



# THE Pension Digest

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Collin W. Fritz and  
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## The Special Reporting Required for a Nonqualifying Transfer Contribution

It doesn't happen often, but once in a while a mistake will occur with respect to transferring funds from one IRA custodian to another IRA custodian. For example, Jan Mitchell, has a \$15,000 IRA CD and she also has a \$5,000 CD with First National Bank. Jan Mitchell is age 57. On July 20, 2003, your bank, First State Bank, sends a transfer form to First National Bank requesting that all IRA funds be transferred. First National Bank makes a mistake and sends you a check for \$20,000. In February of 2004, this customer realizes a mistake has occurred. She received her January FMV statement and noticed the error.

### ***What needs to be done to correct the error?***

Any type of impermissible or nonqualifying contribution constitutes an excess IRA contribution. This includes an ineligible transfer. An ineligible transfer occurs much less frequently than an ineligible rollover, a contribution in excess of the contribution limits, or an ineligible contribution. These are the “normal” types of excess contributions.

The standard way to correct an excess contribution is to withdraw it, plus the related income, on or before the tax filing deadline (plus extensions). It is assumed the earnings on the excess contribution of \$5,000 were \$150, and this amount was withdrawn on February 28, 2004.

First State Bank will need to report the improper transfer amount of \$5,000 as a traditional IRA contribution in box 1 of the 2003 Form 5498.

First State Bank will also report the payment of the \$5,150 to Jan Mitchell as the return of an excess contribution. First State Bank will furnish the special notice to Jan so that she will

include the \$5,150 (gross amount) and the \$150 (taxable amount) on her 2003 income tax return. In addition, First State Bank will prepare a 2004 Form 1099-R reflecting the same information and reason Code “P1” will be inserted in box 7.

*CWF Comment. The IRS instructions do NOT give any guidance for the above situation. We believe the approach described above is what the IRS would expect an IRA custodian to do.*

## The Special Reporting Required for a Nonqualifying Rollover Contribution

As with transfers, it may not happen often, but once in a while a person will roll over an IRA distribution which does not qualify to be rolled over. Many times it will be the mistake of the accountholder. The accountholder may not know that he or she is ineligible to roll over a required minimum distribution. Or, it could be the fault of the prior IRA custodian. For example, Raul Sanchez has a \$30,000 IRA CD with Nevada State Bank. He is age 73. In January of 2003, he had been informed that his RMD for 2003 was \$1,400. On August 15, 2003, he withdraws the \$30,000. He thinks he recalls Nevada State Bank personnel informing him at that time that he had been paid his required distribution amount earlier in the year. Consequently, on September 30, 2003, he makes a rollover contribution of the entire \$30,000 into your bank, Arizona National Bank. On February 17, 2004, he contacts you. He has just determined that he must have failed to take his required minimum because he did not receive a Form 1099-R from Nevada State Bank for his RMD amount. He asks for your help.

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## Nonqualifying Rollover Contribution, Continued from page 1

Does he owe the 50% tax for having failed to take a required minimum distribution, or does he have an excess contribution situation?

He does not owe the 50% tax. He was paid his RMD amount for 2003 when he withdrew the \$30,000. It might be nice if an IRA custodian would issue two checks in this situation—one for the RMD amount and one for the non-RMD amount. However, the rules do not require an IRA custodian to be this nice.

This RMD amount is ineligible to be rolled over. When he rolled it over, it constituted an excess contribution. The analysis set forth above for an impermissible transfer would apply in the same fashion for an impermissible rollover.

The standard way to correct an excess contribution is to withdraw it plus the related income on or before the tax filing deadline (plus extensions). It is assumed the earnings on the excess contribution of \$1,400 were \$100, and this amount was withdrawn on February 17, 2004.

Arizona National Bank will need to report the improper rollover amount of \$1,400 as a traditional IRA contribution in box 1 of the Form 5498.

Arizona National Bank will also report the payment of the \$1,500 to Raul Sanchez as the return of an excess contribution. Arizona National will furnish the special notice to Raul so that he will include the \$1,500 (gross amount) and the \$100 (taxable amount) on his 2003 income tax return. In addition, Arizona National Bank will prepare a 2004 Form 1099-R reflecting the same information, and reason Code "P1" will be inserted in box 7.

## Withdrawing a 2003 IRA Contribution in the Year 2004

For purposes of this article, we are going to assume that your customer, John Black, age 50, made a \$3,000 contribution on March 15, 2003 for 2003. On April 1, 2004, John decides he should not have made the contribution, and he requests to withdraw it. He understands he must also withdraw the related income. He may be requesting this distribution because he had made an excess contribution, or for another reason. *The significant factors in this example are that John made his contribution in 2003 and removed it in 2004, and the law states the income is taxable for the year in which the contribution was made. This will be 2003.*

### **What steps do you and John take to complete this distribution?**

To complete the distribution, you and John need to fill out a distribution form signifying that he is withdrawing a current-year contribution.\* This means John will use the distribution Code of "P1." John receives a check for \$3,150—\$3,000 for the return of the contribution, and \$150 for the interest

earned while the money was deposited in your institution. (If you are not familiar with IRA distribution codes, call CWF at 800-346-3961 and request a sample of IRA Distribution Form #57.)

When John has his taxes prepared for 2003, he can make one or two mistakes resulting from this distribution.

1. He might fail to report the \$3,000 on his 2003 tax return, and/or
2. He might fail to report the \$150 of interest on his 2003 income tax return.

### **How can you help John avoid either of these mistakes?**

CWF strongly recommends that you provide Mr. Black with CWF's IRA Form #67. The IRS requires an IRA custodian to furnish a special disclosure in this situation. He should take this form with him to his tax preparer. A completed sample of Form #67 is shown on the next page. This form fulfills the same disclosure purpose as the 1099-R.

### **Why is this form necessary?**

After all, won't you be sending John Black a 1099-R showing what his distribution and earnings are relevant to this contribution and its subsequent withdrawal? While that is true, keep in mind that you have already issued your 1099-Rs for the year 2003—these were sent out prior to January 31, 2004. John Black will not receive a 2004 1099-R for this particular distribution until January 2005.

A completed sample of the 2004 1099-R, which will be mailed in January 2005, is shown on page 3. The dollar information repeats what John will have received if you provided him with CWF's Form #67—also shown on page 3.

### **Is it necessary for John to amend his return?**

Hopefully, John and his tax preparer waited with filing his 2003 tax return so that this withdrawal of his contribution will be properly reflected on his 2003 tax return. If John's 2003 tax return has already been filed, an amended return should be filed as soon as possible.

Note that you will not check box 2b of the 1099-R, "taxable amount not determined" because you have determined that the only amount to be taxed is the income portion.

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\*Definition of "Current-Year Contribution": A current-year contribution is one for which the tax deadline (plus extensions) has not yet passed. Thus, a contribution made at any time in 2003, for 2003, or between January 1 2003, and April 15, 2004 (during the carryback period) is considered a current-year 2003 contribution.

**Withdrawing a 2003 IRA Contribution in the Year 2004,  
Continued from page 2**

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0119		Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.	
PAYER'S name, street address, city, state, and ZIP code <b>First National Bank 111 Main Street Anytown, MN 55111</b>		1 Gross distribution <b>\$ 3000.00</b>	2004		Form 1099-R
		2a Taxable amount <b>\$ 150.00</b>			
PAYER'S Federal identification number <b>11-1111111</b>		3 Capital gain (included in box 2a) \$		4 Federal income tax withheld \$	Copy C For Recipient's Records
RECIPIENT'S identification number <b>111-11-1111</b>		5 Employee contributions or insurance premiums \$		6 Net unrealized appreciation in employer's securities \$	
RECIPIENT'S name <b>John Black</b>		7 Distribution code(s) <b>P1</b>		8 Other \$	This information is being furnished to the Internal Revenue Service.
Street address (including apt. no.) <b>333 Fulton Avenue</b>		9a Your percentage of total distribution %		9b Total employee contributions \$	
City, state, and ZIP code <b>Anytown, MN 55111</b>		10 State tax withheld \$		11 State/Payer's state no. \$	12 State distribution \$
Account number (optional) <b>Anytown, MN 55111</b>		13 Local tax withheld \$		14 Name of locality \$	15 Local distribution \$

Form 1099-R (keep for your records) Department of the Treasury - Internal Revenue Service

**Special Explanation Regarding the Withdrawal  
of a 2003 "Current-Year" Contribution**

Custodian/Trustee: **First National Bank, 111 Main Street, Anytown, MN 55111**

Accountholder's Name: **John Black**

Social Security Number: **111-11-1111** IRA Account Number: **0111111111**

This form explains to you, the Accountholder, the complex rules for the withdrawal of a "current-year" contribution. A current-year contribution is one for which the tax deadline (plus extensions) has not yet passed. Thus, a contribution made at any time in 2003, for 2003, or between January 1, 2003, and April 15, 2004, for 2003 (during the carryback period) is considered a current-year contribution for 2003.

If you satisfy the following three (3) requirements, you will not be taxed on the withdrawal of a 2003 current-year contribution from your IRA.

- 1) You must withdraw the contribution by April 15, 2004 (plus extensions) or such other date as is explained on the reverse side,
- 2) No deduction must have been allowed for the contribution for the tax year in question; and
- 3) Any interest or other income earned by the contribution must also be withdrawn. The interest or other income earned on this contribution must be included in your gross income, and the 10% additional tax on a distribution prior to age 59½ must be paid, if applicable.

**Accountholder's Instructions to Withdraw and Signature**

✓ On **June 1, 2003** (specify date) I contributed \$ **3,000.00** to my IRA account for the 2003 tax year. On this date **April 1, 2004**, I hereby instruct you (the custodian/trustee) to withdraw \$ **3,000.00** plus the related income of **150.00**.

Signature of Accountholder \_\_\_\_\_ Date **April 1, 2004**

**Special Explanation by Custodian/Trustee—  
Because Action is Required by the Accountholder**

✓ On **April 1, 2004** (specify date) we, as custodian/trustee of your IRA account, distributed to you, the accountholder, \$ **3,150.00** of which **\$3,000.00** is the return of your contribution and \$ **150.00** is the related income (i.e. earnings/interest).

You must reflect on your Federal income tax return all amounts distributed to you. However, you will reflect two amounts on your Federal income tax return: the gross amount and the taxable amount. We expressly recommend that you consult with your tax advisor or preparer, or that you review IRS Publication 590. The following paragraphs discuss the Federal income tax consequences.

You have withdrawn a 2003 current-year contribution. You must reflect this distribution on the tax return for the year in which you made the contribution and not the year in which it was withdrawn, or for the tax year for which the contribution was made.



## Recharacterizing a 2003 Contribution in 2004

This time of year is the season for recharacterizations. People are visiting their tax accountants. The accountants will be telling some of your accountholders they were ineligible to convert their traditional IRA to a Roth IRA in 2003, or, if eligible to perform the conversion transaction, that it was not in their best interest to have done so. Or, they may tell the accountholder that they were ineligible to make a \$3,000/\$3,500 contribution to their Roth IRA or that they do not wish to make their contribution to the traditional IRA, as it is non-deductible. The point is—you, as an IRA custodian or trustee, can expect to see some of your IRA accountholders instruct you that they want to recharacterize a contribution made in 2003, for 2003, before he or she files a 2003 federal income tax return in 2004. Most such accountholders will normally complete the recharacterization on or before the tax-filing deadline for 2003. This is April 15, 2004. However, a person will have until October 15, 2004, to recharacterize a contribution. A person, who timely files his or her 2004 income tax return without having made a recharacterization, may file an amended return and still make the recharacterization within six months of the due date of his or her return, excluding extensions.

This explanation focuses on how you can assist your customer(s) to understand how he or she will need to handle the recharacterization on his or her 2003 income tax return. Recharacterizations are confusing to everyone involved. This is especially true for 2003 contributions which are recharacterized in 2004, because, as with excess contributions, these recharacterization transactions will be reported on the 2004 Form 1099-R and the 2004 Form 5498, which are not furnished until January of 2005 and May 2005. These forms obviously arrive well after the time the accountholder needs the information to file his or her 2003 federal income tax return. This is why the IRS requires an IRA custodian to furnish a written explanation to the accountholder. Also, be aware that the IRS has not yet issued the 2004 versions of Forms 1099-R and 5498. For this article, we have used the "2003" forms and merely inserted the year "2004" over "2003" on these documents.

Three situations are illustrated: (1) recharacterizing a Roth IRA contribution to be a contribution to a traditional IRA; (2) recharacterizing a contribution to a traditional IRA to be a contribution to a Roth IRA, and (3) recharacterizing a conversion contribution.

### Situation #1. Annual Roth IRA Contribution Recharacterized to a Traditional IRA Contribution

Lisa Water made a \$3,000 contribution to a Roth IRA on 1-10-03, for 2003. The fair market value of this IRA as of 12-31-03 was \$3,100. Lisa is not married, and she is not an active participant in an employer-sponsored plan. Her MAGI


for 2003 was \$123,000. Therefore, she has determined that she is not eligible to make a contribution to a Roth IRA. There were earnings of \$180 related to the contribution of \$3,000 as of 3-3-04. One of the methods to correct an excess contribution is to recharacterize it. She chose to recharacterize this contribution, plus earnings, on 3-3-04. The fair market value of this IRA as of 12-31-04 will be \$3,400.

#### Step #1. Accountholder Must Instruct to Recharacterize

The individual must instruct you (the IRA custodian) to recharacterize. The individual is required to furnish you with very specific information. You can make his/her task easier by making available to your accountholder a form such as CWF's "Notice of Recharacterization of IRA Contribution" as set forth on page 7.

#### Step #2. You (the IRA Custodian) Must Furnish an Explanation to the Accountholder

You should furnish an explanation to your accountholder similar to the one below.

Special Explanation to Accountholder for an IRA Recharacterization for the 2003 Tax Year	
(Name of Accountholder) _____	
<p>The purpose of this special explanation is to provide you with information about your recharacterization. You recharacterized a contribution which you made for the 2003 tax year. You will need to properly report and explain your recharacterization when you file your 2003 federal income tax return. We have furnished to you a copy of the <i>IRA Recharacterization Form</i> which you executed. You will also want to review the 2003 instructions for Form 8606. The IRS' instructions require you, as the IRA accountholder, to attach an explanation to your income tax return indicating the original contribution amount, the amount which was recharacterized, and the amount of earnings which was recharacterized. You may attach a copy of the IRA Recharacterization Form for this purpose.</p> <p>In some situations you will need to do more than just attach an explanatory statement. If both the original contribution and the recharacterization occurred during 2003, then you must also include on the 2003 tax return the amount deemed distributed from the one IRA on Form 1040, line 15(a) (or similar form). This is the gross amount you recharacterized. You should also complete line 15(b), the taxable amount, with zero. If the recharacterization of the contribution for 2003 occurred in 2004 then you only need to attach the explanatory statement.</p>	
Accountholder _____	Date _____
Custodian _____	Date _____
<div>  IRA #56-TREX (1/03)           <span style="margin-left: 100px;">White — Custodian/Trustee    Yellow — Accountholder</span> <span style="float: right;">© 2003 Collin W. Fritz &amp; Associates, Ltd.</span> </div>	



## Recharacterizing a 2003 Contribution in 2004, Continued from page 4

### Step #3. You Will Prepare the Various Reporting Forms

1. You will prepare a 2003 Form 5498 to report the original contribution to the Roth IRA of \$3,000 as shown.

2003		VOID		CORRECTED	
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	
		2 Rollover contributions \$		2003	
		3 Roth IRA conversion amount \$		Form 5498	
TRUSTEE'S or ISSUER'S federal identification no.		PARTICIPANT'S social security number		4 Recharacterized contributions \$	
PARTICIPANT'S name		5 Fair market value of account \$3100.00		6 Life insurance cost included in box 1 \$	
Street address (including apt. no.)		7 IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA <input checked="" type="checkbox"/>		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.	
City, state, and ZIP code		8 SEP contributions \$		9 SIMPLE contributions \$	
Account number (optional)		10 Roth IRA contributions \$3000.00		11 Check if RMD for 2004 <input type="checkbox"/>	
Form 5498 Cat. No. 50010C Department of the Treasury - Internal Revenue Service					

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2. You will prepare a 2004 Form 1099-R to report the "deemed" distribution from the Roth IRA to the traditional IRA. It should be reported as follows. Box 2 is to be completed with the gross distribution amount (\$3,180) and box 2a is to be completed with a 0.00. The reason code in box 7 is to be an "R" for recharacterization.

2004		CORRECTED (if checked)			
PAYER'S name, street address, city, state, and ZIP code		1 Gross distribution \$3180.00		OMB No. 1545-0119	
		2a Taxable amount \$0.00		2004	
		2b Taxable amount not determined <input type="checkbox"/>		Form 1099-R	
PAYER'S federal identification number		3 Capital gain (included in box 2a) \$		4 Federal income tax withheld \$	
RECIPIENT'S identification number		5 Employee contributions or insurance premiums \$		6 Net unrealized appreciation in employer's securities \$	
RECIPIENT'S name		7 Distribution code(s) R		8 Other <input type="checkbox"/>	
Street address (including apt. no.)		9a Your percentage of total distribution %		9b Total employee contributions \$	
City, state, and ZIP code		10 State tax withheld \$		11 State/Payer's state no. \$	
Account number (optional)		13 Local tax withheld \$		14 Name of locality \$	
		15 Local distribution \$		12 State distribution \$	
Form 1099-R (keep for your records) Department of the Treasury - Internal Revenue Service					

3. You will prepare a 2004 Form 5498 to report the recharacterized contribution (plus earnings) to the traditional IRA of \$3,180. It should be reported as shown below.

2004		VOID		CORRECTED	
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	
		2 Rollover contributions \$		2004	
		3 Roth IRA conversion amount \$		Form 5498	
TRUSTEE'S or ISSUER'S federal identification no.		PARTICIPANT'S social security number		4 Recharacterized contributions \$3180.00	
PARTICIPANT'S name		5 Fair market value of account \$3400.00		6 Life insurance cost included in box 1 \$	
Street address (including apt. no.)		7 IRA <input checked="" type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA <input type="checkbox"/>		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.	
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					

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### Situation #2. Annual Traditional IRA Contribution Recharacterized to be a Roth IRA Contribution

Sara Roe made a \$2,000 contribution to a traditional IRA on 2-10-03, for 2003 rather than a Roth IRA. The fair market value of this traditional IRA was \$2,125 as of 12-31-03. Sara is not married. She is an active participant in an employer-sponsored plan. Her MAGI was \$92,000. There were earnings of \$190 related to the contribution of \$2,000 as of 2-20-04. Sara has determined on 2-20-04 she will recharacterize her traditional IRA contribution to be a Roth IRA contribution because she is not able to claim a deduction for her \$2,000 contribution to the traditional IRA. The fair market value of this IRA as of 12-31-04 will be \$2,300.

#### Step #1. Accountholder Must Instruct to Recharacterize

The individual must instruct you (the IRA custodian) to recharacterize. The individual is required to furnish you with very specific information. You can make his or her task easier by making available to your accountholder a form such as CWF's "Notice of Recharacterization of IRA Contribution" as set forth on page 7, or a similar form.

#### Step #2. You (IRA Custodian) Must Furnish an Explanation to the Accountholder

You should furnish your accountholder an explanation similar to the one shown in Step #2 of Situation #1.

#### Step #3. You Will Prepare the Various Reporting Forms

1. You will prepare a 2003 Form 5498 to report the original contribution to the traditional IRA of \$2,000. It should be reported as shown below:

2003		VOID		CORRECTED	
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) \$2000.00		OMB No. 1545-0747	
		2 Rollover contributions \$		2003	
		3 Roth IRA conversion amount \$		Form 5498	
TRUSTEE'S or ISSUER'S federal identification no.		PARTICIPANT'S social security number		4 Recharacterized contributions \$	
PARTICIPANT'S name		5 Fair market value of account \$2125.00		6 Life insurance cost included in box 1 \$	
Street address (including apt. no.)		7 IRA <input checked="" type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA <input type="checkbox"/>		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.	
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					

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2. You will prepare a 2004 Form 1099-R to report the "deemed" distribution from the traditional IRA to the Roth IRA. It should be reported as follows. Box 1 is to be completed with the gross distribution amount (\$2,190) and box 2a is to be completed 0.00. The reason code in box 7 is to be an "R" for recharacterization.

**Recharacterizing a 2003 Contribution in 2004,  
Continued from page 5**

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0119		<b>Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.</b>
PAYER'S name, street address, city, state, and ZIP code		1 Gross distribution <b>\$ 2190.00</b>		
PAYER'S Federal identification number		2a Taxable amount <b>\$ 0.00</b>		<b>2004</b> Form 1099-R
RECIPIENT'S identification number		2b Taxable amount not determined <input type="checkbox"/> Total distribution <input type="checkbox"/>		
RECIPIENT'S name		3 Capital gain (included in box 2a) \$		<b>Copy C For Recipient's Records</b>
Street address (including apt. no.)		4 Federal income tax withheld \$		
City, state, and ZIP code		5 Employee contributions or insurance premiums \$		This information is being furnished to the Internal Revenue Service.
Account number (optional)		6 Net unrealized appreciation in employer's securities \$		
		7 Distribution code(s) <b>R</b>		8 Other \$
		9a Your percentage of total distribution %		
		9b Total employee contributions \$		10 State tax withheld \$
		11 State/Payer's state no. \$		
		12 State distribution \$		13 Local tax withheld \$
		14 Name of locality \$		
		15 Local distribution \$		

Form 1099-R (keep for your records) Department of the Treasury - Internal Revenue Service

3. You will prepare a 2004 Form 5498 to report the recharacterized contribution (plus earnings) to the Roth IRA of \$2,000. It should be reported as shown below.

<b>2628</b> <input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		OMB No. 1545-0747		<b>IRA Contribution Information</b>
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) \$		
TRUSTEE'S or ISSUER'S Federal identification no.		2 Rollover contributions \$		<b>2004</b> Form 5498
PARTICIPANT'S social security number		3 Roth IRA conversion amount \$		
PARTICIPANT'S name		4 Recharacterized contributions <b>\$ 2190.00</b>		<b>Copy A For Internal Revenue Service Center File with Form 1096.</b> For Privacy Act and Paperwork Reduction Act Notice, see the 2003 General Instructions for Forms 1099, 1098, 5498, and W-2G.
Street address (including apt. no.)		5 Fair market value of account \$ <b>2300.00</b>		
City, state, and ZIP code		6 Life insurance cost included in box 1 \$		7 IRA SEP SIMPLE Roth IRA <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input checked="" type="checkbox"/>
Account number (optional)		8 SEP contributions \$		
		9 SIMPLE contributions \$		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  
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**Situation #3. Recharacterizing a Conversion Contribution from a Traditional IRA to a Roth IRA**

Francoise Bell converted \$30,000 from her traditional IRA to a Roth IRA on 1-15-03. The fair market value of this Roth IRA was \$33,000 as of 12-31-03. She is not married. On 3-1-04 her accountant has told her she was not eligible to make the Roth IRA conversion contribution for 2003, as her MAGI was \$103,000. The related income has been \$3,900. The recharacterized amount is \$33,900. In order to eliminate this excess contribution, she elects to recharacterize this conversion contribution on 3-1-04. The fair market value of the traditional IRA as of 12-31-04 will be \$37,000.

**Step #1. Accountholder Must Instruct to Recharacterize**

The individual must instruct you (the IRA custodian) to recharacterize. The individual is required to furnish you with very specific information. You can make his or her task easier by making available to your accountholder a form such as CWF's "Notice of Recharacterization of IRA Contribution" set forth on page 7 or a similar form.

**Step #2. You (IRA Custodian) Must Furnish an Explanation to the Accountholder**

You should furnish your accountholder an explanation similar to the one shown in Step #2 of Situation #1.

**Step #3. You Will Prepare the Various Reporting Forms**

1. You will prepare a 2003 Form 5498 to report the original conversion contribution to the Roth IRA of \$30,000 as shown below:

<b>2628</b> <input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		OMB No. 1545-0747		<b>IRA Contribution Information</b>
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) \$		
TRUSTEE'S or ISSUER'S Federal identification no.		2 Rollover contributions \$		<b>2003</b> Form 5498
PARTICIPANT'S social security number		3 Roth IRA conversion amount <b>\$ 30000.00</b>		
PARTICIPANT'S name		4 Recharacterized contributions \$		<b>Copy A For Internal Revenue Service Center File with Form 1096.</b> For Privacy Act and Paperwork Reduction Act Notice, see the 2003 General Instructions for Forms 1099, 1098, 5498, and W-2G.
Street address (including apt. no.)		5 Fair market value of account \$ <b>33000.00</b>		
City, state, and ZIP code		6 Life insurance cost included in box 1 \$		7 IRA SEP SIMPLE Roth IRA <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input checked="" type="checkbox"/>
Account number (optional)		8 SEP contributions \$		
		9 SIMPLE contributions \$		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  
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2. You will prepare a 2004 Form 1099-R to report the "deemed" distribution from the Roth IRA to the traditional IRA. It should be reported as follows. Box 1 is to be completed with the gross distribution amount (\$33,900) and box 2a is to be completed 0.00. The reason code in box 7 is to be an "R" for recharacterization.

<input type="checkbox"/> CORRECTED (if checked)		OMB No. 1545-0119		<b>Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.</b>
PAYER'S name, street address, city, state, and ZIP code		1 Gross distribution <b>\$ 33900.00</b>		
PAYER'S Federal identification number		2a Taxable amount <b>\$ 0.00</b>		<b>2004</b> Form 1099-R
RECIPIENT'S identification number		2b Taxable amount not determined <input type="checkbox"/> Total distribution <input type="checkbox"/>		
RECIPIENT'S name		3 Capital gain (included in box 2a) \$		<b>Copy C For Recipient's Records</b>
Street address (including apt. no.)		4 Federal income tax withheld \$		
City, state, and ZIP code		5 Employee contributions or insurance premiums \$		6 Net unrealized appreciation in employer's securities \$
Account number (optional)		7 Distribution code(s) <b>R</b>		
		8 Other \$		9a Your percentage of total distribution %
		9b Total employee contributions \$		
		10 State tax withheld \$		11 State/Payer's state no. \$
		12 State distribution \$		
		13 Local tax withheld \$		14 Name of locality \$
		15 Local distribution \$		

Form 1099-R (keep for your records) Department of the Treasury - Internal Revenue Service

## Recharacterizing a 2003 Contribution in 2004, Continued from page 8

3. Prepare a 2004 Form 5498 to report the recharacterized contribution (plu52220

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2004 <input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		OMB No. 1545-0747		
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) \$	2004 Form 5498	
TRUSTEE'S or ISSUER'S federal identification no.		2 Rollover contributions \$		
PARTICIPANT'S social security number		3 Roth IRA conversion amount \$	4 Recharacterized contributions \$ 33900.00	
PARTICIPANT'S name		5 Fair market value of account \$ 37000.00	6 Life insurance cost included in box 1 \$	
Street address (including apt. no.)		7 IRA <input checked="" type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA <input type="checkbox"/>	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.	
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				
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## CWF'S Form 54-TR

### Notice of Recharacterization of IRA Contribution

#### To: Current Custodian/Trustee

Name: \_\_\_\_\_ Date: \_\_\_\_\_  
Address: \_\_\_\_\_  
City/State/Zip: \_\_\_\_\_  
Phone: (\_\_\_\_\_) \_\_\_\_\_

#### From: Depositor or Grantor

Name: \_\_\_\_\_ SSN: \_\_\_\_\_  
Address: \_\_\_\_\_ Date of Birth: \_\_\_\_\_  
City/State/Zip: \_\_\_\_\_ Phone: — Home: \_\_\_\_\_  
Work: \_\_\_\_\_

I hereby instruct you that I wish to irrevocably recharacterize my previous contribution. The successor IRA will be with the ☐ current custodian/trustee or ☐ a successor custodian/trustee as indicated below. If I have indicated a successor custodian/trustee, then you are to issue a check for the amount indicated below to the successor custodian or trustee. I understand I must provide the following information to have my previous contribution recharacterized:

#### The Original Contribution

Account Number: \_\_\_\_\_  
Date of Contribution: \_\_\_\_\_  
Amount: \_\_\_\_\_

#### The Recharacterized Contribution

Account Number: \_\_\_\_\_  
Date of Contribution: \_\_\_\_\_  
Amount: \_\_\_\_\_

#### Type of Original Contribution (Check only one)

- ☐ 1. Conversion/Rollover to Roth IRA  
☐ 2. Annual Contribution to a Roth IRA for \_\_\_\_\_ tax year  
☐ 3. Annual Contribution to a traditional IRA for \_\_\_\_\_ tax year

#### Type of Recharacterized Contribution

- ☐ 1. Rollover to a traditional IRA  
☐ 2. Annual contribution to a traditional IRA for the same tax year  
☐ 3. Annual Contribution to a Roth IRA for the same tax year

#### Instruction and Amount to Recharacterize

##### I elect to recharacterize \$ \_\_\_\_\_

Which is ☐ all or ☐ a portion of my original contribution.

It is adjusted by:

- a. Related Earnings (losses) \_\_\_\_\_  
b. Interest Penalty Fee \_\_\_\_\_  
c. Administrative Fee \_\_\_\_\_  
d. Other \_\_\_\_\_  
e. Recharacterized Net Amount \_\_\_\_\_

☐ Liquidate all of my accounts and transfer the cash proceeds by sending a check to the successor custodian/trustee;

☐ Liquidate the accounts I specify below and transfer the cash proceeds by sending a check to the successor custodian/trustee:

☐ Transfer all such assets "in kind" to the successor custodian/trustee;

☐ Transfer "in kind" the assets I specify below to the successor custodian/trustee:

I instruct you to transfer the recharacterized net amount to the successor custodian/trustee. I want this recharacterized net amount to come from the following assets held within my referenced IRA and paid in the instructed manner. I understand that there may be various fees associated with liquidating and/or transferring such assets in kind. These fees are set forth above. I authorize you to deduct such fees from the IRA.

I acknowledge that you have instructed me to consult with my legal or tax advisor because of the complexity and importance of this matter. This recharacterization is being made on or before the due date (including extensions) for filing my individual Federal income tax return for the taxable year for which the contribution was made. I expressly assume all responsibility for this recharacterization of IRA funds. I realize that my election to recharacterize my contribution is irrevocable.

Signature of Depositor or Grantor: \_\_\_\_\_

Date: \_\_\_\_\_

#### Acknowledgment of Current IRA Custodian/Trustee:

We acknowledge receiving your recharacterization instruction. We will report the original contribution on Form 5498, showing the character of the contribution (annual, conversion, etc.) and will report the distribution for recharacterization on Form 1099-R per the current IRS instructions. If your recharacterized contribution has been made into an IRA that you maintain with us, then we will also report the aforementioned contribution as a recharacterized contribution on a Form 5498 (Box 4).

Signature of Current Custodian/Trustee: \_\_\_\_\_

Date: \_\_\_\_\_

#### Acceptance by Successor IRA Custodian/Trustee:

We, the successor custodian/trustee, agree to report this recharacterized contribution as identified above as a recharacterized contribution on Form 5498 and agree to accept this contribution as if it had originally been made to us rather than the previous trustee/custodian.

Successor Custodian/Trustee: \_\_\_\_\_

Phone: \_\_\_\_\_

Address: \_\_\_\_\_

City/State/Zip: \_\_\_\_\_

Signature of Successor Custodian/Trustee: \_\_\_\_\_

Date: \_\_\_\_\_

IRA #54-TR (2/02)

White — Original Custodian/Trustee Yellow — Successor Custodian/Trustee Pink — Depositor/Grantor

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### Special Explanation to Accountholder for an IRA Recharacterization for the 2003 Tax Year

(Name of Accountholder)

The purpose of this special explanation is to provide you with information about your recharacterization. You recharacterized a contribution which you made for the 2003 tax year. You must properly report and explain your recharacterization when you file your 2003 tax return. See the instructions for Form 8606 for more details.

### Special Explanation to Accountholder for an IRA Recharacterization for the 2004 Tax Year

(Name of Accountholder)

The purpose of this special explanation is to provide you with information about your recharacterization. You recharacterized a contribution which you made for the 2004 tax year. You will need to properly report and explain your recharacterization when you file your 2004 federal income tax return. We have furnished to you a copy of the *IRA Recharacterization Form* which you executed. You will also want to review the 2004 instructions for Form 8606. The IRS' instructions require you, as the IRA accountholder, to attach an explanation to your income tax return indicating the original contribution amount, the amount which was recharacterized, and the amount of earnings which was recharacterized. You may attach a copy of the *IRA Recharacterization Form* for this purpose.

In some situations you will need to do more than just attach an explanatory statement. If both the original contribution and the recharacterization occurred during 2004, then you must also include on the 2004 tax return the amount deemed distributed from the one IRA on Form 1040, line 15(a) (or similar form). This is the gross amount you recharacterized. You should also complete line 15(b), the taxable amount, with zero. If the recharacterization of the contribution for 2004 occurred in 2005 then you only need to attach the explanatory statement.

Accountholder \_\_\_\_\_ Date \_\_\_\_\_  
Custodian \_\_\_\_\_ Date \_\_\_\_\_

IRA #56-TREX (11/03)

White — Custodian/Trustee Yellow — Accountholder

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## 2004 Contribution Limits for Single-Participant Plans

Although most financial institutions are afraid of offering SEP plans, SIMPLE plans and the one-person 401(k) plans, we have decided to set forth a comparative contribution chart for 2004. There are times when your self-employed customers will benefit greatly by being able to make a contribution to a SEP, SIMPLE or 401(k) plan. Many of your customers will want to take advantage of the much higher contribution limits. This is especially true as the economy improves.

### Maximum Contribution Comparison

Sole Proprietor Net Profits	"Net Profits, Less 1/2 SE Tax	SIMPLE IRA	SEP/ Profit Sharing/ Money Purchase	Single-Participant 401(k) *	"% of Net Profit, Less 1/2 SE Tax"
\$ 1,000	\$ 929	\$ 929	\$ 186	\$ 929	100%
5,000	4,647	4,647	929	4,647	100%
10,000	9,294	9,277	1,859	9,294	100%
17,486	16,251	9,484	3,250	16,250	100%
30,000	27,881	9,831	5,576	18,576	67%
50,000	46,468	10,385	9,294	22,294	48%
75,000	69,701	11,078	13,940	26,940	39%
100,000	93,211	11,771	18,642	31,642	34%
125,000	117,876	12,463	23,575	36,575	31%
147,422	139,998	13,084	28,000	41,000	29%
150,000	142,542	13,156	28,508	41,000	29%
175,000	167,207	13,848	33,441	41,000	25%
205,000	196,805	14,680	39,361	41,000	21%
213,304	204,998	14,910	41,000	41,000	20%

\* Maximum single-participant 401(k) contribution limits do not reflect the additional \$3,000 "catch-up" contribution available to individuals age 50 or older.

\$17,486 represents the last amount where 100% is contributed and deductible.

\$147,422 represents where one first reaches the level of \$41,000 combined.

\$213,304 represents the amount of net profit necessary to accumulate \$41,000 without needing a 401(k) deferral. Profit sharing contribution only.

Note: Elective deferral limit for 2004 is \$13,000 and \$16,000 if age 50 or older.

The chart above illustrates that a person, in certain situations will be able to have a combined contribution (elective deferral plus the standard profit sharing contribution) of much more than 25% of his compensation. This chart illustrates that generally much larger contributions are permitted by the 401(k) plan versus the SEP, SIMPLE or profit sharing plans. However, at lower income levels, the SIMPLE plan will be very attractive.

Also remember that the one-person 401(k) plan can have a loan feature which the SEP and SIMPLE do not have. CWF will be glad to assist you or your customers to establish one of these "employer" plans. Call us at 1-800-346-3961 for additional information.