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President Bush Re-Proposes Bold Changes to IRAs and Elective Deferral Plans

On January 31, 2003, President Bush proposed a number of bold (radical) changes to the laws governing traditional IRAs, Roth IRAs, Coverdell Education Savings Accounts, Archer Medical Savings Accounts, Qualified Tuition Plans (section 529 Plans), 401(k) plans, 403(b) plans, and section 457 plans and SIMPLE IRA plans. With some modifications, President Bush has now re-proposed these changes.

Here is our summary of President Bush's proposals as set forth in a public release by the U. S. Treasury on February 7, 2005.

His proposals themselves are an overview, and there is still much detail which is unknown. It is too early to know how many of these proposals will be enacted into law.

Three New Accounts are proposed—Retirement Savings Accounts (RSAs), Lifetime Savings Accounts (LSAs) and Employer Retirement Savings Accounts (ERSAs). The first two are individual savings plans, and the last one creates ERSAs to promote and vastly simplify employer plans with elective deferral provisions. Rather than having separate rules for 401(k) plans, 403(b) plans, SIMPLE IRA plans, and governmental section 457 plans, there will be just one set of rules as set forth for ERSAs.

The RSA—The purpose of the RSA is to provide funds for a person's retirement. As discussed in prior newsletters, the traditional IRA, over the years, has

evolved into serving purposes more than just retirement. That progression would be stopped. This would be a retirement account. It would be very similar to the existing Roth IRA account. The maximum annual contribution limit would be \$5,000 per year, and a person would be required to have earned income to make the contribution. These new rules would apply for 2006 and subsequent years. However, there would be no limitation based on age or amount of modified adjusted gross income. There would be no tax deduction granted for making the contributions, but the earnings of the account would be tax free if distributed to the accountholder when he or she was age 58 or older or disabled, or to a beneficiary after the accountholder died. Married individuals could roll amounts from their RSA over to their spouses' RSA. Qualified distributions from the retirement account would be distributions made after age 58 or in the event of death or disability. Any other distribution would be a nonqualified distribution and, as with current nonqualified distributions from Roth IRAs, would be includable in income (to the extent it exceeds basis) and subject to a 10 percent additional tax. Distributions would be deemed to come from basis first. As with current Roth IRA law, no minimum required distribution rules would apply to RSAs during the account owner's lifetime. Presumably, the rules

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which mandate distributions to a Roth IRA beneficiary would apply to the new RSA accounts. However, this topic was not addressed in the President's proposals, as it primarily focused on contributions. The \$5,000 limit would be indexed for inflation. The impact of the RSA on traditional IRAs and Roth IRAs would be as follows.

Traditional IRAs—Traditional IRAs would not be repealed or eliminated. As written, December 31, 2005 (and not April 15, 2006) would be the last day a person would be able to make a contribution (other than for rollovers and transfers) to a traditional IRA. To encourage people to convert or roll over their traditional IRA to the Retirement Savings Account before January 1, 2007, their distribution would be taxed over four years (2006-2009). For conversions on or after January 1, 2007, the tax on the distribution would be due for the year of the conversion. Unlike under existing law, all traditional IRA accountholders would be eligible to convert their traditional IRA. That is, the eligibility requirement of having less than \$100,000 of modified adjusted gross income would no longer apply.

It does not appear that any traditional IRA accountholder would be required to convert his or her traditional IRA funds to the Retirement Savings Account. All existing traditional IRA distribution rules would continue to apply to both IRA accountholders and beneficiaries. The traditional IRA will continue to exist to handle rollovers from employer-sponsored retirement plans.

Roth IRAs—They would continue to exist, but the account would be renamed to be a Retirement Savings Accounts (RSAs). There would be new rules defining a qualified distribution. There will be only three qualifying events (age 58, disability, or death). It appears that the first-time home buyer exception would not exist after December 31, 2005. The five-year requirement would be repealed for purposes of determining if a distribution is "qualified" (i.e. tax free).

Amounts converted to an RSA from a traditional IRA account would be subject to a five-year holding period. Distributions attributable to a conversion from a traditional IRA prior to the end of the five-year period starting with the year the conversion was made or, if

earlier, the date on which the individual turns 58, becomes disabled, or dies would be subject to an additional 10 percent early distribution tax on the entire amount. The five-year period is separately determined for each conversion contribution. To determine the amount attributable to a conversion, a distribution is treated as made in the following order: regular contributions; conversion contributions (on a first-in-first-out basis); earnings. To the extent a distribution is treated as made for a conversion contribution, it is treated as made first from the portion, if any, that was required to be included in gross income because of the conversion.

The LSA—The LSA is a non-retirement account and can be used for any type of savings purpose. For example, the LSA could be used for a child's education, a new home, healthcare needs, or for an individual to start their own business. It is clearly an account designed to encourage a person to save and invest. The annual contribution limit would be \$5,000 per year and a person would not be required to have earned income to make the contribution. The contribution must be cash. However, there would be no limitations based on age or amount of modified adjusted gross income. There would be no tax deduction granted for making the contributions, but the earnings of the account, when withdrawn, would be tax free regardless of the reason for the withdrawal. As with the Roth IRA, the earnings would come out of the IRA only after all contributions (annual or conversion) had been distributed. Contributions would start in 2006. The \$5,000 limit would be indexed for inflation.

The LSA will impact existing non-IRA tax-preferred accounts as follows.

- Contribution limits would apply to all accounts held in an individual's name, rather than to contributors. The LSA contribution limit would be indexed for inflation.

- Married individuals could roll amounts from their LSAs over to their spouses' LSAs. As with current Roth IRA law, no minimum required distribution rules would apply to LSAs during the account owner's lifetime.

**Changes to IRAs & Elective Deferral Plans,
Continued from page 2**

Coverdell Education Savings Accounts (CESA) and Qualified Tuition Plans (QTP's) — A person with a CESA would be eligible to convert the funds within the CESA to the LSA, but would not be required to do so. This right to convert would exist only if exercised on or before December 31, 2007. The right to contribute to a CESA will continue to exist after December 31, 2007.

Control over an account in a minor's name would be exercised exclusively for the benefit of the minor, until the minor reached the age of majority (determined under applicable state law), by the minor's parent or legal guardian acting in that capacity.

Taxpayers would be able to convert balances in Coverdell Education Savings Accounts (ESAs) and Section 529 Qualified Tuition Plans (QTPs) to LSA balances. All conversions made before January 1, 2007, would be on a tax-free basis, subject to the following limitations. An amount can be rolled into an individual's LSA from a QTP only if that individual was the beneficiary of the QTP or ESA as of December 31, 2004. The amount that can be rolled over to an LSA from an ESA is limited to the sum of the amount in the accounts as of December 31, 2004, plus any LSA from a QTP is limited to the sum of (i) the lesser of \$50,000 or the amount in the QTP as of December 31, 2004, plus (ii) any contributions and earnings to the QTP during 2005. Total rollovers to an individual's LSA attributable to 2005 contributions to the individual's ESAs and QTPs cannot exceed \$5,000 (plus any earnings on those contributions.)

QTPs would continue to exist as separate types of accounts, but could be offered inside an LSA.

**SET FORTH BELOW IS A Q & A FOR THESE TWO
NEW ACCOUNTS AS ORIGINALLY PROVIDED BY THE U.S.
TREASURY IN 2003 AND AS MODIFIED BY CWF IN 2005.**

I have been contributing to IRAs for years. Will I have to stop? After 2005, you will no longer be able to contribute to an IRA. However, your ability to contribute to both an LSA and an RSA, will give you much more flexibility to save for your future. You will be able to save up to \$5,000 (indexed in the future for inflation) in an LSA plus up to \$5,000 (indexed in the future for inflation) in an RSA for a total of \$10,000 in tax-preferred savings. In addition, you will have much

more flexibility to take distributions for what you deem appropriate when you deem it appropriate.

Will there be any income limitations on making contributions to LSAs or RSAs? There are no income limitations on making contributions to LSAs. You can make a contribution to an LSA even if you have no wage income. Thus, you can make contributions on behalf of your children or other family members, in order to help them save for home ownership, health emergencies, education, retirement, or other future costs. While there are no maximum income limitations on making contributions to RSAs, you may not contribute more than your compensation (wages) income to an RSA.

What tax benefits do I receive if contributions are not deductible? While all contributions to LSAs and RSAs will be nondeductible, all distributions from LSAs and RSAs (except for RSA distributions prior to age 58, death or disability) will be excludable from taxable income. As a result, all investment earnings can be distributed tax free. This is the same tax treatment as under current Roth-IRA law.

Can I convert my existing IRAs, ESAs, and QSTPs to an LSA or RSA? You may convert an ESA, or QSTP to an LSA anytime before January 1, 2007. In the case of a conversion of a QSTP or ESA, no amount would be taxable in the year of the conversion.

You may convert a traditional IRA to an RSA at any time. The amount converted will be taxable except to the extent that you have basis in your IRA. If you convert prior to January 1, 2007, you will be able to spread the tax on the conversion over a four-year period. For conversions on or after January 1, 2007, the total taxable amount will be included in your gross income for the year of the conversion.

Will the Saver's Credit still be available after the enactment of the LSA/RSA proposal? Yes. The Saver's Credit will continue to be available for elective deferrals and RSA contributions made after 2005. It would not be available with respect to LSA contributions.

**Changes to IRAs & Elective Deferral Plans,
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Who will be able to become trustees for the LSAs and RSAs?

The rules that now apply to IRAs regarding who can be a trustee will apply to LSAs and RSAs. Thus, the trustee will have to be a bank or another person who demonstrates to the IRS that the manner in which they will administer the trust will be consistent with the rules applicable to LSAs and IRAs.

Will LSAs and RSAs be permitted to be held in the form of an annuity?

Yes. LSAs and RSAs may be held in the form of a nontransferable annuity contract issued by an insurance company that meets the rules that currently apply to individual retirement annuities.

Can I make LSA or RSA contributions on behalf of other persons, such as my children or spouse?

Yes, you may make LSA or RSA contributions on behalf of any other individual. However, total contributions made on behalf of an individual may not exceed \$5,000 for LSAs and \$5,000 (or compensation income, if less) for RSAs. In the case of a married couple filing jointly, RSA contributions up to \$5,000 can be made for each spouse (including, for example, a homemaker who does not work outside the home) if the combined compensation of both spouses is at least equal to the contributed amount.

Will catch-up contributions be available for LSAs or RSAs? Catch-up contributions will not be available for LSAs or RSAs, but the limits applicable to all individuals in LSAs and RSAs will be significantly greater than the existing IRA limits, even with catch-up.

The ERSA. The purpose of the ERSA as with the RSA is to provide funds for a person's retirement. The difference is that the ERSA is established pursuant to an employer plan which authorizes elective deferrals. Under existing law, there are five types of plans which allow for elective deferral contributions—401(k) plans, 403(b) plans, SIMPLE IRA plans, and governmental section 457 plans. President Bush's proposal is that as of January 1, 2006, the ERSA would replace these five plans. ERSA would follow existing, but simplified rules for 401(k) plans.

There will be further discussion of the proposed ERSA changes in upcoming months—if it looks like these changes will be enacted into law.

Understanding the Recharacterizing of a 2004 Contribution in 2005

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 2004, 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 2004, for 2004, before he or she files a 2004 federal income tax return in 2005. Most such accountholders will normally complete the recharacterization on or before the tax-filing deadline for 2004. This is April 15, 2005. However, a person will have until October 15, 2005, 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 2004 income tax return. Recharacterizations are confusing to everyone involved. This is especially true for 2004 contributions which are recharacterized in 2005, because, as with excess contributions, these recharacterization transactions will be reported on the 2005 Form 1099-R and the 2005 Form 5498, which are not furnished until January of 2006 and May 2006. These forms obviously arrive well after the time the accountholder needs the information to file his or her 2004 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 2005 versions of Forms 1099-R and

**Recharacterizing a Contribution,
Continued from page 4**

5498. For this article, we have used the "2004" forms and merely inserted the year "2005" over "2004" 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 1-10-04, for 2004. The fair market value of this IRA as of 12-31-04 was \$3,100. Lisa is not married, and she is not an active participant in an employer-sponsored plan. Her MAGI for 2004 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 3-3-05. One of the methods to correct an excess contribution is to recharacterize it. She chose to recharacterize this contribution, plus earnings, on 3-3-05. Assume the fair market value of this IRA as of 12-31-05 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 8.

**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 on page 8.

Step #3. You Will Prepare the Various Reporting Forms

1. You will prepare a 2004 Form 5498 to report the original contribution to the Roth IRA of \$3,000 as shown.

2004		VOID		CORRECTED	
1. IRAs contributions (other than rollovers) in boxes 2-4 and 6-10		2. Rollover contributions		3. Roth IRA conversion amount	
\$ 3,000		\$		\$	
4. Rollover contributions		5. Fair market value of account		6. Life insurance cost (included in box 1)	
\$		\$ 3,100		\$	
7. IRA, SEP, SIMPLE, ROTH, or 529		8. SEP contributions		9. SIMPLE contributions	
X		\$		\$	
10. Rollover contributions		11. Check if RMD for 2005			
\$ 3,000					

Form 5498 Cat. No. 50010C Department of the Treasury - Internal Revenue Service

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2. You will prepare a 2005 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.

2005		VOID		CORRECTED	
1. Gross distribution		2a. Taxable amount		3. Capital gain (included in box 2a)	
\$ 3,180		\$ 0.00		\$	
2b. Taxable amount not determined		4. Federal income tax withheld		5. Employee contributions or insurance premiums	
		\$		\$	
6. Net unrealized appreciation in employer's securities		7. Distribution code(s)		8. Other	
\$		R		\$	
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 Cat. No. 14430G Department of the Treasury - Internal Revenue Service

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**Recharacterizing a Contribution,
Continued from page 5**

3. You will prepare a 2005 Form 5498 to report the recharacterized contribution (plus earnings) to the traditional IRA of \$3,180. It should be reported as shown below.

2005		IRA Contribution Information	
1. TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code		1. IRA contributions (other than rollovers) in boxes 2-11 and 12-19	
2. Rollover contributions		2. Rollover contributions	
3. Roth IRA conversion amount		3. Roth IRA conversion amount	
4. Rollover contributions		4. Rollover contributions	
5. Fair market value of account		5. Fair market value of account	
6. Life insurance cost included in box 1		6. Life insurance cost included in box 1	
7. <input checked="" type="checkbox"/> IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA		7. <input checked="" type="checkbox"/> IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA	
8. SEP contributions		8. SEP contributions	
9. SIMPLE contributions		9. SIMPLE contributions	
10. Roth IRA contributions		10. Roth IRA contributions	
11. Check if RMD for 2005		11. Check if RMD for 2005	

Form 5498 Cat. No. 500100 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 2-10-04, for 2004, rather than a Roth IRA. The fair market value of this traditional IRA was \$2,125 as of 12-31-04. 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 2-20-05. Sara has determined, on 2-20-05, 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. Assume the fair market value of this IRA as of 12-31-05, 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 8, 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 2004 Form 5498 to report the original contribution to the traditional IRA of \$2,000. It should be reported as shown below:

2004		IRA Contribution Information	
1. TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code		1. IRA contributions (other than rollovers) in boxes 2-11 and 12-19	
2. Rollover contributions		2. Rollover contributions	
3. Roth IRA conversion amount		3. Roth IRA conversion amount	
4. Rollover contributions		4. Rollover contributions	
5. Fair market value of account		5. Fair market value of account	
6. Life insurance cost included in box 1		6. Life insurance cost included in box 1	
7. <input checked="" type="checkbox"/> IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA		7. <input checked="" type="checkbox"/> IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA	
8. SEP contributions		8. SEP contributions	
9. SIMPLE contributions		9. SIMPLE contributions	
10. Roth IRA contributions		10. Roth IRA contributions	
11. Check if RMD for 2005		11. Check if RMD for 2005	

Form 5498 Cat. No. 500100 Department of the Treasury - Internal Revenue Service

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2. You will prepare a 2005 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.

2005		Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.	
1. PAYER'S name, street address, city, state, and ZIP code		1. Gross distribution	
2. Taxable amount		2. Taxable amount	
3. Capital gain (included in box 2a)		3. Capital gain (included in box 2a)	
4. Federal income tax withheld		4. Federal income tax withheld	
5. Employee contributions or insurance premiums		5. Employee contributions or insurance premiums	
6. Net unrealized appreciation in employer's securities		6. Net unrealized appreciation in employer's securities	
7. Distribution code		7. Distribution code	
8. Other		8. Other	
9a. Your percentage of total distribution		9a. Your percentage of total distribution	
9b. Total employee contributions		9b. Total employee contributions	
10. State tax withheld		10. State tax withheld	
11. State/Payer's state no.		11. State/Payer's state no.	
12. State distribution		12. State distribution	
13. Local tax withheld		13. Local tax withheld	
14. Name of locality		14. Name of locality	
15. Local distribution		15. Local distribution	

Form 1099-R Cat. No. 144363 Department of the Treasury - Internal Revenue Service

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3. You will prepare a 2005 Form 5498 to report the recharacterized contribution (plus earnings) to the Roth IRA of \$2,000. It should be reported as shown below.

2005		IRA Contribution Information	
1. TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code		1. IRA contributions (other than rollovers) in boxes 2-11 and 12-19	
2. Rollover contributions		2. Rollover contributions	
3. Roth IRA conversion amount		3. Roth IRA conversion amount	
4. Rollover contributions		4. Rollover contributions	
5. Fair market value of account		5. Fair market value of account	
6. Life insurance cost included in box 1		6. Life insurance cost included in box 1	
7. <input type="checkbox"/> IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input checked="" type="checkbox"/> Roth IRA		7. <input type="checkbox"/> IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input checked="" type="checkbox"/> Roth IRA	
8. SEP contributions		8. SEP contributions	
9. SIMPLE contributions		9. SIMPLE contributions	
10. Roth IRA contributions		10. Roth IRA contributions	
11. Check if RMD for 2005		11. Check if RMD for 2005	

Form 5498 Cat. No. 500100 Department of the Treasury - Internal Revenue Service

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**Recharacterizing a Contribution,
Continued from page 6**

**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 1-15-04. The fair market value of this Roth IRA was \$33,000 as of 12-31-04. She is not married. On 3-1-05, her accountant told her she was not eligible to make the Roth IRA conversion contribution for 2004, as her MAGI was \$103,000. The related income is \$3,900. The recharacterized amount is \$33,900. In order to eliminate this excess contribution on 3-1-05. Assume the fair market value of the traditional IRA as of 12-31-05 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 8 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 2004 Form 5498 to report the original conversion contribution to the Roth IRA of \$30,000 as shown below:

2004		VOID	CORRECTED	OMB No. 1545-0047	
TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code		1 IRA contributions (other than rollovers) in boxes 2-4 and 8-10		2004	
		\$		Form 5498	
2 Rollover contributions		\$			
3 Roth IRA conversion amount		\$			
4 Recharacterized contributions		\$			
5 Fair market value of account		\$		33,000	
6 Life insurance cost included in box 1		\$			
7 IRA SEP SIMPLE ROTH		8 SEP contributions		9 SIMPLE contributions	
10 Rollover contributions		\$		30,000	
11 Check if RMD for 2005					
Form 5498		Cat. No. 50010C		Department of the Treasury - Internal Revenue Service	
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2. You will prepare a 2005 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.

9898		VOID	CORRECTED	OMB No. 1545-0119	
PAYER'S name, street address, city, state, and ZIP code		1 Gross distribution		2005	
		\$		Form 1099-R	
2a Taxable amount		\$		0.00	
2b Taxable amount not determined					
3 Capital gain (included in box 2a)		\$			
4 Federal income tax withheld		\$			
5 Employee contributions or insurance premiums		\$			
6 Net unrealized appreciation in employer's securities		\$			
7 Distribution code(s)		R			
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		Cat. No. 14430G		Department of the Treasury - Internal Revenue Service	
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3. Prepare a 2005 Form 5498 to report the recharacterized contribution (plus earnings) of \$33,900 to the traditional IRA. It should be reported as shown below:

2005		VOID	CORRECTED	OMB No. 1545-0047	
TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code		1 IRA contributions (other than rollovers) in boxes 2-4 and 8-10		2005	
		\$		Form 5498	
2 Rollover contributions		\$			
3 Roth IRA conversion amount		\$		33,900	
4 Recharacterized contributions		\$			
5 Fair market value of account		\$		37,000	
6 Life insurance cost included in box 1		\$			
7 IRA SEP SIMPLE ROTH		8 SEP contributions		9 SIMPLE contributions	
10 Rollover contributions		\$		30,000	
11 Check if RMD for 2005					
Form 5498		Cat. No. 50010C		Department of the Treasury - Internal Revenue Service	
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Conclusion. You will certainly be receiving requests to recharacterize, in calendar year 2005, a contribution which was made in calendar year 2004.

Taxpayers and their accountants are beginning to understand the concept of recharacterizing a contribution as a correction tool. The taxpayer (or accountant) will need to complete the Form 8606 to report the recharacterization. The instructions for the Form 8606 state the taxpayer is to attach a statement explaining the recharacterization. This explanation should indicate the total amount recharacterized, the original contribution, the earnings or loss, and the amount that is now deductible, if applicable. The instructions also indicate that an IRA custodian has the duty to furnish this same information to the accountholder.

Recharacterizing a Contribution,
Continued from page 7

CWF'S Form 54-TR

Notice of Recharacterization of IRA Contribution

To: Current Custodian/Trustee

Name:
Address:
City/State/Zip:
Phone: ()

Date:

From: Depositor or Grantor

Name:
Address:
City/State/Zip:

SSN:

Date of Birth:
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 a 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

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.

☐ 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 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 the 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 custodian/trustee.

Successor Custodian/Trustee:

Phone:

Address:

City/State/Zip:

Signature of Successor Custodian/Trustee:

Date:

☒ IRA 54-TR (2/05) White — Original Custodian/Trustee Yellow — Successor Custodian/Trustee Pink — Depositor/Grantor Blue — 2004/2005 IRA 54-TR (2/05) Blue — 2004/2005 IRA 54-TR (2/05)

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 _____

Special Explanation to Accountholder for an IRA
Recharacterization for the 2005 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 2005 tax year. You will need to properly report and explain your recharacterization when you file your 2005 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 2005 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 2005, then you must also include on the 2005 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 2005 occurred in 2006 then you only need to attach the explanatory statement.

Accountholder _____ Date _____

Custodian _____ Date _____