

THE Pension Digest

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A Summary of Two of the Special Tax Rules for Armed Forces' Personnel Who Serve in Combat Zones and Interrelationship With the IRA Rules

Much of the material presented here is taken from IRS Publication 3, “Armed Forces’ Tax Guide.” In the following discussion, “you” is the individual serving in the Armed Forces.

There are two special rules which apply to individuals who serve in combat zones. The first special rule allows certain armed services to exclude certain income from taxation. The second special rule allows different (i.e. extended) deadlines for certain tax transactions, including the making of IRA contributions.

Special Rule #1 – Exclusion of Certain Income

If you are a member of the U.S. Armed Forces who serves in a combat zone (defined later), you can exclude certain pay from your income. You do not have to receive the pay while you are in a combat zone, are hospitalized, or in the same year you served in a combat zone. However, your entitlement to the pay must have fully accrued in a month during which you served in the combat zone or were hospitalized as a result of wounds, disease, or injury incurred while serving in the combat zone. Enlisted personnel, warrant officers, and commissioned warrant officers can exclude the following amounts from their income. (Other officer personnel are discussed later.)

- Active duty pay earned in any month you served in a combat zone.
- Imminent danger/hostile fire pay.
- A reenlistment bonus if the voluntary extension or reenlistment occurs in a month you served in a combat zone.
- Pay for accrued leave earned in any month you served in a combat zone. The Department of Defense must determine that the unused leave was earned during that period.
- Pay received for duties as a member of the Armed Forces in clubs, messes, post and

station theaters, and other nonappropriated fund activities. The pay must be earned in a month you served in a combat zone.

- Awards for suggestions, inventions, or scientific achievements you are entitled to because of a submission you made in a month you served in a combat zone.
- Student loan repayments that are attributable to your period of service in a combat zone (provided a full year’s service is performed to earn the repayment).

Retirement pay and pensions do not qualify for the combat zone exclusion.

Partial (Month) Service: If you serve in a combat zone for one or more days during a particular month, you are entitled to an exclusion for that entire month.

CWF Observation: Since pension distributions are not entitled to be excluded from income, the receipt of IRA distributions while you are in a combat zone would not be entitled to be excluded from income.

Combat Zone: A combat zone is any area the President of the United States designates by Executive Order as an area in which the U.S. Armed Forces are engaging or have engaged in combat. An area usually becomes a combat zone and ceases to be a combat zone on the dates the President designates by Executive Order.

Afghanistan Area. By Executive Order No. 13239, Afghanistan (and airspace above) was designated as a combat zone beginning September 19, 2001.

The Kosovo Area. By Executive Order No. 13119 and Public Law 106-21, the following locations (including air space above) were designated as a combat zone and a qualified hazardous duty area beginning March 24, 1999.

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- Federal Republic of Yugoslavia (Serbia/Montenegro)
- Albania
- The Adriatic Sea
- The Ionian Sea — north of the 39th parallel (including all of the airspace in connection with the Kosovo operation.)

Persian Gulf Area. By Executive Order No. 12744, the following locations (and airspace above) were designated as a combat zone beginning January 17, 1991.

- The Persian Gulf
- The Red Sea
- The Gulf of Oman
- The part of the Arabian Sea that is north of 10 degrees north latitude and west of 68 degrees east longitude
- The Gulf of Aden
- The total land areas of Iraq, Kuwait, Saudi Arabia, Oman, Bahrain, Qatar, and the United Arab Emirates

Qualified Hazardous Duty Area. Beginning November 21, 1995, a qualified hazardous duty area in the former Yugoslavia is treated as if it were a combat zone. The qualified hazardous duty area includes:

- Bosnia and Herzegovina
- Croatia
- Macedonia

Qualifying Service Outside Combat Zone. Military service outside a combat zone is considered to be performed in a combat zone if:

- The service is in direct support of military operations in the combat zone, and
- The service qualifies you for special military pay for duty subject to hostile fire or imminent danger.

Military pay received for this service will qualify for the combat zone exclusion if the other requirements are met.

Nonqualifying Presence in Combat Zone. The following military service does not qualify as service in a combat zone.

- Presence in a combat zone while on leave from a duty station located outside the combat zone,
- Passage over or through a combat zone during a trip between 2 points that are outside a combat zone, and
- Presence in a combat zone solely for your personal convenience.

You do not need to claim the combat zone exclusion on your tax return because this type of income is excluded normally from your wages.

Special Rule #2 — Extension of Certain Deadlines

The following actions have been extended pursuant to rules discussed later.

- Filing any return of income, estate, or gift tax (except employment and withholding taxes),

- Paying any income, estate, or gift tax (except employment and withholding taxes),
- Filing a petition with the Tax Court for redetermination of a deficiency, or for review of a Tax Court decision,
- Filing a claim for credit or refund of any tax,
- Bringing suit for any claim for credit or refund,
- Purchasing a replacement home to postpone paying tax on the gain on the sale (before May 7, 1997) of your old home,
- Making a qualified retirement contribution to an IRA,
- Allowing a credit or refund of any tax by the IRS,
- Assessment of any tax by the IRS,
- Giving or making any notice or demand by the IRS or the payment of any tax, or for any liability for any tax,
- Collection by the IRS of any tax due, and
- Bringing suit by the United States for any tax due.

CWF Observation: The deadline has clearly been extended for the making of contributions. We believe there would also be an extension of the deadlines for the following IRA transactions situations: (1) withdrawing an excess contribution or a current-year contribution; (2) recharacterizing an IRA or Roth IRA contribution; (3) an election by an inheriting IRA beneficiary; and (4) the taking of an RMD IRA distribution. We at CWF will be checking with the IRS to see if the IRS agrees that the extension applies in these situations, also.

Additional Discussion —

Extension of Deadline

Certain periods of time are disregarded when determining whether certain tax matters have been taken care of on time. For ease of understanding, this publication refers to these provisions as “extensions of deadlines.” These deadline extensions should not be confused with other parts of the tax law that refer to extensions of time for performing acts.

Combat Zone/Qualified Hazardous Duty Area Extension

The deadline for filing tax returns, paying taxes, filing claims for refund, and taking other actions with the IRS is automatically extended if you serve in the Armed Forces in a combat zone/qualified hazardous duty area, or have qualifying service outside of a combat zone/qualified hazardous duty area. See Qualifying service outside combat zone, earlier.

Additionally, if you are deployed overseas away from your permanent duty station in support of operations in a qualified hazardous duty area, but outside the qualified hazardous duty area, you also receive these extensions (but not other combat zone benefits). The deadline for IRS to take certain actions, such as collection and examination actions, is also extended. See Combat Zone, earlier, for the beginning dates for the Afghanistan area combat zone, the Kosovo area combat zone, the Persian Gulf area combat zone, and the qualified hazardous duty areas.

Your deadline for taking actions with the IRS is extended for 180 days after the later of:

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- The last day you are in a combat zone/qualified hazardous duty area or have qualifying service outside of the combat zone/qualified hazardous duty area (or the last day the area qualified as a combat zone or qualified hazardous duty area), or
- The last day of any continuous qualified hospitalization (defined later) for injury from service in the combat zone/qualified hazardous duty area or while performing qualifying service outside of the combat zone/qualified hazardous duty area.

Qualified Hospitalization. The hospitalization must be the result of an injury received while serving in a combat zone or a qualified hazardous duty area. Qualified hospitalization means;

- Any hospitalization outside the United States, and
- Up to 5 years of hospitalization in the United States

In additional to the 180 days, your deadline is extended also by the number of days that were left for you to take the action with the IRS when you entered a combat zone/qualified hazardous duty area (or began performing qualifying service outside the combat zone/qualified hazardous duty area). If you entered the combat zone/qualified hazardous duty area (or began performing qualifying service outside the combat zone/qualified hazardous duty area) before the period of time to take the action began, your deadline is extended by the entire period of time you have to take the action. For example, you had 3 1/2 months (January 1 - April 15, 2002) to file your 2001 tax return. Any days of this 3 1/2 month period that were left when you entered the combat zone (or the entire 3 1/2 months if you entered the combat zone by January 1, 2002) are added to the 180 days when determining the last day allowed for filing your 2001 tax return.

Other Granted Extensions

Support Personnel. The deadline extension provision also applies if you are serving in a combat zone or a qualified hazardous duty area in support of the Armed Forces. This includes Red Cross personnel, accredited correspondents, and civilian personnel acting under the direction of the Armed Forces in support of those forces.

Spouses. Spouses of individuals who served in a combat zone are entitled to the same deadline extension with two exceptions.

- The extension does not apply to a spouse for any tax year beginning more than 2 years after the date the area ceases to be a combat zone.
- The extension does not apply to a spouse for any period the qualifying individual is hospitalized in the United States for injuries incurred in a combat zone.

Extended Contribution Deadlines for Soldiers in Combat Zones

A person who is in the Armed Forces (including a reservist on active duty for more than 90 days during the year) is considered to be an active participant in an employer-maintained retirement plan for purposes of applying the tax deduction rules for a contribution to a traditional IRA.

The IRS does not emphasize to as large an extent as we would like, that the spouse of a person serving in a combat zone is generally also entitled to an extension of the deadline for IRA and Roth IRA contributions.

The IRS makes clear that the armed service personnel must instruct the IRA custodian of the specific year for which he or she is making the contribution.

The IRS gives two examples for applying the extension rules. The IRS examples have been written to discuss the revised filing deadlines for a person who has served in a combat zone. For most people, the filing deadline is the April 15 after the end of the calendar year. Since the deadline for filing the return and making an IRA contribution is the same day, these examples illustrate the contribution deadline for an IRA contribution in addition to indicating the filing deadline for a specific year.

Example 1. Captain Margaret Jones entered Saudi Arabia on December 1, 2000. She remained there through March 31, 2002, when she departed for the United States. She was not injured and did not return to the combat zone. The deadlines for filing Captain Jones' 2000, 2001, and 2002 returns are figured as follows.

The 2000 Tax Return. The deadline is January 10, 2003. This deadline is 285 days (180 plus 105) after Captain Jones' last day in the combat zone (March 31, 2002). The 105 additional days are the number of days in the 3 1/2 month filing period that were left when she entered the combat zone (January 1 - April 15, 2001).

The 2001 Tax Return. The deadline is January 10, 2003. The deadline is 285 days (180 plus 105) after Capt. Jones' last day in the combat zone (March 31, 2002).

The 2002 Tax Return. The deadline is not extended because the 180-day extension period after March 31, 2002, ends on September 27, 2002, which is before the start of the filing period for her 2002 return (January 1 - April 15, 2003).

Example 2. Petty Officer Leonard Brown's ship entered the Persian Gulf on January 5, 2001. On February 15, 2001, Leonard was injured and was flown to a U.S. hospital. He remained in the hospital through April 20, 2002. The deadlines for filing Petty Officer Brown's 2000, 2001 and 2002 returns are figured as follows.

The 2000 Tax Return. The deadline is January 27, 2003. Petty Officer Brown has 281 days (180 plus 101) after his last day in the hospital (April 21, 2002) to file his 2000 return. The

Extended Contribution Deadlines, Continued from page 3

101 additional days are the number of days in the 3 1/2 month filing period that were left when he entered the combat zone (January 5 - April 15, 2001).

The 2001 Tax Return. The deadline is January 31, 2003. Petty Officer Brown has 285 days (180 plus 105) after April 21, 2002, to file his 2001 tax return. The 105 additional days are the number of days in the 2002 filing period that were left when he entered the combat zone.

The 2002 Tax Return. The deadline is not extended because the 180-day extension period after April 21, 2002, ends on October 18, 2002, which is before the start of the filing period for his 2002 return (January 1 - April 15, 2003).

Summary. For most taxpayers, the deadline to make an IRA contribution for 2002 was April 15, 2003; the deadline for 2001 was April 15, 2002; the deadline for 2000 was April 15, 2001, etc. However, these deadlines do not apply to armed forces personnel serving in designated combat zones, their spouses and certain support personnel. These individuals are still authorized to make a contribution for a prior year if certain rules are met.

Each individual will need to instruct in writing for what tax year he or she is making the contribution. He or she will/should certify that he or she qualifies for the extended contribution/filing deadline. The law defines a deadline for each qualifying individual. Be aware CWF does have the form, Certification of Extended Contribution Deadline for Combat Zone Personnel, available for purchase.

It is very convenient that the deadline for making an IRA contribution for a prior year is the same as it is for filing the tax return for such year.

The IRA custodian does have special reporting duties with respect to such contributions. These are discussed in the separate article, "IRA Custodians have Special Reporting Duties for U.S. Armed Forces in Designated Combat Zones."

The Prime Rate

The following chart has been prepared by the Federal reserve. The prime rate has had an interesting history. The 2002 rate (an presumably the 2003 rate) is very similar to the rates from 1956-1967.

Rate
Rate of interest in money and capital markets
Federal Reserve System
Short-term or money market
Private securities
Bank loans to business
Prime rate
Not seasonally adjusted
Twelve months ending December

The prime rate is a 7-day rate with weekends and holidays containing the prior business day's value. The daily prime is therefore more suitable for many purposes.

Released on 8/18/2003

<u>Year</u>	<u>Prime</u>	<u>Year</u>	<u>Prime</u>
1956	3.77	1980	15.26
1957	4.20	1981	18.87
1958	3.83	1982	14.85
1959	4.48	1983	10.79
1960	4.82	1984	12.04
1961	4.50	1985	9.93
1962	4.50	1986	8.33
1963	4.50	1987	8.21
1964	4.50	1988	9.32
1965	4.54	1989	10.87
1966	5.63	1990	10.01
1967	5.63	1991	8.46
1968	6.31	1992	6.25
1969	7.96	1993	6.00
1970	7.91	1994	7.15
1971	5.73	1995	8.83
1972	5.25	1996	8.27
1973	8.03	1997	8.44
1974	10.81	1998	8.35
1975	7.86	1999	8.00
1976	6.84	2000	9.23
1977	6.83	2001	6.91
1978	9.06	2002	4.67
1979	12.67		

IRA Custodians Have Special Reporting Duties for U.S. Armed Forces in Designated Combat Zones

Set forth are the special instructions on page R-12 of the 2003 Instructions for Forms 1099-R and 5498.

An individual who is serving in or in support of the Armed Forces in a designated combat zone or qualified hazardous duty area has an additional period after the normal contribution due date of April 15 to make IRA contributions for a prior year. The period is the time the individual was in the designated zone or area plus at least 180 days. The individual must designate the IRA contribution for a prior year to claim it as a deduction on the income tax return.

If a qualifying combat zone individual makes a contribution to an IRA after April 15th and designates the contribution for a prior year, you must report the type of contribution (Box 7) and the amount on Form 5498. Report the amount either for (1) the year for which the contribution was made or (2) a subsequent year.

1. If you report the contribution for the year it is made, no special reporting is required. Include the contribution in box 1 of an original Form 5498 or of a corrected Form 5498 if any original was previously filed.

2. If you report the contribution on Form 5498 in a subsequent year, you must include the year for which the contribution was made, the amount of the contribution, and one of the following indicators:

- a. Use "JG" (Joint Guard) or "AF" (Allied Force) for the Kosovo area.
- b. Use "JE" (Joint Endeavor) for the Persian Gulf area.
- c. Use "EF" (Enduring Freedom) for Afghanistan, Uzbekistan, Kyrgyzstan, Pakistan, Tajikistan, and Jordan.
- d. Use "IF" (Iraqi Freedom) for Arabian Peninsula Areas (the

Persian Gulf, the Red Sea, the Gulf of Oman, the portion of the Arabian Sea that lies north of 1

0 degrees north latitude and west of 68 degrees east longitude, the Gulf of Aden, and the total land areas of Iraq, Kuwait, Saudi Arabia, Oman, Bahrain, Qatar, and the United Arab Emirates and the airspace above such locations).

Under **2** above, enter the information in the blank box to the left of box 10. **Do not** enter the amount in box 1 (or box 10). For example, enter a \$2,000 IRA contribution designated for Joint Guard for the tax year 1998 as "JG 1998 2000" in the blank box.

See **Pub. 3**, Armed Forces' Tax Guide, for a list of the locations within the designated combat zones and qualified hazardous duty areas.

Magnetic media/electronic filers. You may request an automatic waiver from filing combat zone Forms 5498 by submitting **Form 8508**, Request for Waiver From Filing Information Returns Magnetically. Once you have received the waiver, you may report all Forms 5498 for combat zone participants on paper. Alternatively, you may report contributions made by the normal contribution due date magnetically or electronically and report the contributions made after the normal contribution due date on paper. You may also report prior year contributions by combat zone participants on a corrected Form 5498 magnetically, electronically, or on paper.

See **Magnetic Media/Electronic Reporting** in the 2003 General Instructions for Forms 1099, 1098, 5498, and W-2G for information on how to request a waiver on Form 8508.

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TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code		1 IRA contributions (other than amounts in boxes 2-4 and 8-10) \$	OMB No. 1545-0747 <div style="font-size: 2em; font-weight: bold;">2003</div> Form 5498	IRA Contribution Information
		2 Rollover contributions \$		
TRUSTEE'S or ISSUER'S Federal identification no.	PARTICIPANT'S social security number	3 Roth IRA conversion amount \$	4 Reclassified contributions \$	Copy A For Internal Revenue Service Center File with Form 1096. For Privacy Act and Paperwork Reduction Act Notice, see the 2003 General Instructions for Forms 1099, 1098, 5498, and W-2G.
PARTICIPANT'S name		5 Fair market value of account \$	6 Life insurance cost included in box 1 \$	
Street address (including apt. no.)		7 IRA SEP SIMPLE Roth IRA <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		
City, state, and ZIP code		8 SEP contributions \$	9 SIMPLE contributions \$	
Account number (optional)		10 Roth IRA contributions \$	11 Check if RMD for 2004 <input type="checkbox"/>	

Form **5498**

Cat. No. 50010C

Department of the Treasury - Internal Revenue Service

Deemed IRAs in Qualified Retirement Plans

As of January 1, 2003, the law authorized a person to contribute funds to a "Deemed IRA" within an employer qualified plan. In 2001, EGTRRA added Code section 408(q)—Deemed IRAs Under Qualified Employer Plans. This section was amended by JCWAA in 2002. Employers have been waiting for the IRS to issue guidance. In June, the IRS issued proposed regulations under section 408 of the Code.

The purpose of the law authorizing Deemed IRAs is clear. The Fidelitys of this world want the large super-store approach for IRAs and pension plans. In general, the law now allows a qualified employer plan to be so written that a participant may make his or her traditional and/or Roth IRA contributions to the same qualified employer plan which receives his or her employer's contribution and his or her elective deferrals. Deemed IRA contributions are defined to include annual, rollover and transfer contributions. Since SEP and SIMPLE contributions are considered to be employer contributions, such contributions cannot be made to a Deemed IRA. These regulations are proposed to be effective on or after August 1, 2003. Taxpayers may rely on these regulations even if the final regulations are more restrictive. For purposes of the law and this article, IRA means both a trust or custodial account or an annuity.

The IRS acknowledges the proposed regulation is not all encompassing as it does not address all situations. For example, all of the aspects of rollovers and transfers are not covered. The IRS, however, does give the following guidance.

1. Voluntary employee contributions to an account established within an eligible retirement plan meeting the requirements of Code section 408 or section 408A will be treated as a "Deemed" IRA or Roth IRA contributions rather than as contributions to the eligible retirement plan. A voluntary employee contribution is defined as any non-mandatory contribution with respect to which the employee has designated to be a Deemed IRA contribution.

Based on the 2003 instructions for Forms 1099-R and Form 5498, the Deemed IRAs will need to have these forms prepared.

2. The qualified plan document must contain provisions authorizing the making of Deemed IRA contributions. Such provisions must be in effect at the time the deemed IRA contributions are accepted. A limited exception is provided. An employer with a plan having a plan year commencing before January 1, 2004 (but after December 31, 2002) is not required to have such provisions in the plan document until the end of such year. For example, an employer with a calendar year plan year has until 12-31-04 to adopt such provisions and an employer with a 11-1-03 to 10-31-04 plan has until 10-31-04 to adopt such provisions.

3. It will be permissible to establish a separate trust for each individual's deemed IRA. It will also be permissible to have a single trust accept the Deemed IRA contributions from many contributors. In this case, there will need to be separate accounting for the interest of each contributor.

4. The Deemed IRA trust or trusts must be separate from the trust of the qualified employer plan. However, for investment purposes, the assets of the IRA trust(s) and the pension trust may be combined. That is, the prohibition of Code section 408(a)(5) does not apply. There would need to be separate accounting for the interest of each trust (and account). Gains and losses must be allocated to such separate trusts.

5. The Deemed IRA must qualify as an IRA under Code section 408. This includes the rule that the trustee or the custodian of the IRA must be a bank or other entity which has received the IRS' approval to serve as a no-bank trustee or a no-bank custodian. The individual IRA trusts or the comprehensive Deemed IRA trust will have to comply with the governmental reporting requirements—RMD notices, January statements, 1099-R forms and 5498 forms.

We at CWF believe this rule creates "new business" opportunities for banks. Any business sponsoring a qualified employer will need to have a contractual relationship with an IRA custodian or trustee. The contract (and the qualified employer plan) will need to define what the employer would do and what the IRA custodian/trustee would do.

6. An overriding rule or principle is that the qualified employer plan and the Deemed IRAs are treated as separate entities for purposes of the Internal Revenue Code. Each is subject to its own set of laws and rules with respect to eligibility, participation, contributions, distributions, investments, nondiscrimination, administration and disclosure. In the IRS' explanation of the regulation, the IRS furnishes three examples of how the application of this principle will determine how certain situations are to be handled even though the actual regulation does not contain specific provisions for these issues.

Example #1. Code section 72(t) provides many exceptions to when the 10% additional tax will not be owed for certain distributions from qualified employer plans and IRAs. Although some of the exceptions apply whether the distribution is from a qualified employer plan or from an IRA, in numerous situations the exceptions apply to distributions from a qualified employer plan but not an IRA or vice versa. For example, a distribution from a qualified employer plan to an ex-spouse on account of a divorce will not be assessed the 10% additional tax but the tax would be assessed if the distribution is from an IRA. And a distribution from an IRA used to pay first time home buyer expenses will not be assessed the 10% additional tax, but the 10% additional tax would be assessed if the distribution was from a qualified employer plan.

Example #2. The explanation indicates a qualified employer plan could certainly permit a surviving spouse of an IRA owner

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to treat the deceased spouse's IRA as his or her own. However, such surviving spouse would not be able to make voluntary employee contributions because he or she is not an employee. We at CWF find this example confusing since, if the deemed IRA is considered to be an IRA, then the QP eligibility rules should not have to be applied to a spouse who has inherited his or her spouse's IRA.

Example #3. In Announcement 99-2, the IRS discussed that an employer may permit employees to authorize payroll deductions so that the employer could then directly deposit such amounts as contributions into a traditional IRA or Roth IRA. Such instructions and contributions could now be made to a deemed IRA within a qualified employer plan.

7. The IRA distribution rules will govern distributions from Deemed IRAs.

A. The regulations provide a very broad rule—"any restrictions that a trustee, custodian, or insurance company is permitted to impose on traditional or Roth IRAs may be imposed on distributions from deemed IRAs."

This means an employer has great flexibility in setting rules and procedures for distributions. Distributions would not need to be made immediately. They could be made within a reasonable time after the end of a quarter. All of the options provided by the law would now be made available to the inheriting IRA beneficiary.

B. The IRA RMD rules must be met for Deemed IRAs and the QP RMD rules must be met for the qualified employer plan. Deemed IRAs could be aggregated with IRAs and Deemed IRAs. IRA RMDs have never been able to be aggregated with QPs RMDs. QP RMDs have never been able to be aggregated with other QP RMDs.

9. The explanation also discusses how Deemed IRAs are treated under Title I of ERISA. In general, the ERISA rules do not apply. The exclusive benefit fiduciary and co-fiduciary rules do apply. In general, the applicable ERISA rules will apply to Deemed IRAs in a manner similar to SEPs. The DOL and not the IRS has the jurisdiction to write the regulation for Title I of ERISA and with respect to the prohibited transaction rules.

10. Within the regulation (and the explanation) the IRS describes what happens if the qualified employer plan has disqualifying defects. In this situation, the IRS concludes there will be no Deemed IRAs because Code section 408(q) applies only if the plan is qualified. This problem can be resolved in one of two ways. First, the account, even though it does not qualify as a Deemed IRA, may be saved if the account has been designed (i.e. there is a savings provision) to meet the requirements of Code section 408 or 408A (including the commingling rule). Second, the Employee Plans Compliance Resolution System (EPCPRS) can be used to correct the defects in the qualified employer plan. The IRS states that the governing revenue procedure (Rev. Proc. 2002-47, 2002-29) will be revised to include provisions permitting submissions for Deemed IRAs.

11. Within the regulation (and the explanation) the IRS describes what happens if the Deemed IRA provisions of the qualifying employer plan which have been written to comply with the requirements of Code section 408 or 408A do not so qualify. The IRS concludes in this situation that the accounts do not qualify as deemed IRAs and that the qualified employer plan no longer will be qualified. Again, the EPCPRS could be used to correct the defects.

The above disqualifying defect rules may well cause participants to think whether they want to make Deemed IRA contributions to the employer's qualified plan. The law is unsettled as to the issue if an employer does not correct such defects.

Summary. The IRS has provided initial guidance on Deemed IRAs. To a certain degree, qualified employer plans are now competitors with financial institutions for traditional IRA and Roth IRA deposits. However, such pension plans will be required to retain a financial institution to serve as the trustee/custodian of the Deemed IRAs. This "trustee" service is one which you may wish to sell to your business customers with pension plans.

Automatic Extension for Filing Forms 1099 and 5498

The IRS has issued a temporary and proposed regulation authorizing an automatic extension of 30 days to file the Forms 1099 series and 5498 with the IRS. A filer may now request this automatic 30-day extension without being required to sign the Form 8809 and provide an explanation.

An explanation and signature is still required to receive an extension beyond the first 30 days.

Note that no extension has been granted with respect to when the recipient must be furnished his or her copy.

Supreme Court to Decide if a Sole Shareholder is Covered by ERISA

The U. S. Supreme Court has decided to hear the case, *Yates v. Hendon*, U.S., No. 02-458, cert granted 6/27/03. This is a bankruptcy case, but an integral part of the case is the need to decide if a sole shareholder may be a participant/employee of an ERISA plan. The DOL for years has argued and ruled that "an individual" or his or her spouse are not deemed to be "employees" of an employer that is wholly owned by the individual and his or her spouse for the purpose of determining if an employee benefit plan exists. Many courts have used this regulation to argue that shareholders are not entitled any ERISA protection. The U. S. Solicitor General was asked by the Court to file an amicus brief expressing the view of the federal government. Somewhat surprisingly, that view is not the view of the DOL. Theodore B. Olson submitted his brief. He argued "Title I of ERISA contains several provisions that plainly contemplate that working owners may be participants in employee benefit plans." He also argued, "the alternative – that working owners may participate in tax-qualified pension plans under the Internal Revenue Code, and even have some of their pension benefits guaranteed by the Pension Benefit Guaranty Corp, but have no enforceable rights under Title I – would make scant sense."

If the sole shareholder is covered by ERISA along with his or her other employees, then the funds which this shareholder has within a qualified plan will be exempt from the bankruptcy trustee as well as other creditors.

We will keep you updated as to what the court decides. It may even be possible that the Court would give an idea whether they believe a one person plan (i.e. shareholder with no employees) is entitled to ERISA protection.

Banking Regulators Do Not Support Increase in FDIC Insurance Coverage Limits

The House passed proposed legislation (H.R. 522/Deposit Insurance Reform Act) to increase the FDIC insurance coverage limits. The limits for most individual accounts would increase to \$130,000 from \$100,000 except the limit for IRAs and other pension accounts would increase to \$260,000.

Similar legislation is being considered in the Senate. It was assigned to the Senate Banking Committee. The Chairman of this committee is Richard Shelby (R-ALA). It appears he is NOT in favor of increasing the insurance limits. He asked Treasury, the FDIC, the OCC, and the OTS for their positions. They informed the senator that they were not in favor of increasing

the coverage limits. They argued the increase in the limits would influence the institutions to engage in higher risk actions. However, they did argue for two law changes – an institution could accept pension deposits only if it was well capitalized or adequately capitalized and had received a brokered deposit waiver from the FDIC and to give pass-through treatment to section 457 plans as well as other pension plans. It appears that the Bush administration is also not in favor of the higher limits.

New Tax Law Signed May 28, 2003

The Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA) is now law. It contained no changes to IRA laws or pension laws. The following changes were made:

1. Created special tax rates for dividends received by individual shareholders. There will now be a 5% rate and a 15% rate. Under existing law, the maximum rate could have been 39.6%.
2. Increased the child tax credit to \$1,000 per child for 2003 and 2004. Previously, it was \$600 per child.
3. Lowered certain marginal tax rates for 2003-2004 as follows:

Existing Rate	New Rate
38.6%	35.0%
35.0%	33.0%
30.0%	28.0%
27.0%	25.0%
4. The tax rate on capital gains was reduced from 10% and 20% to 5% and 15%.
5. Marriage relief was granted by increasing the standard deduction for married couples for 2003 and 2004.
6. Various law expensing and depreciating law changes to induce businesses increase spending.

September 30, 2003 – Final Deadline for Amending QP Plans

The IRS has given a final reminder that September 30, 2003 is the deadline for amending and restating a qualified plan for GUST law changes which was established pursuant to a master prototype plan or volume submitter plan. If a plan is not timely amended, then it will lose its tax qualified status. The IRS did so in a news release (IR-2003-81).