

# Retirement PLAN news

## Restatement and amendment deadlines

Qualified plans must operate in accordance with their plan documents. Ongoing legal and regulatory changes in retirement plan rules frequently require plan sponsors to amend and restate their plans to keep their documents in compliance. Preapproved plans (i.e., master and prototype documents and volume submitter plans) must be rewritten, reviewed and approved by the IRS, and readopted by employers once every six years.

We are currently in the midst of the first six-year restatement cycle, and the EGTRRA document has been approved by the IRS. Employers using preapproved defined contribution plan documents must restate (readopt) them by April 30, 2010.

### Cumulative list concept

In order to know what qualification requirements should be included when a plan is being rewritten, the IRS devised the cumulative list concept. Each year, an updated list is issued containing qualification requirements for plans that must be rewritten the following

year. The cumulative list simplifies the amendment and review process by establishing cutoff dates: Generally, any laws and/or guidance issued after one cumulative list is published will automatically be included on the next list for the next restatement cycle.

Here's an example: The EGTRRA preapproved document was written based on the cumulative list issued at the end of 2004 (IRS Notice 2004-84), and the submission deadline for IRS review and approval was January 31, 2006. Most laws and regulatory changes that occurred after the 2004 Cumulative List are not incorporated into the EGTRRA document restatement. Thus, even though many PPA provisions became effective before the plans were approved in early 2008 and might already have been in operation, virtually no PPA language is incorporated into the approved document.

However, the Treasury Department and the IRS both have the power to, and often do, require interim document amendments to incorporate changes after a cumulative list has been issued. Preapproved plans must make these so-called "snap-on" amendments to incorporate the changes by the prescribed



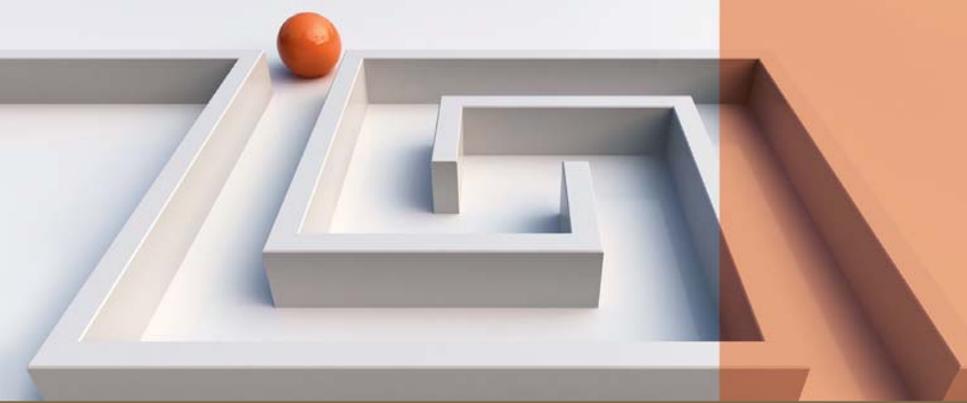
deadline. Required changes since the last restatement cycle will be written into the next document.

### PPA amendment deadline

The Pension Protection Act of 2006 (PPA), which was enacted after the 2004 Cumulative List was published, requires that plans operate under PPA provisions as each becomes effective but does not require that plans be amended until the end of the first plan year beginning on or after January 1, 2009.

Ordinarily, required amendments like those for PPA changes could be made up until a plan's due date for filing its tax return for the 2009 plan year. However, the IRS has indicated that there

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## New nonspouse beneficiary rollover rules

The Worker, Retiree, and Employer Recovery Act of 2008 (WRERA), enacted December 23, 2008, contains provisions pertaining to distributions made to nonspouse beneficiaries. The requirements are effective for plan years beginning after December 31, 2009, and affect the distribution options and mandatory tax withholding rules of distributions for nonspouse beneficiaries.

The provision allowing a nonspouse beneficiary the option of rolling over a deceased participant's plan balance to an inherited IRA was introduced by the Pension Protection Act of 2006. There have been subsequent changes, but WRERA clears up the confusion and provides new rules.

Many plan sponsors have already updated their plans to allow this type of transaction. Sponsors who already offer this option — as well as sponsors who don't — may not be aware of the changes that WRERA requires starting in 2010.

**No longer optional.** Under WRERA, the nonspouse beneficiary rollover distribution is a *required* plan provision. Thus, *all* qualified plans must allow for nonspouse beneficiary distributions by direct rollover.

**Mandatory withholding applies.** An equally important change is that *nonspouse beneficiary distributions will be considered "eligible rollover distributions,"* thus making them subject to mandatory 20% tax withholding and notice requirements. Changing this type of death benefit to an eligible rollover distribution will now result in a 20% mandatory tax withholding on any amounts not directly rolled over to an inherited IRA.

**Notice requirements.** If they have not already been doing so, plan sponsors must begin providing nonspouse beneficiaries with the 402(f) notice, also known as the "Special Tax Notice" or "Rollover Notice," when a distribution is requested. The normal 30- to 180-day time frame for this notice applies.

**Take heed.** All plan sponsors should ensure that these requirements are met and that distributions to nonspouse beneficiaries have federal income tax withheld appropriately. Special explanations may have to be provided to nonspouse beneficiaries so that they fully understand the tax impact of their decisions beginning next year.

## Restatement and amendment deadlines

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may be anti-cutback issues (which, if not correctly handled, would reduce a benefit already earned by the participant) if the PPA amendment is not completed before the end of the plan year. (The IRS plans to publish a list of anti-cutback issues.) This amendment deadline applies to both interim and discretionary amendments made pursuant to statutory PPA provisions and any PPA-related regulations. Thus, the EGTRRA restatement deadline of April 30, 2010, is not applicable to the PPA amendment, and plans may need to be amended for PPA before they are restated for EGTRRA. In this case, the PPA amendment should then be brought over to the EGTRRA restatement.

### Individually designed plans and PPA

Individually designed plans that are off-calendar-year Cycle D plans have an opportunity to meet the deadline for adopting PPA language by the last day of their 2009 plan year. To accomplish this, they may elect to be Cycle E plans, which would change the submission period to between February 1, 2010, and January 31, 2011. These plans will be Cycle D plans for the *following* restatement cycle, which has a submission period of February 1, 2014, through January 31, 2015. In this case, employers would not have a full five years between cycles.

### HEART, EESA, and WRERA amendments

The amendment for the Heroes Earnings Assistance and Relief Tax Act of 2008 (HEART) is not due until the 2010 plan year, although some plans are incorporating HEART and PPA provisions at the same time. The Emergency Economic Stabilization Act of 2008 (EESA) amendment is also not due until the 2010 plan year, but some plans are incorporating EESA and PPA provisions at the same time. An amendment for the provision suspending required minimum distributions, part of the Worker, Retiree, and Employer Recovery Act of 2008 (WRERA), is not due until the 2011 plan year. The IRS has promised guidance on the scope and timing of the amendment.



# Roth IRA conversion in 2010

Roth IRA conversions are a hot topic. Effective January 1, 2010, a provision in the Tax Increase Prevention and Reconciliation Act of 2006 (TIPRA) eliminates the \$100,000 limit on adjusted gross income (AGI) that previously prevented higher income taxpayers from converting a traditional individual retirement account (IRA) to a Roth IRA. This change opens up a number of retirement and tax planning opportunities for both employees and plan sponsors.

## Background

Contributions made into a Roth IRA have already been taxed; therefore when a traditional IRA is converted into a Roth IRA, the individual is required to pay taxes on the conversion amount by including it as gross income for the year the conversion occurs. One reason Roth IRA conversions are attractive is that earnings may ultimately be withdrawn tax free (as long as all requirements are met).

To be eligible for tax-free treatment, the Roth IRA must have been in existence for five years and the IRA owner must be age 59½ or older, disabled, or deceased. Another benefit is that Roth IRAs are not subject to the required minimum distribution (RMD) rules. (Note that an individual currently receiving RMDs from a traditional IRA cannot convert the current year's RMD amount to a Roth IRA.)

## 2010 conversion rules

Taxpayers who convert a traditional IRA into a Roth IRA in 2010 have a special opportunity for paying the income tax due on the conversion amount. Ordinarily, the taxpayer would include the total amount as income for the 2010 tax year. Under the new

law, instead of paying income tax on a 2010 Roth conversion in the same year, taxpayers can opt to defer their tax burden by a year and then spread it over two years, paying equal amounts in 2011 and 2012. This relief applies only to Roth conversions in 2010.

**Example:** Jane decides to convert \$200,000 from her traditional IRA into a Roth IRA in 2010. The next decision she must make is whether to:

- Include the full \$200,000 in gross income in 2010, or
- Include \$100,000 in gross income in 2011 and another \$100,000 in 2012.

Some individuals who convert to a Roth IRA in 2010 may prefer to pay the taxes in 2010, especially if they are wary of possible tax rate increases. After 2010, those who convert to a Roth IRA will have to pay related income taxes in the year the conversion is completed. However, there's one way taxpayers can moderate the tax burden of a Roth conversion: Instead of converting the entire value of a traditional IRA to a Roth IRA in a single tax year, they can convert smaller amounts over the course of several years.

## Not so fast

Volatility in the investment markets can sometimes throw a wrench into the works. Fortunately, it's possible to undo a Roth IRA conversion through a process called "recharacterization," a popular option when the value of an individual's account drops soon after converting to a Roth IRA. Recharacterization allows an individual to change the amount that was initially converted to a Roth IRA (with earnings) back to a traditional IRA, and the amount recharacterized remains tax deferred. Taxpayers have until the due date of their federal income-tax return (including extensions)



for the year the Roth IRA conversion occurs to consider a recharacterization.

**Example:** John converts his \$250,000 traditional IRA into a Roth IRA in February of 2008. In February of 2009, his account balance has dropped to \$150,000.

If John takes no further action, he will have to include the \$250,000 conversion amount as income for the 2008 tax year, even though it is now worth only \$150,000. If John recharacterizes his Roth IRA back into a traditional IRA, the conversion and recharacterization will have no tax consequences for the 2008 tax year. John may convert this money to a Roth IRA at a later time.

## End run

In 2010, the AGI income restriction will still apply to Roth IRA contributions. (The limit for 2009 is \$101,000, \$159,000 for married joint filers.) However, those with AGI exceeding the eligibility limit will have the option of contributing to a traditional IRA and later converting it to a Roth IRA. TIPRA has generally circumnavigated the Roth IRA AGI limit for all taxpayers.



# RECENT developments

## ▶ 403(b) Form 5500 relief

On July 20, 2009, the DOL issued Field Assistance Bulletin (FAB) 2009-2 to provide transitional relief to ERISA 403(b) plans that are now required to meet the Form 5500 reporting requirements for the 2009 plan year. The DOL understands the challenges that many 403(b) plan administrators are facing in terms of accurately reporting required financial information on the Form 5500. Many administrators are finding it difficult to gather financial information on old annuity contracts and custodial accounts with vendors that have either been deselected or are no longer receiving contributions. FAB 2009-2 listed several requirements

that must be met for a 403(b) plan to be permitted to exclude certain contracts or accounts from the 2009 Form 5500.

## ▶ Final investment advice regulations delayed

The final rules regarding investment advice that must be provided to participants and beneficiaries in qualified plans and IRAs have been delayed until November 18, 2009. Originally issued January 21, 2009, with an effective date of March 23, 2009, the rules were initially delayed until May 22, 2009. The Department of Labor then pushed back the effective date to November to allow more time to evaluate the comment letters it had received, several of which

raised issues with the final rules. Congress is also working on legislation that may change these regulations.

## ▶ Extension ending for charitable donations from IRAs

The Pension Protection Act of 2006 (PPA) created a provision allowing taxpayers age 70½ or older to make direct, tax-free contributions of up to \$100,000 per year from their IRAs to qualified charitable organizations. This tax benefit was then extended until December 31, 2009. Subsequently, required minimum distributions from IRAs were waived for 2009. However, charitable donations are still eligible for the tax-free treatment through the December deadline.

The general information in this publication is not intended to be nor should it be treated as tax, legal, or accounting advice. Additional issues could exist that would affect the tax treatment of a specific transaction and, therefore, taxpayers should seek advice from an independent tax advisor based on their particular circumstances before acting on any information presented. This information is not intended to be nor can it be used by any taxpayer for the purpose of avoiding tax penalties.

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