roth account balance is less than the investment (basis) in the Roth account due to losses, the taxpayer will treat the amount of the investment, reduced by any previous Roth account distributions of basis, as contributions in the Roth IRA (Treas. Reg. 1.408A-10, Q&A 3). Generally, this means that current or future earnings in the Roth IRA will be treated as nontaxable Roth IRA contributions up to the amount needed for basis recovery. The IRS has not yet clarified how Roth IRA holders will track this.
- ◆ The Pension Protection Act of 2006 inadvertently applied the conversion eligibility requirements to designated Roth account rollovers to Roth IRAs. The Worker, Retiree, and Employer Recovery Act of 2008 removes these eligibility requirements for designated Roth account rollovers, retroactively effective on January 1, 2008.

Additional Rollovers to Roth IRAs

Legislation enacted in 2008 allows the following three types of payments to be rolled over to Roth IRAs.

Military-Related Death Payments

The Heroes Earnings Assistance and Relief Tax (HEART) Act provides that beneficiaries who receive certain tax-free military death gratuity payments or Servicemembers' Group Life Insurance payments are allowed to roll over this money to their Roth IRAs. Specific rules apply to this type of rollover.

- ◆ The rolled amount is not subject to the annual contribution limit or the contribution eligibility restrictions that apply to Roth IRAs.
- ◆ The amount rolled over may not exceed the total gratuity and insurance payments received by the survivor.
- ◆ The amount rolled over is considered nontaxable (basis), and therefore is nontaxable when distributed.
- ◆ The rollover must be completed within one year of the survivor's receipt of the benefit.
- ◆ The 60-day rollover rule and the one-rollover-per-year rules do not apply.

Exxon Valdez Settlement Payments

The Tax Extenders and Alternative Minimum Tax Relief Act contains a provision that allows a plaintiff receiving a settlement in the Exxon Valdez litigation to roll over that amount to a Roth IRA, subject to the following rules.

- ◆ The rolled over amount is not subject to the annual contribution limit or the contribution eligibility restrictions that apply to Roth IRAs.

- ◆ The amount rolled over cannot exceed \$100,000 (reduced by any prior tax year Exxon Valdez settlement income rolled over to an IRA or retirement plan) or the settlement amount received in the taxable year, whichever is less.
- ◆ The amount rolled over to a Roth IRA is taxable in the year it is received.
- ◆ The rollover must be completed by the recipient's tax return due date for the year the payment is received.
- ◆ The 60-day rollover rule and the one-rollover-per-year rules do not apply.

Airline Bankruptcy Payments

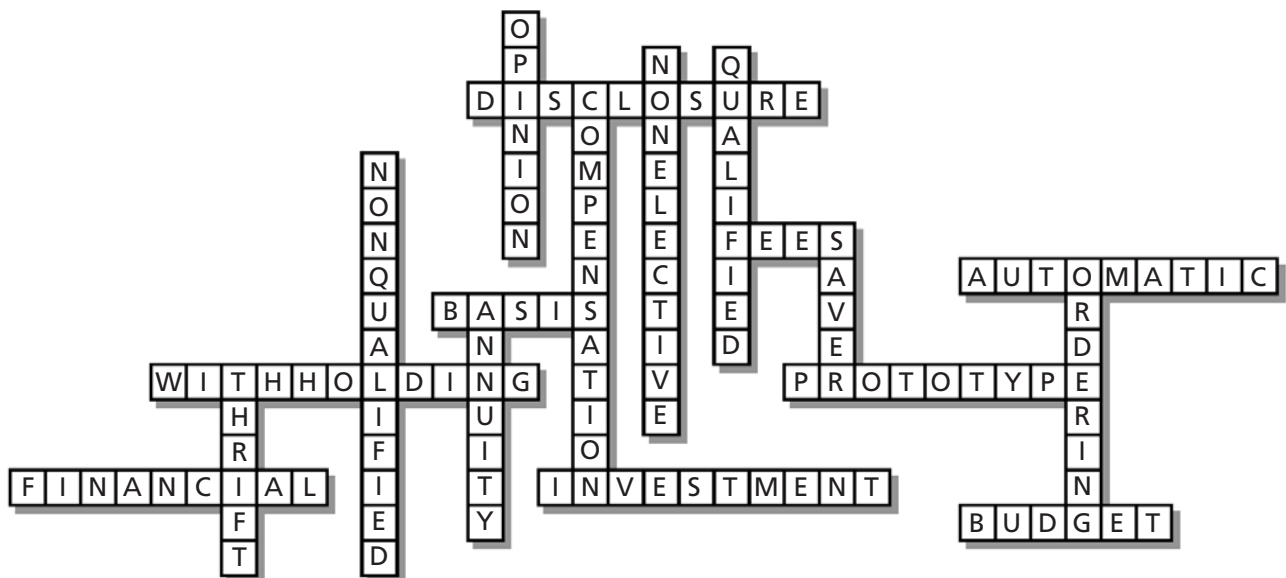
Airline employees who receive qualifying settlement payments from certain airline bankruptcy proceedings are permitted to roll those amounts to Roth IRAs as provided by the Worker, Retiree, and Employer Recovery Act. Certain requirements pertain to these rollovers.

- ◆ The recipient must be a current or former airline employee of a commercial passenger airline that participated in an employer's terminated or restricted defined benefit plan.
- ◆ The airline must report the names of the recipients and the amounts and years of such payments to the IRS and the employee.
- ◆ The rolled over amount is not subject to the annual contribution limit or the contribution eligibility restrictions that apply to Roth IRAs.
- ◆ Rollover of the payment must be completed within 180 days of receipt.

All three of these rollovers should be reported on Form 5498 by entering the rollover amount in Box 2. ❖

Test Your Knowledge **Answers to Last Month's Puzzle**

Be sure to check the last page of each month's *Retirement Plans Bulletin* for training puzzles.
Your next chance to participate and **win** is in this issue!



IRS Tools: SIMPLE IRA Plan Fix-It Guide

SIMPLE

The retirement plans community often forgets that the IRS can be the source of hands-on help in maintaining employer-sponsored retirement plans. One good example of this can be found as close as the IRS website. The IRS has a series of “fix-it” guides available to assist employers in keeping plans in compliance with regulations. The *SIMPLE IRA Plan Fix-It Guide* can give an employer real insight into the requirements of SIMPLE IRA plans and valuable, practical operational information.

This IRS website is presented in an easy-to-use chart. The four column headings are

- ◆ potential mistakes,
- ◆ how to identify the mistake,
- ◆ how to correct the mistake (subdivided into corrective action and correction program(s) available), and
- ◆ how to avoid the mistake.

Potential Mistakes

The IRS lists 10 potential mistakes, which are presented as questions to the employer.

- 1** Do you have more than 100 employees who earned at least \$5,000 in compensation for the prior year?
- 2** Do you sponsor a SIMPLE IRA plan and also maintain another retirement plan?
- 3** Does the plan document reflect the recent SIMPLE IRA law changes?
- 4** Were all eligible employees allowed to participate according to the SIMPLE IRA plan’s eligibility requirements?
- 5** Were correct employer contributions made on behalf of the eligible employees?
- 6** Is the plan’s definition of compensation for all deferrals and allocations used correctly?
- 7** Were employee salary deferral contributions timely deposited to employees’ SIMPLE IRAs after withholding from the employees’ salary?
- 8** Were employer contributions made timely to the employees’ SIMPLE IRAs?
- 9** Have all SIMPLE IRA plan notification requirements been satisfied?
- 10** Did you make employer contributions to all eligible employees whether or not they terminated during the plan year?

If an employer does not understand the context of the question, the employer can click on a “(More)” link and be forwarded to a page that gives a complete explanation of the issue and the employer’s responsibilities.

Operational Tips

If an employer answers “no” to any of these questions, she can then proceed to identify and correct the mistake, plus learn what to do to avoid the mistake in the future. The IRS offers simple explanations in each column of the chart. The employer, however, has the option again to click on “(More)” to receive more in-depth assistance with each subject, as shown in this one section of the chart.

SIMPLE IRA Plan Fix-It Guide

-----Trends-----	-----Tips-----			
Potential Mistake	How to Find the Mistake	How to Fix the Mistake		How to Avoid the Mistake
		Corrective Action	Correction Program(s) Available	
1) Do you have more than 100 employees who earned at least \$5,000 in compensation for the prior year? (More)	Review prior year's compensation data (from payroll records, W-2s, quarterly filings with the state) and determine if there were more than 100 employees who earned \$5,000 or more in compensation during the previous year. (More)	EPCRS If the number of employees is in excess of 100, you must cease contributions to the SIMPLE IRA. You cannot make any new contributions, either from the employer or from the employee, to the SIMPLE IRA plan as long as the number of employees remains in excess of 100. (More)	VCP Audit CAP (More)	Prior to establishing a SIMPLE IRA plan, determine whether you are eligible to have a SIMPLE IRA plan. Do you have more than 100 employees? Are you a member of a controlled group or affiliated service group? (More)

If an employer requests more information on the correction processes, the IRS chart will walk the employer step-by-step through the process. For example, note in the preceding sample section of the chart that if the employer wants to correct a SIMPLE IRA plan that has too many eligible employees, the IRS recommends that the employer use the Employee Plans Compliance Resolution System (EPCRS) and cease contributions to the plan. If the employer clicks on “(More),” the IRS chart helps by walking the employer through the correction procedure step-by-step. The IRS also explains how these correction methods work in conjunction with the EPCRS. The following is the IRS' easy-to-understand explanation of the correction process for this error.

If this is the first year of the plan or after the grace period, you should cease making any new contributions to the plan. You can file a VCP application requesting that contributions made for previous years in which the plan had more than 100 employees remain in the employees' SIMPLE IRA accounts. If relief is not requested (or granted) under VCP for previously made ineligible contributions, then those amounts, with applicable earnings, should be removed from the SIMPLE IRA accounts. You should return salary deferral contributions (and related earnings) to the employees. Report the returned amounts on Form 1099-R as a taxable distribution that is not eligible for rollover. Employer contributions (and related earnings) should be returned to you and reported on a Form 1099-R issued to the participant indicating the taxable amount as zero. In addition, since no contributions could have been made to the SIMPLE IRA, the contributions are excess contributions that are subject to excise tax. For each year that there are excess contributions in the SIMPLE IRA plan, you, the employer, are subject to excise tax under §4972 of the Code, and are required to file a Form 5330 excise tax return. In addition, for each year that excess contributions are made to a participant's SIMPLE IRA, the affected participant is liable for excise tax under §4973 of the Code and is required to file a Form 5329. The excise tax liabilities occur for each year until the excess contributions are removed from the SIMPLE IRAs.

An essential element of the chart is the final column containing recommendations on how the employer may avoid the mistake in the future. The answers are common sense, easily implemented operational procedures.

Summary

Financial organizations can perform an important customer service by alerting employers and plan administrators to this site. Anyone that wants a copy of this valuable worksheet can access it at http://www.irs.gov/pub/irs-tege/simple_fixit_guide.pdf. The IRS also has correction guides for SEPs, SAR-SEPs, and 401(k) plans. Another way to access any of these charts is to go to the IRS website at www.irs.gov and click on “Retirement Plans Community” at the top of the screen under the IRS name. On the next screen choose “Correcting Plan Errors” from the left-hand side of the screen. Access to these charts is under the heading “Identifying, Correcting, and Avoiding Common Plan Errors” in the first column. ❖

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QRP FOCUS

FOCUS ON LOAN OFFSETS AND DEEMED DISTRIBUTIONS



Christine LeBlanc
FEATURED CONSULTANT

Please send topics for Ascensus' QRP Focus column to the following address: Editor, *Retirement Plans Bulletin*, Ascensus, Inc., P.O. Box 979, Brainerd, MN 56401. The editor does not guarantee that questions will appear in the column and regrets that no personal responses can be sent.

Q What is a loan default?

A For a plan loan to be granted an exemption from the IRS' prohibited transaction rules, loan payments must be made according to a level amortized schedule with payments occurring at least quarterly. When a scheduled loan payment is not made by the end of the quarter in which it is due, the loan goes into default. At this point, the plan may allow for a "cure period." This cure period would give the participant until the end of the following quarter to catch up on payments. The decision to offer a cure period is made at the plan level and must be applied uniformly to all participants.

Q When does a loan become a deemed distribution?

A A loan becomes a deemed distribution when 1) it has not been paid off within the maximum time frame (five years for most loans), 2) a defaulted loan's payments have not been caught up to date by the end of the cure period (if the plan allows), 3) a loan exceeds the maximum permissible amount, or 4) an event designated by the plan, such as severance from employment, occurs.

Q What are the tax consequences of a deemed distribution?

A A deemed distribution is not an actual distribution for all tax purposes. A deemed distribution is reported on Form 1099-R, *Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*, for the year in which the deemed distribution takes place and normal tax consequences apply (including possible 10 percent early distribution penalty). Because this is not a true distribution, the deemed distribution cannot be rolled over into an IRA or another retirement plan. Additionally, after a deemed distribution, the loan is still considered a

plan asset and may still be repaid. The loan continues to accrue interest, and that balance is used in determining the maximum loan amount available for any subsequent loans.

Q What is a loan offset?

A A loan offset occurs when, under the terms of the loan, the participant's accrued benefit is reduced by the amount of the outstanding loan (to "repay" the loan and enforce the plan's security interest). As opposed to a deemed distribution, a loan offset is considered an actual distribution. Since the offset is considered a distribution, the loan is no longer part of the plan assets, is not included as an outstanding loan when calculating the maximum loan availability for a new loan, and cannot be repaid.

Q When can a loan be offset?

A A defaulted loan can be offset only when there is a distribution trigger available to the participant under the plan. The participant must be eligible to take a distribution. Plans do have the discretion, however, to require loan offsets once a participant has reached a triggering event (e.g., death, disability, severance from employment) even if there has not been a default before the triggering event. Care should be taken to apply this policy uniformly across all participants to avoid discrimination issues.

Q What are the tax consequences of a loan offset?

A A loan offset is treated as a distribution for all tax purposes. The distribution is subject to income taxes, as well as any applicable penalty taxes, and is reported on Form 1099-R. Provided that the offset takes place before a deemed distribution, it can be rolled over into an IRA or another retirement plan following the normal rollover rules. ♦

IRA Advisor



Tom Stoffel

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Please send questions for Ascensus' IRA Advisor column to the following address: Editor, *Retirement Plans Bulletin*, Ascensus, Inc., P.O. Box 979, Brainerd, MN 56401. The editor does not guarantee that questions will appear in the column and regrets that no personal responses can be sent.

Q In these uncertain financial times, our clients may need help paying for their day-to-day expenses. Can they take hardship distributions from their Traditional IRAs to cover some of their living expenses?

A Yes and no. A "hardship distribution" from a qualified retirement plan (QRP) is a way for plan participants to access their QRP retirement savings before retirement if they have a specific financial hardship. Otherwise, participants generally must meet a "triggering" event (e.g., separation from service, disability) before they can access their QRP assets. Traditional and Roth IRAs do not allow for the same type of hardship distributions as QRPs because IRA holders may access their IRA assets at any time; they don't have to wait for a triggering event to take a distribution. But IRAs do allow for some early distribution penalty exceptions that are not available in QRPs:

- ◆ distributions to cover unreimbursed medical expenses that exceed 7.5 percent of the IRA holder's adjusted gross income;
- ◆ distributions to cover the higher education expenses of an IRA holder, a spouse, or dependents; and
- ◆ distributions to cover health insurance premiums for the IRA holder (and family) after having received unemployment compensation for 12 consecutive weeks as a result of separation from employment.

These three penalty exceptions provide an opportunity to use IRA assets for a special purpose, rather than for retirement, without the burden of the 10 percent early distribution penalty typically associated with a distribution to someone under age 59½. These penalty exceptions do not, however, change the taxability of the money distributed from the IRA.

Q Are there any special IRA provisions, other than the required minimum distribution relief, that help to ease some of the pressure of the current economic climate?

A There is a special exception to the 1-rollover-per-12-months rule that IRA administrators should be aware of if they have clients who have IRAs at financial institutions that were taken over by the Federal Deposit Insurance Corporation (FDIC). Generally, distributions from Traditional IRAs are subject to tax and possible penalty for the year that the distribution is made, even if the distribution is made without the IRA holder's consent by the FDIC (as the receiver of an insolvent savings institution). And amounts distributed from an IRA and rolled over within 60 days generally cannot be rolled over again within a 12-month period beginning on the date of the original distribution. There is, however, an exception to this rule if the distribution meets *all three* of the following requirements.

- 1 The distribution is made from a failed financial institution by the FDIC as receiver for the institution.
- 2 The distribution is not initiated by either the custodial institution or the depositor.
- 3 The distribution is made because the custodial institution is insolvent, and the receiver is unable to find a buyer for the institution.

An IRA holder who meets the requirements and who has already completed 1 rollover in the past 12 months may complete a second rollover contribution into an IRA at your financial organization because of this relief. ♦

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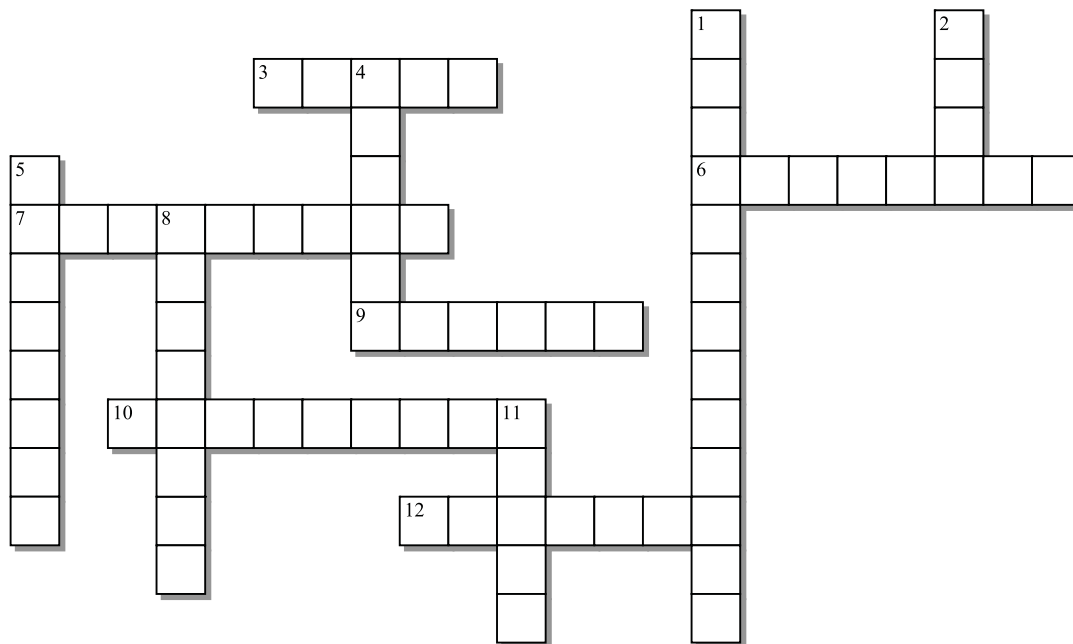
Test Your Knowledge

Win an Ascensus IRA Fact Book!

Five names will be drawn from those of you who complete this crossword puzzle correctly and submit it within 48 hours of receiving this issue of the *Retirement Plans Bulletin*. Please see the bottom of the page for details.

Answers **and winners' names** will be published in next month's issue.

(Hint: Answers can be found within the articles in this issue.)



Across

- 3 This legislative act (acronym) allows survivors who receive certain tax-free military death gratuity payments to roll them to their Roth IRAs.
- 6 This transaction only applies to the movement of money between like IRAs.
- 7 For a plan loan to be granted an exemption from the IRS prohibited transaction rules, loan payments must be made on this type of schedule.
- 9 The IRS' series of "fix-it" guides for assisting employers in keeping their plans compliant includes a guide for correcting this type of IRA plan.
- 10 This type of beneficiary does not have the option of rolling over inherited Roth IRA assets.
- 12 This is the location of the first 2009 *Fall Forum* conference, to be held September 21-23.

Down

- 1 If an employer wants to correct a SIMPLE plan that has too many eligible employees, the IRS recommends that the employer use the Employee Plans Compliance Resolution System (EPCRS) and cease making these.
- 2 Participants of a terminated 403(b) plan must be given this notice detailing the tax consequences associated with their distribution options.
- 4 One of the basic steps of terminating a 403(b) plan is to distribute these as soon as administratively feasible.
- 5 This type of distribution is a feature of many retirement plans but not IRAs.
- 8 Unlike a transfer, this movement of money from one retirement savings vehicle to another is reportable.
- 11 When terminating a 403(b) plan, Form 5500 must be filed if the 403(b) plan is subject to this legislation (acronym).

Please fax your completed crossword to 218-825-5010, Attention: Customer Service. Include your email address in the space below and on the fax cover sheet. If you are one of the five people whose name is drawn from those who sent in correct responses within the first 48 hours, we will send you an email offer for a **FREE IRA Fact Book**.

Email address: _____