THE Pension Digest

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## ALSO IN THIS ISSUE –



**Collin W. Fritz and Associates, Inc.,**
***"The Pension Specialists"***



# Upcoming January 2004 Tasks

With January 2004 fast approaching, an IRA custodian needs to remember that the 2004 RMD Notice is required to be provided to those accountholders who are already in required distribution, and to those for whom 2004 will be their first distribution year. The rules require that you notify these accountholders in one of two ways: (1) Notify the accountholder that a distribution is required, and calculate the required minimum amount and include it with the notice (CWF Form #62, Version 1 or 2); (2) Simply provide notice that a distribution is required, and offer to calculate the RMD upon the accountholder's request (CWF Form #62, Version 6). The penalty for not furnishing this notice to required accountholders is $50 per customer to whom it was required to be furnished, but was not. CWF has 6 versions of Form #62 to aid your institution in fulfilling this duty. We also have Form #62, Version 7, to be furnished to an inherited IRA beneficiary. The IRS does not require you to furnish this notice to an inheriting beneficiary, but CWF strongly recommends it.

Another requirement is that an IRA custodian must provide a withholding notice to those IRA accountholders taking periodic or scheduled distributions. This notice must be furnished each and every year. You will want to include wording to this effect: "The law requires us to inform you that income tax withholding does apply to your IRA distribution. We have included a form on which you may provide us with your instruction, if this is your first distribution year, or change your previous withholding instruction. If you do not desire to change your previous instruction, you do not need to return this form; we will withhold using your previous instruction." You will want to be aware, that for any accountholders who are paid 4-12 times per year (quarterly or monthly), you only need to provide the withholding notice once. For accountholders who are paid less often than quarterly (1, 2, or 3 payments per year), you will need to provide the withholding notice prior to each distribution, but no sooner than 6 months prior to the distribution date. CWF has an RMD Notice which incorporates the withholding notice (CWF Form #62, Version 5).

Your institution will also soon be preparing 1099-Rs and January fair market value statements.

What some financial institutions do not realize, is that instead of making multiple mailings, these notices and information reports may be combined and mailed to your accountholders in one mailing. The 1099-R, January statement and the RMD and withholding notices may all be combined and mailed to your accountholders in one envelope. This would be a time-saving and cost-efficient way to meet these requirements.

## Deadlines

**Reminder:** December 31, 2003, is the deadline for completing a 2003 Roth IRA conversion contribution. There are no extensions granted for conversions.

**Reminder:** December 31, 2003, is the deadline for establishing a new profit sharing "Keogh" plan. Plan documents must be signed by such date. The plan may, in general, still be funded by the tax-filing deadline plus extensions.

We have heard that some farmers had good years. They may well want to establish a new profit sharing plan.

In comparison, an employer has until the tax-filing deadline plus extensions to adopt and fund a SEP-IRA plan.

# 2003 Publication 590 Issued

The IRS has recently issued the 2003 version of Publication 590 (Individual Retirement Arrangements (IRAs)). The IRS has made some very good changes. Some were technical changes, and others were more substantive. These changes are described below. The IRS should be commended, because these changes do improve the publication by explaining more clearly the rules which apply to IRAs. However, there is one change we wish they would not have made. SEP-IRAs are no longer covered in Publication 590 even though there continues to be coverage of SIMPLE-IRAs. If one wants to learn about SEP-IRAs, he or she will now need to refer to Publication 560 (Retirement Plans for Small Business).

CWF will be sending the 2003 Publication 590 to its clients who have the IRA Procedures Manual, by the middle of January, 2004.

**The Introduction**

In this section, the IRS has prepared a new table, Table 1-2, to reflect how a traditional IRA differs from a Roth IRA. See page 3.

**Traditional IRAs**

The IRS made the following changes.

On page 9, the IRS adds the following sentence. "Generally, distributions from SEP-IRAs are subject to the withdrawal and tax rules that apply to traditional IRAs." This is a good addition, as many people do not understand that a SEP-IRA is a traditional IRA which simply is authorized to accept much larger contributions.

On page 11, the IRS chose to add a definition of when a person attains age 70½, to clarify the rule that contributions cannot be made to a person's traditional IRA for the year he or she attains age 70½. The following paragraph was added:

> "You attain age 70½ on the date that is six calendar months after the 70th anniversary of your birth. If you were born on June 30, 1933, the 70th anniversary of your birth is June 30, 2003, and you attained age 70½ on December 30, 2003. If you were born on July 1, 1933, the 70th anniversary of your birth is July 1,2003, and you attained age 70½ on January 1, 2004.

On page 12, the IRS made a technical correction for determining the spousal contribution amount for the lesser compensation. Paragraph 2(b) was added because one must subtract from the two spouses' combined compensation the total contributions amount made by the spouse with the greater compensation and not just his or her deductible contributions.

Also on page 12, an Example 2 was added to the discussion of determining for which year a person is considered covered by an employer plan. Example 2 was a good addition, because many employers sponsor profit sharing plans with a discretionary contribution formula. The long standing rule is that a person is NOT an active participant for a given year if the employer or the employee has not made an actual contribution during the calendar year.

On page 18, the IRS added discussion of the topic of what to do if a person inherits an IRA. First, the term "beneficiary" is defined. A beneficiary can be any person or entity the owner chooses to receive the benefits of the IRA after he or she dies. Second, the IRS adds a provision that makes it clear the IRS believes a nonspouse beneficiary can make a trustee-to-trustee transfer of an inherited IRA even though he or she is not allowed to roll over any funds paid from the inherited IRA. Third, the IRS gives a good explanation of the rules which apply when the decedent's IRA has basis. "If you inherit a traditional IRA from a person who had a basis in the IRA because of nondeductible contributions, that basis remains with the IRA. Unless you are the decedent's spouse and choose to treat the IRA as your own, you cannot combine this basis with any basis you have in your own traditional IRA(s) or any basis in traditional IRA(s) you inherited from other decedents. If you take distributions from both an inherited IRA and your IRA, and each has basis, you must complete separate Forms 8606 to determine the taxable and nontaxable portions of those distributions."

On page 21, the IRS added the following three paragraphs covering when a beneficiary is able to claim an income tax deduction for the estate tax which results from certain distributions from the inherited IRA.

> "Federal estate tax deduction. A beneficiary may be able to claim a deduction for estate tax resulting from certain distributions from a traditional IRA. The beneficiary can deduct the estate tax paid on any part of a distribution that is income in respect of a decedent. He or she can take the deduction for the tax year the income is reported. For information on claiming this deduction, see Estate Tax Deduction under Other Tax Information in Publication 559, Survivors, Executors, and Administrators.
>
> Any taxable part of a distribution that is not income in respect of a decedent is a payment that beneficiary must include in income. However, the beneficiary cannot take any estate tax deduction for this part.
>
> A surviving spouse can roll over the distribution to another traditional IRA and avoid including it in income for the year received."

**Rollover Rules**

The following changes were made in the section covering rollovers.

Added a thorough discussion of the rules for automatic waivers and other waivers. This was a desired change, since the new waiver rules are very important and they went into effect in 2002.

Expanded the discussion of how the taxpayer reports a rollover distribution from an IRA on lines 15a (gross amount) and lines 15b (taxable amount) of Form 1040. First, the IRS now instructs what needs to be done if the total amount distributed was not rolled over. The taxable portion of the part that was not rolled over is to be inserted on line 15b. The taxpayer is to write "ROLLOVER" next to line 15b to explain why the taxable amount is less than the gross amount. Second, if the funds were rolled over to an employer plan, the taxpayer is instructed to attached a statement to his or her tax return

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Table I-2. **How Are a Traditional IRA and a Roth IRA Different?**
This table shows the differences between traditional and Roth IRAs. Answers in the middle column apply to traditional IRAs. Answers in the right column apply to Roth IRAs.

| **Question** | **Answer** | |
|---|---|---|
| | **Traditional IRA**? | **Roth IRA**? |
| Is there an age limit on when I can set up and contribute to a . . . . . . . . . . . . | Yes. You must not have reached age $70^1/_2$ by the end of the year. See *Who Can Set Up a Traditional IRA?* in chapter 1. | No. You can be any age. See *Can You Contribute to a Roth IRA?* in chapter 2. |
| If I earned more than $3,000 in 2003 ($3,500 if I was 50 or older by the end of 2003), is there a limit on how much I can contribute to a . . . . . . . . . . . . . | Yes. For 2003, you can contribute to a traditional IRA up to:<br>• $3,000, or<br>• $3,500 if you were 50 or older by the end of 2003.<br>There is no upper limit on how much you can earn and still contribute. See *How Much Can Be Contributed?* in chapter 1.<br>***Note.*** The $3,000 and $3,500 amounts do not increase for 2004. | Yes. For 2003, you may be able to contribute to a Roth IRA up to:<br>• $3,000, or<br>• $3,500 if you were 50 or older by the end of 2003,<br>but the amount you can contribute may be less than that depending on your income, filing status, and if you contribute to another IRA. See *How Much Can Be Contributed?* and Table 2–1 in chapter 2.<br>***Note.*** The $3,000 and $3,500 amounts do not increase for 2004. |
| Can I deduct contributions to a . . . . . | Yes. You may be able to deduct your contributions to a traditional IRA depending on your income, filing status, whether you are covered by a retirement plan at work, and whether you receive social security benefits. See *How Much Can You Deduct*? in chapter 1. | No. You can never deduct contributions to a Roth IRA. See *What is a Roth IRA?* in chapter 2. |
| Do I have to file a form just because I contribute to a . . . . . . . . . . . . . . . . . . | Not unless you make nondeductible contributions to your traditional IRA. In that case, you must file Form 8606. See *Nondeductible Contributions* in chapter 1. | No. You do not have to file a form if you contribute to a Roth IRA. See *Introduction* in chapter 2. |
| Do I have to start taking distributions when I reach a certain age from a . . . | Yes. You must begin receiving required minimum distributions by April 1 of the year following the year you reach age $70^1/_2$. See *When Must You Withdraw Assets? (Required Minimum Distributions)* in chapter 1. | No. If you are the owner of a Roth IRA, you do not have to take distributions regardless of your age. See *Are Distributions Taxable?* in chapter 2. |
| How are distributions taxed from a . . | Distributions from a traditional IRA are taxed as ordinary income, but if you made nondeductible contributions, not all of the distribution is taxable. See *Are Distributions Taxable?* in chapter 1. | Distributions from a Roth IRA are not taxed as long as you meet certain criteria. See *Are Distributions Taxable?* in chapter 2. |
| Do I have to file a form just because I receive distributions from a . . . . . . . . | Not unless you have ever made a nondeductible contribution to a traditional IRA. If you have, file Form 8606. | Yes. File Form 8606 if you received distributions from a Roth IRA (other than a rollover, recharacterization, certain qualified distributions, or a return of certain contributions). |

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explaining the rollover. The reason for this is that the IRS does not require the employer plan to prepare a Form 5498 or any other form to show that the plan received a rollover contribution. Third, if the taxpayer took the distribution in November–December of 2003, but completes the rollover in 2004, then the taxpayer is instructed to attach a statement to his or her tax return explaining what he or she did. This is needed because the rollover occurring in 2004 is not reported under standard procedures until May of 2005. For individuals using the 1040A form, the line references discussed above should be changed to lines 11a and 11b.

Expanded the discussion of how the taxpayer reports a rollover distribution from an employer plan on line 16a (gross amount) and line 16b (taxable amount) of Form 1040 to cover the situation that a portion of the distribution may be the return of his or her after-tax employee contributions. This amount will be nontaxable even if the person does not roll it over. The taxpayer is to write "ROLLOVER" next to line 16b to explain why the taxable amount is less than the gross amount. For individuals using the 1040A form, the line references discussed above should be changed to lines 12a and 12b.

**Recharacterizations**

The following changes were made in the sections covering conversions, recharacterizations and reconversions.

This section is now found in the section covering traditional IRAs, after the rollover section on page 27. The 2002 version had these three topics discussed in the Roth IRA sections on pages 56-58. This change makes sense, as the funds must first come out of the traditional IRA before there can be a conversion contribution into the Roth IRA. The IRS adds the following definition of a conversion contribution—the amount that you withdraw and timely contribute (convert) to the Roth IRA is called a conversion contribution.

It appears the IRS has done another flip-flop on the deadline for recharacterizing a contribution. The 2002 version stated the accountholder had six months after the tax-filing deadline. This was normally October 15 of the following year. the 2003 version states the recharacterization must be completed by the due date of the tax return plus extensions. This is a major change. Under the 2002 version, the taxpayer could recharacterize even if he or she had already filed his or her tax return. This will not be permissible under the 2003 version. Once a person files his or her tax return, it will no longer be possible to recharacterize a contribution. In this situation, the IRS is not being kinder and gentler.

A paragraph is added describing the rule that a recharacterization does not count as a rollover for purposes of the once-per-year rollover limitation. This is true even if the contribution would have been treated as a rollover contribution by the second IRA if it had been made directly to the second IRA rather than as a recharacterization of a contribution to the first IRA. Example: A person takes a distribution from her traditional IRA. She is not sure if she will convert it to a Roth IRA by rolling it over or if she will roll it over to a traditional IRA. If she would roll it over to the traditional IRA, it would count for purposes of the once-per-year rule. However, if she makes a conversion contribution to the Roth IRA and then recharacterizes it, it will not count for purposes of the once-per-year rollover limitation.

The IRS has issued the following chart to determine the amount of net income due to an IRA contribution and the total amount to be recharacterized:

| | | |
|---|---|---|
| **1.** Enter the amount of your IRA contribution for 2004 to be recharacterized. . . . . . . . . . . . . . . . . . | **1.** | ________ |
| **2.** Enter the fair market value of the IRA immediately prior to the recharacterization (include any distributions, transfers, or recharacterization made while the contribution was in the account). . . . . | **2.** | ________ |
| **3.** Enter the fair market value of the IRA immediately prior to the time the contribution being recharacterized was made, including the amount of such contribution and any other contributions, transfers, or recharacterizations made while the contribution was in the account . . . . . | **3.** | ________ |
| **4.** Subtract line 3 from line 2 . . . . . . . . . . | **4.** | ________ |
| **5.** Divide line 4 by line 3. Enter the result as a decimal (rounded to at least three places). . . . . . . . . . . . . . . . . . . . . . . . | **5.** | ________ |
| **6.** Multiply line 1 by line 5. This is the net income attributable to the contribution to be recharacterized.. . . . . . . . . . . . . . | **6.** | ________ |
| **7.** Add lines 1 and 6. This is the amount of the IRA contribution plus the net income attributable to it to be recharacterized. . . . . . . . . . . . . . . . . . | **7.** | ________ |

**Changes to Distribution Rules**

There were changes to the sections covering distributions. Some of the changes made should have been made before the 2003 version, but it is good they have been made now. The order of discussion for the 2003 version is: (1) when can you withdraw or use assets; (2) contributions returned before the due date of return; (3) required minimum distributions for IRA owners; (4) required minimum distributions for IRA beneficiaries; and (5) taxation topics, including penalties and additional taxes. These changes were primarily "clarification" changes. We believe section (5)— the taxation topic—should be the second topic, and then the other topics should be discussed. Even so, the IRS changes make it easier to understand the rules applying to distributions.

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The IRS adds a very basic sentence to the introduction (when can you withdraw or use assets) of the distribution section. It is: "you can withdraw or use your traditional IRA assets at any time."

There appears to not have been any changes in the discussion of withdrawal of contribution by the due date (plus extensions). The deadline is defined as the filing date plus extensions.

A number of paragraphs have been added to improve the RMD discussion for living IRA owners as well as IRA beneficiaries. The IRS clearly breaks the discussion into two separate categories: owners and beneficiaries. The IRS had not done this as well as it should have in 2002 and earlier versions.

With respect to the RMD rules for IRA owners, the following changes were made. First, there is now a specific definition of a required minimum distribution (RMD). The amount that must be distributed each year is referred to as the required minimum distribution. Second, an explanation is given stating that if you take more than the minimum for a given year, you are not allowed to offset this excess against a future year's RMD. Third, the express statement is made that the IRA accountholder or the IRA trustee must figure the RMD for each year. Fourth, the statement that special rules apply to RMDs from individual annuities. Fifth, a discussion of the special rules which apply when there is a change in the marital status of the age 70½ or older accountholder or if there is a change in his or her beneficiary for a reason other than there having been a change on account of the spouse's death. The IRS should have given some examples to explain these rules, but they did not. Sixth, a paragraph has been added making it clear that contributions made after December 31 do not need to be added to the December 31 balance for RMD calculation purposes. Seventh, the "distribution period" is defined and Tables II (Joint) and Table III are referenced. Eighth, the IRS includes a specific paragraph to discuss the rules which apply in the year of the owner's death. The general rule is: you figure the RMD for the year in which an IRA accountholder dies as if the owner lived for the entire year.

CWF suggestion. We would suggest the Tables be renumbered as follows: Uniform (I); Joint stays as II, and Single/Beneficiary would be III. Currently, I is the Single/Beneficiary, II is Joint, and III is the Uniform.

A number of paragraphs have been added to improve the RMD discussion for IRA beneficiaries. In fact, the IRS has split the discussion to make it more clear that there are RMDs for owners and also for beneficiaries. It is now made more clear that the rules to be applied depend upon whether the accountholder died on or after the required beginning date or before such date. And the special rules are explained for when the beneficiary is not an individual, a trust is the beneficiary, and the separate accounting rules.

With respect to the taxation of distributions from traditional IRAs and assessment of the 10% additional tax and other penalty taxes, the changes were minimal.

### Roth IRA Changes

With respect to Roth IRAs, the IRS made the following changes:

The first change is that deemed IRAs (either Roth or traditional) may be established within a qualified employer plan on or after January 1, 2003, if certain rules are met. The plan must authorize separate accounts which, in general, must meet the Roth IRA rules or the traditional IRA rules.

The second change is that the IRS has created a new chart to be used to determine if a distribution from a Roth IRA is a qualified distribution. This chart is set forth on page 6.

The third change is that the IRS cut back on the number of examples presented with respect to figuring the ordering rules and the taxable part of a Roth IRA distribution. In the 2002 version, the IRS had given three examples. In the 2003 version, there is just one example.

The fourth change is to add an explanation of the rule that you (i.e. accountholder) cannot use your Roth IRA to satisfy an RMD for a traditional IRA or vice versa.

**Summary.** The IRS has issued the 2003 version of the IRS Publication 590, Individual Retirement Accounts. Most of the changes improve the publication. The discussion of the RMD rules was improved greatly by adding discussion of some of the new rules. The only change we are unhappy with was the decision to remove the SEP chapter and simply reference Publication 560. The IRS should rethink this decision.

# Last Minute IRS Changes to Form 1099-R

### CWF's Observations

The IRS has made some last-minute changes to its 2003 Form 1099-R. The IRS has greatly simplified the text under Code "J" on the 2003 1099-R instructions. Code "8" and "P" are used with Code "J" for excess contributions. The text under Codes "T" and "Q" has changed slightly. You will want to be sure to pay close attention to your completion of the 1099-R to be certain you use the correct code in the correct situation. DO NOT use code "8" or "P" with code "Q" or "T."

CWF believes these codes changes will apply for both 2003 and 2004 reporting.

**Change to 2003 Instructions for Form 1099-R and 5498—Guide to Distribution Codes (Box 7)**

The *Explanations* for Codes J, Q, and T shown in the **Guide to Distribution Codes** for Roth IRA distributions has changed. If you have issued a Form 1099-R (or applicable substitute) for 2003 for a Roth IRA distribution, you may have to issue a corrected return based on the changes in the chart below.

| Distribution Codes | Explanations | *Used with code . . . (if applicable) |
|---|---|---|
| **J—Early distribution from a Roth IRA.** | Use Code J for a distribution from a Roth IRA when Code Q and Code T **do not** apply. | 5, 8, or P |
| **Q—Qualified distribution from a Roth IRA.** | Use Code Q for a distribution from a Roth IRA if **you know** that the participant meets the 5-year holding period and:<br>• The participant has reached age 59 ½, or<br>• The participant died, or<br>• The participant is disabled.<br>**Note:** *If any other codes, such as 5, 8, or P apply, use Code J.* | None |
| **T—Roth IRA distribution, exception applies.** | Use Code T for a distribution from a Roth IRA if **you do not know** if the 5-year holding period has been met but:<br>• The participant has reached age 59 ½, or<br>• The participant died, or<br>• The participant is disabled.<br>**Note:** *If any other codes, such as 5, 8, or P apply, use Code J.* | None |

* See the **Caution** for the Box 7 instructions on page R-8.

Also, for Codes 5, 8, and P, delete any reference to Codes T and/or Q that is shown in the "Used with code . . . (if applicable)" column.

The above changes will appear in the 2004 Instructions for Forms 1099-R and 5498.

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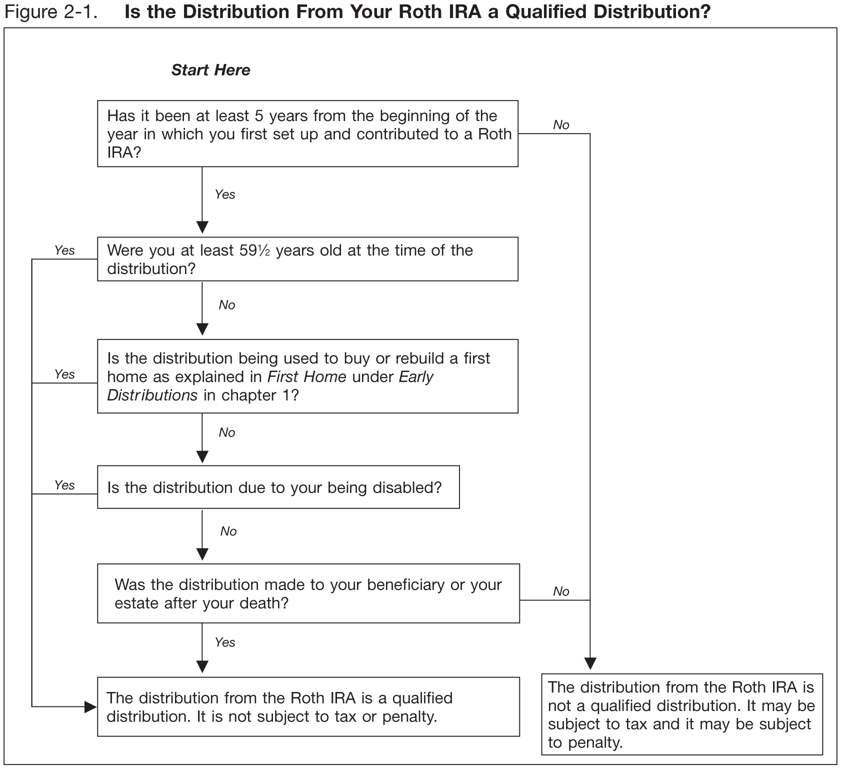
Figure 2-1. **Is the Distribution From Your Roth IRA a Qualified Distribution?**



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# Key Retirement Plan Rules for 2003

| Type of Plan | Last Date for Contribution | Maximum Contribution | Maximum Deduction | When to Set Up Plan |
|---|---|---|---|---|
| **SEP** | Due date of employer's return (including extensions). | Smaller of $40,000 or 25%[1] of participant's compensation.[2] | 25%[1] of all participants' compensation.[2] | Any time up to due date of employer's return (including extensions). |
| **SIMPLE IRA and SIMPLE 401(k)** | **Salary reduction contributions:** 30 days after the end of the month for which the contributions are to be made.[3]<br><br>**Matching contributions or nonelective contributions:** Due date of employer's return (including extensions). | **Employee:** Salary reduction contribution, up to $8,000.<br><br>**Employer contribution:** *Either* dollar-for-dollar matching contributions, up to 3% of employee's compensation,[4] *or* fixed nonelective contributions of 2% of compensation.[2] | Same as maximum contribution.<br><br>Same as maximum contribution. | Any time between 1/1 and 10/1 of the calendar year.<br><br>For a new employer coming into existence after 10/1, as soon as administratively feasible. |
| **Qualified** | Due date of employer's return (including extensions).<br><br>**Note:** For a defined benefit plan subject to minimum funding requirements, contributions are due in quarterly installments. See *Minimum Funding Requirements* in chapter 4. | Defined Contribution Plans<br><br>**Money Purchase:** Smaller of $40,000 or 100%[1] of participant's compensation.[2]<br><br>**Profit-Sharing:** Smaller of $40,000 or 100%[1] of participant's compensation.[2]<br><br>Defined Benefit Plans<br>Amount needed to provide an annual benefit no larger than the smaller of $160,000 or 100% of the participant's average compensation for his or her highest 3 consecutive calendar years. | Defined Contribution Plans<br><br>**Money Purchase:** 25%[1] of all participants' compensation.[2]<br><br>**Profit-Sharing:** 25%[1] of all participants' compensation.[2]<br><br>Defined Benefit Plans<br>Based on actuarial assumptions and computations. | By the end of the tax year. |

[1]Net earnings from self-employment must take the contribution into account.
[2]Compensation is generally limited to $200,000.
[3]Does not apply to SIMPLE 401(k) plans. The deadline for qualified plans applies instead.
[4]Under a SIMPLE 401(k) plan, compensation is generally limited to $200,000.

# Sometimes Late is Too Late

We have all learned that a person may, in some situations, recharacterize a traditional contribution to be a Roth IRA contribution or vice versa. The problem is: this works only if done within certain time limits, and some accountants and attorneys are not aware of the limits and so give their clients improper advice.

The following situation is a typical situation. Nat and Anita Niles come to your institution in November of 2003 and inform you their tax accountant has informed them to go to their IRA custodian and move their funds from their two Roth IRAs to two traditional IRAs. They had opened two Roth IRAs in March of 2001 by making two $2,000 contributions for tax year 2000. In the following year, on April 3, 2002, each contributed another $2,000 to such Roth IRA for tax year 2001. The current balance of both Roth IRAs, as of November 30, 2003, is $4,675. The accountant has now told them that they were never eligible to make the Roth IRA contributions because their modified adjusted gross income exceeded $160,000. Is it permissible for Nat and Anita to solve their problem by simply moving the Roth IRA funds to traditional IRAs? Is it permissible for the IRA custodian to adopt the position that "we are not the tax advisor and therefore we have the right to always rely on the instruction of the accountant/attorney?"

The answer to both questions is "no."

Moving funds from a Roth IRA to a traditional IRA is permissible (i.e. authorized by the tax laws) only if an annual contribution or a conversion contribution is recharacterized. There is no such thing as converting funds within a Roth IRA to a traditional IRA. The law defines a conversion to be when funds within a traditional IRA are moved into a Roth IRA and not vice versa.

There is a time deadline which applies to recharacterizations. The deadline is the tax-filing deadline for such tax year plus six months. Therefore, a contribution for tax year 2000 must have been recharacterized by October 15, 2001, and a contribution for tax year 2001 must have been recharacterized by October 15, 2002. These deadlines were missed. It is too late to move the Roth IRA funds to a traditional plan. To move them to a traditional IRA would only make the tax situation worse than it presently is. They would be excess contributions within the traditional IRAs.

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**Sometimes Late is Too Late,**
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This does not mean that the funds should stay within the Roth IRAs, as they are excess contributions. In general, the law imposes a 6% excise tax for each and every year the excess contributions remain in the Roth IRAs. The 6% excise tax is owed for tax years 2000-2002 and will be owed for tax year 2003 if not corrected by withdrawal by December 31, 2003.

Nat and Anita should each withdraw their $4,000 of excess Roth IRA contributions by December 31, 2003 to avoid the 6% excise tax for 2003. They should file amended returns for 2000-2002 and pay the 6% tax which is owed. That is their concern. Although they may decide to withdraw the earnings amount of $675 for tax administration reasons, the law apparently does not require them to do so.

The IRA custodian, in this situation, should understand why it should not take the position that it is protected as long as they rely on the accountant's tax opinion letter. The reason is: both the traditional IRA owner and the traditional IRA custodian must follow the terms of the IRA plan agreement. It is not just the duty of the IRA owner to follow the terms of the IRA plan agreement. Article I clearly states that an IRA custodian shall accept a contribution for a traditional IRA only if the proposed contribution is less than $3,000/$3,500 (as applicable), is a qualifying rollover, is a qualifying SEP contribution, or is a qualifying recharacterization. Nat and Anita's proposed contribution does not meet these eligibility rules, and, therefore, the IRA custodian has the duty to say the proposed contribution cannot be made.

# New Backup Withholding Rate—28%

President Bush signed into law the Jobs and Growth Tax Relief Reconciliation Act of 2003 (Public Law 108-27) on May 28, 2003. This new law retroactively changes the backup withholding rate to 28% from 30% for any amounts paid after December 31, 2002. IRA Announcement 2003-45 is set forth below. In general, this Announcement, as issued on July 14, 2003, states the IRS will not be able to reflect this change in various 2003 forms and publications, since they have already been printed, but will do so in the 2004 versions.

**ANNOUNCEMENT 2003-45**

**Purpose**

This announcement is to advise payers about a reduction in the backup withholding rate authorized by section 3406(a)(1) of the Internal Revenue Code. Section 105(a) of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (Public Law 108-27) reduced the rate for backup withholding on reportable payments.

**New Backup Withholding Rate**

For amounts paid after December 31, 2002, the backup withholding rate was reduced to 28%.

**New Rate Not Reflected in 2002 Products**

The backup withholding rate shown in the latest revision of the following products is incorrect for amounts paid after December 31, 2002.

***Tax Forms***

- Instructions for the Requester of form W-9
- Instructions for the Requester of Forms W-8BEN, W-8ECI, W-8EXP, and W-8IMY

The instructions for the Requester of Form W-9 will be revised in December 2003, to reflect the new backup withholding rate for amounts paid after December 31, 2002.

The Instructions for the Requester of Forms W-8BEN, W-8ECI, W-8EXP, and W-8IMY will be revised in August 2003 to reflect the new rates.

**Technical Publications**

- Publication 27, Your Federal Income Tax
- Publication 225, Farmer's Tax Guide
- Publication 505, Tax Withholding and Estimated Tax
- Publication 515, Withholding of Tax on Nonresident Aliens and Foreign Corporations
- Publication 525, Taxable and Nontaxable Income
- Publication 542, Corporations
- Publication 550, Investment Income and Expenses
- Publication 583, Starting a Business and Keeping Records
- Publication 1212, List of Original Issue Discount Instruments Instruments

The 2003 version of these publications will have the new backup withholding rate for amounts paid after December 31, 2002.

**New Rate Not Reflected in 2003 Products**

The backup withholding rate shown in the 2003 version of the following products is incorrect for amounts paid after December 31, 2002.

- Form W-9, Request for Taxpayer Identification Number and Certification
- Form W-2G, Certain Gambling Winnings
- Form 1099-CAP, Changes in Corporate Control and Capital Structure
- Form 1099-G, Certain Government Payments
- Form 1099-INT, Interest Income
- Form 1099-OID, Original Issue Discount
- Form 1099-MISC, Miscellaneous Income
- Form 1099-PATR, Taxable Distributions Received From Cooperatives
- Instructions for Form 1042-S

The 2004 version of these forms and instructions will show the new backup withholding rate for amounts paid after December 31, 2002.