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



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Self-Audit of 5498 Reporting for 2008

2828 <input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		OMB No. 1545-0747		2008 Form 5498	IRA Contribution Information
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) \$			
		2 Rollover contributions \$			
TRUSTEE'S or ISSUER'S federal identification no.	PARTICIPANT'S social security number	3 Roth IRA conversion amount \$		4 Recharacterized contributions \$	
PARTICIPANT'S name		5 Fair market value of account \$		6 Life insurance cost included in box 1 \$	
Street address (including apt. no.)		7 <input type="checkbox"/> IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA			
City, state, and ZIP code		8 SEP contributions \$		9 SIMPLE contributions \$	
Account number (see instructions)		10 Roth IRA contributions \$		11 Check if RMD for 2009 <input type="checkbox"/>	

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

Do Not Cut or Separate Forms on This Page — Do Not Cut or Separate Forms on This Page

As an IRA custodian/trustee, you will be preparing the 5498 forms for 2008 and the magnetic media equivalent correctly. You must file this form with the IRS by June 1, 2009.

If you'd like to conduct a self-audit of your 5498s, ask yourself the following questions:

Question #1: “Did I prepare the form for as many IRA accountholders and beneficiaries as the rules require?” The IRS can assess a penalty for each Form 5498 that you missed.

An IRA custodian must prepare a Form 5498 for any IRA accountholder who falls into one of the following classifications. (Note that the IRS is concerned with getting certain contribution information and the IRA's fair market value (FMV) as of 12-31-xx, or the date of death. Regular, spousal, rollover, SEP, Roth Conversion, Recharacterizations and SIMPLE contributions are reported,

but transfer contributions are not.)

To audit 2008, the classifications are:

- A regular or spousal contribution made on behalf of an accountholder during the period of 1-1-08 to 4-15-09, but only if such contribution was made for the 2008 tax year;
- A rollover contribution made by the accountholder during the period of 1-1-08 to 12-31-08;
- A Roth conversion contribution by the accountholder during the period of 1-1-08 to 12-31-08;
- A Recharacterization contribution by the accountholder during the period of 1-1-08 to 12-31-08;
- An accountholder or a beneficiary who had an account balance as of 12-31-08;
- A deceased accountholder who had an account balance as of their date of death in 2008;

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**Self Audit,
Continued from page 1**

- A SEP contribution made during the period of 1-1-08 to 12-31-08;
- A SIMPLE contribution made during the period of 1-1-08 to 12-31-08;
- A Roth IRA contribution made on behalf of the accountholder during the period of 1-1-08 to 4-15-09, but only if such contribution was made for the 2008 tax year.

If a person falls into any of these classifications, then a 2008 Form 5498 must be generated for that person. Later, an example will be helpful in illustrating the application of these rules.

A Special Rule

A Form 5498 must be generated for each source of an IRA account. If a person has his or her own IRA, and then, as a beneficiary, inherits another IRA, the IRA custodian must generate two Form 5498s. If a person has a beneficiary's interest in his deceased mother's IRA, a beneficiary's interest in his deceased father's IRA, plus his own IRA, then the IRA custodian must generate three Form 5498s.

This separate IRA for each separate source of IRA funds also applies to surviving spouses. That is, if Jane Doe has her own IRA and she also is the sole beneficiary of her just-deceased husband's IRA (John Doe), then the IRA custodian must generate two Form 5498s for her. One will be for her personal IRA and the other will be "Jane Doe as IRA beneficiary of John Doe." Both forms will list her Social Security Number. It is assumed she did not treat his IRA as her own.

Note that the data processing departments and software vendors must devise systems which will generate these separate forms, or you must generate them manually. There will need to be some system code in addition to the Social Security Number to instruct the computer system to generate separate forms.

An Example — How many 5498 forms for 2008 must be prepared?

First Bank of Red Lake, USA had 1,800 IRAs as of 1-1-08. 1,570 of these were traditional IRAs, 215 were Roth IRAs, 10 were SEP-IRAs and 5 were SIMPLE-IRAs.

The following events took place in 2008, and between 1-1-08 and 4-15-09.

With Respect to the Traditional IRAs:

1. 100 IRAs were closed out in 2008. Of these 100, 25 had made contributions for 2008 before closing out. (Keep in mind that these 100/25 figures are included in the 1,570.)
2. Of the 1,570 accounts, only 450 made regular contributions for 2008, and only 95 made a rollover contribution.
3. 85 new IRAs with regular contributions were established in 2008, for 2008;
4. 135 new IRAs with regular contributions were established in 2009, for 2008.
5. 15 IRA accountholders died in 2008. Each had two IRA beneficiaries. 10 of the beneficiaries withdrew their shares (account balances) before 12-31-08.
6. 20 Keogh accountholders made contributions to their Keoghs for 2008.

How many 2008 Form 5498s is First Bank required to generate with respect to the traditional IRAs?

The Calculation

The answer is 1,735. How did we arrive at this number? There were 1,570 accounts to start with. This number is reduced by 75 because these accountholders closed out their accounts and made no other contributions. Result, 1,495. (A Form 5498 must be prepared for the 25 who made a 2008 contribution before closing out the account.) A Form 5498 must be prepared for each of the new IRAs — so add 220 (135 + 85). Result, 1,715.

The 15 deceased IRA accountholders were included in the original 1,800 or 1,570 traditional, and the rule is that you must always generate a Form 5498 for the year of death. So, there is nothing to be added or subtracted with respect to the decedents.

Finally, add 20 5498s for the beneficiaries who still had an account balance as of 12-31-08. Result, 1,735. There is no need or requirement to prepare a Form 5498 for those beneficiaries who have no account balance as of 12-31-08. Furthermore, the Form 5498 is for IRA reporting, so Keogh contributions or year-end balances should not be included on a Form 5498.

With respect to the Roth IRAs:

1. No Roth IRAs were closed out in 2008.
2. Of the 215 accounts, 100 made regular contributions for 2008, and only 20 made a rollover contribution.
3. 50 new Roth IRAs with regular contributions were established in 2008, for 2008;
4. 75 new Roth IRAs with regular contributions were established in 2009, for 2008.
5. One Roth IRA accountholder died in 2008. There were three beneficiaries.

How many 2008 Form 5498s is First Bank required to generate with respect to Roth IRAs?

The Calculation

The answer is 343. How did we arrive at this number? There were 215 accounts to start with. A Form 5498 must be prepared for each of the new IRAs — so add 125 (50 + 75). Result, 340.

The one deceased Roth IRA accountholder is included in the original 215, and the rule is that you must always generate a Form 5498 for the year of death. So, there is nothing to be added or subtracted with respect to the decedents.

Finally, add three 5498s for the beneficiaries who still had an account balance as of 12-31-08. Result, 343. There is no need or requirement to prepare a Form 5498 for those beneficiaries who have no account balance as of 12-31-08.

With Respect to SEP-IRAs:

1. 2 SEP-IRAs were closed out in 2008 with no other contributions.
2. 5 existing SEP-IRAs were funded in 2008.
3. 4 new SEP-IRAs were funded in 2008 for 2008.
4. 7 new SEP-IRAs were funded in 2009 for 2008.

How many 2008 Form 5498s are required to be generated with respect to SEP-IRAs? The answer is 12. There were 8 existing SEP-IRAs as of December 31, 2008 and there were also 4 new SEP-IRAs. The 7 new SEP IRAs opened in 2009 will be reported on the 2009 Form 5498.

With Respect to the SIMPLE-IRAs:

1. Additional contributions were made to all five of the SIMPLE-IRAs;
2. No SIMPLE-IRAs were closed out in 2008;
3. 3 SIMPLE-IRAs were transferred out during 2009;
4. 8 new SIMPLE-IRAs were set up in September of 2008.
5. 4 new SIMPLE-IRAs were set up in 2009.

How many 2008 Form 5498s are required with respect to SIMPLE-IRAs?

Thirteen. SIMPLE-IRAs are also reported on a calendar year basis. Transactions taking place in 2009 (even if for 2008) are not reported on the 2008 form.

Summary

A total of 2,103 Form 5498s must be prepared. This is the sum of:

Traditional IRAs	1,735
Roth IRAs	343
SEP IRAs	12
SIMPLE-IRAs	13
	<hr/>
	2,103

Payroll Deduction IRA Contributions

Payroll-Deduction IRA Programs have lost favor with businesses and with IRA Custodians. The concept of these programs is so simple—an employer decides to help its employees save for their retirement by forwarding funds withdrawn from an employee's paycheck to an IRA custodian. Although one normally thinks of a payroll-deduction program as dealing with traditional IRAs, there is no reason there are not payroll-deduction programs for Roth IRAs. Note that the word "program" is used and not the word "plan." There is generally no plan document for an IRA payroll-deduction program. The employer must be willing to transmit the IRA funds to the IRA custodian as selected by each employee. In general, a business should be willing to offer this special service to all employees.

What Are Payroll Deduction Contributions?

A payroll deduction IRA is a regular IRA that is funded by the accountholder who allows the money to be automatically deducted from his paycheck and deposited directly into his IRA account. Do not confuse the Payroll Deduction IRA with a Salary Reduction SEP or a SIMPLE-IRA plan. The accountholder/employee can elect to set up the deduction from his or her payroll on their own, or the employer can initiate the process. The employer, however, is not required to provide the payroll deduction service.

What is needed to have a payroll-deduction IRA program?

An employee needs to have established a traditional IRA and/or Roth IRA with an IRA custodian. The employee then needs to authorize the employer to deduct the IRA contribution amount from his paycheck.

The employer then must be willing to transmit the employee's authorized deduction contribution amount to the IRA custodian on a timely basis.

What contribution limits apply to payroll-deduction programs?

The standard IRA contribution limits apply, because it is the employee who is actually making the contribution for himself.

What administrative costs are associated with a payroll deduction program?

There will be costs associated with handling each employee's request, however, this cost should be nominal. An employer does not have any type of governmental reporting to submit under a payroll-deduction IRA program. The employer prepares an employee's Form W-2 in the usual manner regardless of whether or not an IRA program is in place. It is left up to the employee to properly reflect the tax effect of this traditional IRA contribution and/or Roth IRA contribution on his tax return. Since the employer has not made a contribution, it is generally not entitled to a deduction. However, any additional payroll costs the employer must pay to establish and operate the payroll program will be able to be claimed as a reasonable business deduction.

How does a payroll-deduction IRA work?

Susannah, age 25, works for Elite Tax Preparation Company which has offered its employees the opportunity to have deductions taken from their salaries to contribute to IRAs that the employees have set up for themselves. The employer makes the contributions by using electronic deposits. Susannah signs up for the program and has \$125 per paycheck deposited into her Roth IRA. There are 24 payrolls per year. Her contributions total \$3,000. Since the contribution limit for 2009 is \$5,000 she would be able to contribute an additional amount of \$2,000.

How does an employer end a payroll-deduction program?

It simply makes the decision to end the program. The employer will need to notify the employees of its discontinuance of the payroll deductions. If the employer uses a payroll service to assist with its payroll work, then the employer will want to notify this service provider also.

Is a payroll-deduction IRA program different from an Employer-Sponsored IRA plan?

Yes. The employer makes contributions with its funds under an employer-sponsored IRA plan, whereas the employer only transmits the employee's own funds under a payroll-deduction IRA program.

Summary.

You may wish to check with your business customers to see if they would want any assistance with operating a payroll-deduction IRA program. Although your best bet may be to offer assistance to employers without a 401(k) plan, there is nothing preventing a business with a 401(k) plan from also offering the payroll-deduction IRA program. Again, more people should be contributing to both 401(k) plans and making Roth IRA contributions. People should be making both types of contributions and not just the 401(k) contribution. A payroll-deduction IRA program should be a relatively simple way to increase the amount of contributions to Roth IRAs and traditional IRAs.

There are both traditional IRA payroll-deduction programs and also Roth IRA payroll-deduction programs.

Terminating a SEP, SARSEP or SIMPLE-IRA Plan

The IRS has issued a number of statements regarding terminating a SEP plan, SARSEP plan or a SIMPLE IRA plan. These statements are set forth below. You will note that the statements are not identical. An employer has a great deal of discretion as to when it can terminate a SEP or SARSEP plan and the employer is not required to (but should) inform its employees of the discontinuance of contributions. An employer has no discretion when it comes to terminating a SIMPLE IRA plan during the current year. An employer can only terminate its SIMPLE Plan on a prospective basis starting next year and the employer must inform its employees of the plan's termination for the upcoming year. The purpose of this article is to suggest that the IRS needs to furnish additional guidance on terminating any of the above plans and explain how the termination affects an individual's IRA or SIMPLE IRA. Current IRS guidance should be expanded. There are two steps to establishing a SEP plan, SARSEP plan or SIMPLE plan. First, the employer completes and signs a plan document form. In the case of a SEP, the employer generally completes and signs Form 5305-SEP. In the case of a SARSEP, the employer completes and signs Form 5305A-SEP. In the case of a SIMPLE IRA plan, the employer completes and signs either the Form 5304-SIMPLE (no designated financial institution) or Form 5305-SIMPLE (a designated financial institution). Secondly, each eligible employee (including the owner when it is a one person business) must have an IRA into which the employer contribution will be made. In the case of a SEP or a SARSEP, a standard traditional IRA (Form 5305 or Form 5305-A) is sufficient as it authorizes a SEP or SARSEP contribution in addition to standard, rollover, or recharacterized contributions. In the case of a SIMPLE IRA, the eligible employee must complete a SIMPLE IRA plan agreement (either Form 5305-S or Form 5305-SA) as the only type of contributions authorized are SIMPLE IRA annual contributions or rollover contributions from another SIMPLE. The IRS discusses what an employer (including a one person business) must do when the employer decides to terminate one of the above plans. See the

statements set forth on the next page. However, the IRS generally does not discuss what effect the employer's decision to terminate the "PLAN has on the individual's underlying traditional IRA or SIMPLE IRA. The IRS, in general, has given little guidance as to when a SEP IRA quits being a SEP IRA. This is important for knowing how to complete box 7 of the Form 5498 or to determine what rules apply if the IRA account holder would file for bankruptcy. The primary reason for this article is to emphasize a statement the IRS makes when an employer chooses to terminate its SARSEP plan. **"Upon termination, the account of each participant retains the characteristics of a traditional IRA and is subject to the rules and provisions of IRA accounts."** The IRS has apparently adopted the approach that if an employer terminates the SARSEP plan, then the funds within the individual's IRA can no longer be SARSEP funds. Such funds are now traditional IRA funds. It will be interesting to see if the IRS applies this same rule in the future to SEP funds and SIMPLE IRA funds. Right now, the IRS certainly does not say the same thing when an employer terminates a SIMPLE IRA plan. The IRS has not given guidance as to when a SIMPLE IRA quits being a SIMPLE IRA. This is important for knowing how to complete box 7 of the Form 5498. Most likely, the two year rule is probably the reason why the SIMPLE IRA does not automatically become a traditional IRA. It may well be that the only way a SIMPLE IRA quits being an SIMPLE IRA (no matter how many years have passed since the last SIMPLE IRA contribution) is if the funds are expressly withdrawn and rolled over into a traditional IRA or transferred from the SIMPLE IRA to a traditional IRA. The IRS also does not say the same thing when an employer terminates a SEP plan as it does when an employer terminates a SARSEP plan. One wonders why not. If an employer terminates its SEP plan, then the funds within the individual's IRA could no longer be SEP funds and would have to be traditional IRA funds. The IRS, in general, has given little guidance as to when a SEP IRA quits being a SEP IRA. This is important for knowing how to complete box 7 of the Form 5498. The IRS needs to give additional guidance for both the employer and the individual account holders with respect to SEP IRAs, SARSEP IRAs and SIMPLE IRAs. Set forth are the IRS statements about termination.

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**Understanding Form 1099-R,
Continued from page 5**

Terminating a SEP Plan

"Although SEPs are established with the intention of continuing indefinitely, the time may come when a SEP no longer suits the purposes of your business. When that happens, consult with your financial institution to determine if another type of retirement plan might be a better alternative. To terminate a SEP, notify the financial institution that you will not make a contribution for the next year and that you want to terminate the contract or agreement. Although not mandatory, it is a good idea to notify your employees that the plan will be discontinued. You do not need to give any notice to the IRS that the SEP has been terminated."

Terminating a SARSEP Plan

"If the time comes when a SARSEP no longer suits the purposes of your business, consult with your financial institution partner to determine if another type of retirement plan might better suit the needs of the business. To terminate a SARSEP, notify the financial institution handling the SEP-IRAs that contributions will no longer be made and that the contract or agreement is being terminated. Upon termination, the account of each participant retains the characteristics of a traditional IRA and is subject to the rules and provisions of IRA accounts. No notice to the IRS that the SARSEP has been terminated is required."

Terminating a SIMPLE IRA Plan

"If the time comes when a SIMPLE IRA no longer suits your needs, consult with your financial institution partner to determine if another type of retirement plan (or, perhaps, no plan at all) might be preferable. A SIMPLE IRA plan can only be terminated prospectively, beginning no earlier than the next calendar year. Contributions must continue until then. To terminate a SIMPLE IRA plan, notify the financial institution that you chose to handle the SIMPLE IRA plan that you will not be making contributions for the next calendar year and that you want to terminate the contract or agreement with it. You must also notify your employees that the SIMPLE IRA plan will be discontinued. You do not need to give any notice to the IRS that the SIMPLE IRA plan has been terminate." ♦

**2008 SEP Contributions for Farmers
and Other Employers**

Many farmers had very good income years for 2008. They may be looking for ways to lower their federal income tax liability. Establishing and funding a SEP IRA may well be the answer.

For 2008, the maximum SEP contribution is the lesser of 25% of compensation or \$46,000. If the farmer is in the 25% tax bracket, contributing \$46,000 will reduce his tax liability by \$11,500 since his deducting the \$46,000 SEP contribution means his taxable income will be \$46,000 less than it otherwise would have been. If your institution would find 20 new SEP customers contributing the maximum \$46,000, you would have \$920,000 of new deposits. These same individuals might make contributions for next year when the maximum contribution limit will be \$49,000.

A small business, including a one person business, establishes a SEP by doing three tasks. First the employer must execute a SEP plan document. This will either be the IRS Form 5305-SEP or a SEP prototype. Second, if applicable, the employer must furnish certain information about the SEP to each eligible employee. Thirdly, each eligible employee must establish a SEP-IRA to receive the employer's SEP contribution.

The business may set up a SEP for 2008 as late as March 15, 2009 (corporation with December tax year) or April 15, 2009 (self-employed with December tax year) as extended by any extension.

Employer contributions to a SEP-IRA will not disqualify a person from making a Roth IRA contribution or a traditional IRA contribution. Making a SEP-IRA contribution does make a person an active participant so their traditional IRA contribution might not be deductible.

Individuals establishing SEP-IRAs should consult with their tax advisor. They certainly should if they have any part-time or full time employees.

If it served an individual's tax purpose, an individual could establish a SEP for 2008 on April 15, 2009 and then set up a one person 401(k) plan for 2009 and subsequent years on the same day. ♦

Direct Rollovers from a Traditional IRA

It is still an infrequent event, but there are times when an individual elects to move funds from his or her traditional IRA or Roth IRA to a qualified plan, a governmental section 457 plan or a section 403(b) plan. To simplify things, the individual many times wants the IRA custodian to issue the check to the qualified plan rather than himself or herself. An IRA custodian is never required to send the funds directly to the employer plan. An IRA custodian may always inform the employer and the individual that they won't send the funds to the employer. Rather, the IRA custodian will make the distribution to the individual and he or she may roll it over, if desired. Many IRA custodians, however, choose to be nice and accommodate the individual. The purpose of this article is to discuss the reporting to be done by the IRA custodian.

Technically, this transaction is not a direct rollover since the law defines that transaction as being the movement of funds from a qualified plan, a governmental section 457 plan or a section 403(b) plan to an IRA. The reverse transaction is not defined as a direct rollover. However, as an administrative matter, the IRS has adopted the same reporting procedures for this transaction.

The IRA custodian is to report the total amount of the distribution in Box 1. The IRA custodian is to report zero (0) in box 2a when funds are sent to an employer plan or when funds are withdrawn from a conduit IRA and paid to the plan trustee. Reason code G is to be inserted in Box 7.

Funds within a traditional IRA may be rolled over into a qualified plan, a governmental section 457(b) plan or a section 403(b) plan. However, funds within an inherited traditional IRA are ineligible to be rolled over or directly rolled over into a qualified plan, a governmental section 457(b) plan or a section 403(b) plan.

No Direct Rollovers from a Roth IRA

Funds within a Roth IRA plan are ineligible to be rolled over into qualified plan, a governmental section 457(b) plan or a section 403(b) plan even if such a plan has designated Roth accounts. Funds within an inherited Roth IRA plan are also ineligible to be rolled over into qualified plan, a governmental section 457(b) plan or a section 403(b) plan even if such plan has designated Roth accounts.

We believe it is only a matter of time before the large financial institutions exercise their strong lobby to change the tax rules so that funds within a Roth IRA will be eligible to be directly rolled over into a designated Roth account within a qualified plan, governmental section 457(b) plan or section 403(b) plan. ♦

When Not to Change a Distribution Code on Form 1099-R and Why Not.

People make mistakes. Sometimes a financial institution will make mistakes. Sometimes it is your customer who make the mistakes. Sometimes the mistake is made by your customer's attorney, accountant or financial planner. There are right ways and wrong ways to correct mistakes. Some mistakes cannot be corrected.

This article illustrates a customer's mistake which the IRA custodian must not try to correct.

An IRA representative called CWF with the following situation. If possible, her management wanted her to change a distribution or transaction code as was being requested by a customer.

Background

A woman had maintained an IRA with another financial institution. In March of 2008 she withdrew the funds from that other institution and made a rollover contribution to the IRA she established with Institution #A. She invested her IRA rollover funds into a 6 month time deposit. Upon maturity in September of 2008 she withdrew the funds from Institution #A. She completed a distribution form. She did not complete any transfer form. Presumably, she contributed these funds to an IRA with another financial institution (Institution B).

Institution #A prepared a 2008 1099-R for her IRA distribution in September. She has recently come to the bank and requested that the bank change its records to show that the funds were transferred to another financial institution rather than being distributed to her. Presumably, her tax advisor has informed her of the once per year rollover rule. The distribution she took in September was ineligible to be rolled over into another IRA because she had already made a rollover contribution within the preceding 12 months. If she did attempt to rollover this amount to another IRA custodian, it would be an excess contribution regardless if Institution #A changed its records. However, if Institution #A changes its records, it won't look like an ineligible rollover to the IRS.

The reason why a financial institution acting as an IRA custodian does not want to change the distribution code in this situation is that it would be tax fraud. She received a distribution and she is ineligible to roll it over. She must include this amount in her income and pay tax on it. Her IRA funds were not transferred. They were distributed to her. It may well be that she did not know about the once per year rollover rule and that she has had to learn a tax lesson the hard way. But Institution #A does not want her problem to become its problem. That may well happen if Institution A decides to change its distribution code. The tax laws and the instructions for preparing the Form 1099-R require Institution #A to prepare a Form 1099-R reporting all IRA distributions (except those which are transfers).

What penalty(ies) might the IRS impose on Institution #A if it would change the distribution code? The worst case scenario is, Institution #A could lose its legal right to act as an IRA custodian. Most likely the IRS and Institution #A would negotiate a monetary settlement. The IRS may well lean towards imposing a sufficiently high penalty to make sure that Institution #A would not make the same decision a second time.