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The IRA Authority !

IRA & Employer Plan Rules, News & Tips in Plain Language

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In This Issue

Annual IRA Calendar

Please mark your calendar with the following deadlines:

May 31, IRA Contribution Information (Form 5498)

May 31 is the deadline by which IRA custodians are required to issue Form 5498, IRA Contribution Information (Form 5498) to IRA owners, unless the custodian files for an extension. Form 5498 can be used as an audit tool for IRA contributions, allowing interested parties to determine whether the IRA custodian properly reported the transactions.

The following are some of the transactions that are reported on Form 5498 for 2018: -

- Box 1: Traditional IRA participant contributions for 2018. This includes contributions made January 1, 2018 to December 31, 2018 for 2018, and January 1, 2019 to April 15, 2019 for 2018.
- Box 2: Rollover contributions made to the IRA during 2018
- Box 3: Roth IRA conversions to Roth IRAs during 2018
- Box 4: Recharacterized contributions and recharacterized conversions between Roth IRAs and non-Roth IRAs during 2018
- Box 8: SEP IRA contributions received by the IRA custodian during 2018, regardless of the year for which the employer makes the contribution.
- Box 9: SIMPLE IRA contributions received by the IRA custodian during 2018, regardless of the year for which the employer makes the contribution
- Box 10: Roth IRA participant contributions for 2018. This

includes contributions made January 1, 2018 to December 31, 2018 for 2018, and January 1, 2019 to April 15, 2019 for 2018.

If none of these transactions were made to the IRA, and the IRA custodian already reported the December 31 fair market value to the IRA owner by January 31, Form 5498 is not required to be issued for the IRA for the year.

RMD Indication

The IRA Custodian is also required to indicate if the IRA owner is required to take an RMD for the 2019 calendar year. If an RMD is required, Box 11 should be checked. This does not apply to Inherited/ Beneficiary IRAs.

A complete list of the information reported in each box of Form 5498 is available in the 2018 version of the IRS instructions, which is available here https://www.irs.gov/forms-instructions .

Clients' Responsibility

Your clients should review the form to determine if their transactions were posted correctly. Common mistakes include:

- IRA contributions made January 1 to April 15 not being applied to the correct tax year
- Transfers posted as rollover contributions and vice versa. Transfers are not reportable, while rollovers contributions must be reported on Form 5498. However, if an error occurs, it could result in a transfer being reported as a rollover and/or rollovers not being reported,
- Requested transactions not processed. Unfortunately, paperwork sometimes does fall through the cracks, resulting in clients' requests not being processed. For instance, a client's requested recharacterization may not have been processed, because the custodian overlooked or did not receive the paperwork. In some cases, the paperwork might not have been processed because it was not completed properly.

Form 5498 is not required to be filed with the IRA owner's tax return. If the information reported on the Form 5498 is accurate, the IRA owner simply needs to keep it with the copy of his or her tax return. If the information is incorrect, the IRA custodian should be contacted immediately to determine if corrections can be made.

IRS PLR 201909003: Inherited IRA Beneficiaries Separately Responsible for Taxes on Separate Shares

When multiple beneficiaries inherit an IRA, each beneficiary is independently responsible for any income taxes and/or penalties assessed on his or her share of the inheritance. Proper accounting must be done to ensure accurate accountability of individual responsibility.

Beneficiaries who inherit IRAs are responsible for paying any incomes taxes that would be owed on tax deferred amounts that they distribute from the inherited IRAs. If there are multiple beneficiaries of one IRA, each beneficiary is independently and separately responsible for any income taxes that would be owed on that beneficiary's share. Taxes are usually assessed on amounts that are distributed, for the year in which the distributions occur. This includes required minimum distributions (RMD).

Inherited IRAs are subject to RMD rules, and failure to take RMDs by the applicable deadline would result in the offending beneficiary owing the IRS a 50% excess accumulation penalty on the RMD shortfall. If an IRA is inherited by multiple beneficiaries, individual beneficiaries are separately responsible for any excess accumulation penalty owed because of any RMD shortfall for his or her inherited share.

The IRS recently confirmed these and other rules in private letter ruling (PLR) 201909003.

Please note: *The beneficiaries of the estate in this PLR were nonspouse beneficiaries. Had the beneficiary been the surviving spouse of the IRA owner, the outcome would have been different. Therefore, the explanations provided in this article does not cover the special provisions that apply to spouse beneficiaries.*

Background

Generally, earnings on investments in IRAs grow on a tax-deferred basis, and are taxed only when those amounts are distributed to the IRA owner . When an IRA owner dies, the beneficiary(ies) of the IRA continue to be eligible for this tax-deferred growth, albeit to a limited extent. This limitation is as a result of RMD rules, which require beneficiaries to take distributions at a higher rate than those that would apply to IRA owners.

Beneficiary Distribution Options

The distribution options that are available to the beneficiary of an IRA are determined by two key factors: (1) Whether the IRA owner died before the required beginning date (RBD), and (2) if the beneficiary is a 'designated beneficiary'.

1) The RBD is April 1 of the year that follows the year in which the IRA owner reaches age 70 ½. For instance, if an IRA owner reaches age 70 ½ in 2019, his RBD is April 1, 2020.

2) A beneficiary is a designated beneficiary only if the following requirements are met:

- The beneficiary is a 'person' who is named directly on the beneficiary form- including through a qualified trust- as defined under Treas. Reg. §1.401(a)(9)-4, Q&A-5-, or becomes the beneficiary as a result of provisions under the governing IRA agreement. Nonpersons, such as charities and estates, are not designated beneficiaries.
- The person is the beneficiary of record at the time of IRA owner's death, and
- There is no non-designated beneficiary that shares primary beneficiary status as of September 30 of the year following the year in which the IRA owner dies.

See next page for a high-level summary of the distribution options that are available to nonspouse designated beneficiaries and non-designated beneficiaries:

Taxation Status of Moving Inherited IRAs to Beneficiaries

Generally, when a beneficiary inherits amounts held in an IRA, that amount is moved to an inherited IRA, using the trustee-to-trustee transfer method. The inherited IRA is required to be properly titled in accordance with IRS requirements, which state that inherited IRAs must be registered in the name of the decedent for the benefit of the beneficiary, and the transfer is nonreportable and nontaxable.

Separate RMD Requirements for Multiple Beneficiaries

If an IRA is inherited by multiple beneficiaries, RMD requirements and excess accumulation penalty apply separately to each beneficiary, based on the beneficiary's separate share of the inherited IRA. Each separate share is determined at the time of the IRA owner's death, adjusted for gains and losses on a pro-rata basis until the transfers occur. Once the transfers are completed, gains and losses for each inherited IRA is based on the performance of the investments for each of those separate IRAs.

Beneficiary Distribution Options		
Beneficiary	**When IRA owner dies before the RBD**	**When IRA owner dies on/after the RBD**
Nonspouse designated beneficiary	• Life expectancy distributions. These are made over the nonrecalculated (subtract one each year) life expectancy of the beneficiary beginning by 12/31 of the year following the year in which the IRA owner dies.	• Life expectancy distributions. These must begin by 12/31 of the year following the year in which the IRA owner dies, and are made over the longer of: • The remaining nonrecalculated life expectancy of the deceased IRA owner, or • The nonrecalculated life expectancy of the beneficiary.
Nonperson/ designated beneficiary	• The 5-Year Rule, requiring full distribution of the inherited IRA by 12/31 of the 5th year that follows the year in which the IRA owner dies.	• Life expectancy payments: Made over the remaining nonrecalculated life expectancy of the deceased IRA owner beginning by 12/31 of the year following the year in which the IRA owner dies.

The Facts of the PLR

In PLR 201909003, at the time of his death, the IRA owner was unmarried and his estate was the beneficiary of his IRA. His estate was inherited by more than one beneficiary.

He died after his RBD, and since the estate was his beneficiary, the only distribution option available was to distribute the assets over his remaining life expectancy.

The PLR Request

In the PLR request, the executor of his estate proposed to split the inherited IRA by transferring each of the estate-beneficiary's share into separate inherited IRAs. These inherited IRAs would be properly titled in accordance with IRS requirements.

Contingent upon the IRS approving such a transfer, the executor requested the following rulings from the IRS:

- The trustee-to-trustee transfers from the decedent's IRA to inherited IRAs for the beneficiaries of the estate would not be treated as distributions to the estate.
- Any taxes owed would be deferred until the amount is distributed from the inherited IRAs, and would be the responsibility of the distributing beneficiary. This extends to income in respect of a decedent (IRD), with the transfers not being treated as transfers under IRC section 691(a)(2), allowing a beneficiary to include distributed amounts in gross incomes for any year in which

such beneficiary takes a distribution from his or her inherited share.

- Each beneficiary would be permitted to stretch distributions over the remaining life expectancy of the decedent.
- The RMD for each inherited IRA would be independent of any RMD taken by other beneficiaries, thus disallowing any RMD aggregation among beneficiaries.
- Any excess accumulation penalty owed as a result of failure to take any RMD would be the responsibility of the beneficiary that failed to take RMDs from his or her separate inherited IRA. And,
- No income taxes or excess accumulation penalty would be passed on to the estate or the executor.

The IRS approved all requests.

Operational Procedures That Protect Ruling

In such a case, care must be taken to ensure that proper operational procedures are followed, in order to protect the provisions approved under the PLR. This includes ensuring that:

- Each inherited IRA is properly titled, in the name of the decedent for the benefit of the beneficiary.
- The amounts are moved to the separate inherited IRAs as nonreportable journals/transfers. And,
- Each inherited IRA holds only amounts inherited from the same decedent. And, in cases where the assets pass through an estate to the underlying beneficiary, such amounts should not be commingled with assets inherited directly from the decedent. This is because the distribution options might be different for each inherited IRA.

For example: Assume that 45-year-old Sue inherited two IRAs from her mother, who was 85 years old at the time of her death.

IRA Number 1 was inherited through her mother's estate as in PLR 201909003

For IRA Number 2, Sue was named on the beneficiary form and was the beneficiary at the time of her mother's death, and therefore inherited the IRA outright. The distributions from IRA Number 1 would be taken over her mother's remaining life expectancy of 6.6 years, and the distributions from IRA Number 2 would be taken over Sue's life expectancy of 37.9 years.

Since the divisor for each IRA would be different, they should not be combined into one inherited IRA. Care must also be taken to ensure that

RMD amounts are accurately determined and taken by any applicable deadline, to avoid any excess accumulation penalty.

Other Individuals Might Need Their Own PLRs

A PLR can be relied on only by the individual to whom it is issued, and is based on the facts and circumstances of the presented case. Further, while a PLR gives a good idea of the IRS's interpretation of laws that govern the issue in question, there is no guarantee that they would come to the same conclusion for other similar cases. As such, it might be practical for other taxpayers to get their own PLRs, if the amount and potential savings is large enough to justify the IRS's $10,000 PLR fee.

A beneficiary should consult with a tax professional for advice about how to proceed with handling similar cases.

Bipartisan Bill for Retirement Reform Introduced in Senate

The Retirement Enhancement and Savings Act of 2019 (RESA), was introduced in the Senate on Monday April 1. The bill, sponsored by Finance Committee Chairman Chuck Grassley (R-IA) and Ranking Member Ron Wyden (D-OR), include the following retirement related provisions, for which the objective is intend to increase participation in employer plans:

- ***Increase Start-up Cost for Retirement Plans for Small Businesses:*** The start-up cost is one of the deterrents to small businesses setting up retirement plans. This cost can be offset by the start-up credit, which is now 50% of cost, up to $500, for three years. The credit would be increased to the greater of: (1) $500 or (2) the lesser of (a) $250 x the number of non-highly compensated employees or (b) $5,000.
- ***New Tax Credit for Auto Enrollment Plans:*** Credit of up to $500 for SIMPLE and 401(k) plans that include an automatic enrollment feature.
- ***Relax the Service Hour Requirements for Eligibility:*** Currently, employers can require employees to work at least 1,000 hours a year, in order to be eligible to participate in a qualified plan, such as a 401(k). Under the new rules, a second-tier eligibility requirement would apply, allowing employees who work 500 hours for three consecutive years to be eligible.
- ***IRA Contribution Compensation for Students:*** Stipends and non-tuition fellowship payments received by graduate and postdoctoral students would be treated as eligible compensation for IRA contribution purposes, allowing these students to make IRA contributions.
- ***Repeal Traditional IRA Contribution Age Limit :*** Remove the age 70 ½ cap on IRA contribution eligibility for traditional IRAs.
- ***Penalty-free Withdrawals :***Allow penalty free

withdrawals for qualified birth or adoption.

- ***RMD Age Increase:*** Increase RMD age from 70 ½ to 72.
- Beneficiary Options: Inherited accounts would be required to be distributed within 10 years, except for:
    - spouse beneficiaries,
    - disabled or chronically ill individuals,
    - individuals who are not more than 10 years younger than the employee (or IRA owner), or
    - child of the employee (or IRA owner) who has not reached the age of majority

Disclaimer

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