THE Pension Digest

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ALSO IN THIS ISSUE –

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"The Pension Specialists"

New 2018 IRA and Pension Tax Law Changes

On Friday, February 9, President Trump signed into law the Bipartisan Budget Act of 2018. Although the primary purpose of the budget law was to establish the federal budget, there were many tax law changes including some IRA and pension tax law changes.

First, the special disaster related tax rules will apply to the victims of the California wildfires. Distributions entitled to the special tax relief are those made on or after October 8, 2017, through December 31, 2018. That is, the 10% penalty tax does not apply and the two special 3 year rules apply. A distribution may be taxed over the three tax years and a person has three years on which to repay/rollover a distribution.

The second change is with respect to the rollover rules. At times, in order to collect tax funds owed by a taxpayer the IRS will levy an individual's pension funds and/or the individual's IRA funds, including inherited funds. That is, a distribution occurs because the IRS requires the pension trustee or the IRA custodian to issue a check to the U.S. Treasury. Sometimes the IRS must return such funds. The new law treats the IRS' repayment of these wrongful levies as being eligible to be rolled over either into the pension plan or an IRA. The IRS has the duty to inform the individual that he or she is eligible to make this special rollover. This change applies to IRS payments made after December 31, 2017.

An IRA owner who is considered to have received an IRA distribution because the IRS wrongfully levied his or her IRA is authorized to return the withdrawn amount to their IRA *(or inherited IRA)*. This special rollover must be made no later than the due date of the individual's tax return for the year the money is returned by the IRS, but not including an extension.

It appears a pension plan is not required to be written to accept such a rollover because such funds may be rolled over into an IRA. The amount eligible to be rolled over is the amount paid to the IRS which is repaid plus any interest paid by the IRS.

This special rollover contribution is not to be counted for purposes of the once per 12 month rollover rule.

This is the first law change expressly authorizing a rollover of inherited IRA funds.

Although this law change certainly benefits the affected taxpayers it does make the rollover rules more complex.

There are other legislative proposals in the U.S. Congress which would allow an IRA beneficiary to roll over inherited funds distributed on an account of the IRA custodian's mistake. Time will tell if there will be an additional law change with respect to inherited IRA and rollover rights.

We will be revising our IRA forms, as applicable, to discuss these new laws.

Preliminary Tax Data – IRA/Pension Statistics for 2016

Tax statistics may be boring, but they are important form many reasons. IRAs and 401(k) plans are tax preferred plans. Individuals receive tax benefits when they make contributions to such plans. The U.S. government is interested because the general tax rule is, when a person takes a distribution he or she must include that distribution in their income and pay the marginal tax rate applying to him or her.

$703 billion was withdrawn from 401(k) plans and other pension plans in 2016. $254 billion was withdrawn from traditional IRAs. One can assume taxes of 20% - 30% were paid on these distributions.

The statistics below make clear an IRA and Keogh custodian wants to understand who its high income clients are. $22.15 billion was contributed to SEP/SIMPLE/Keogh plans by self-employed individuals and 78% came from individuals with incomes of $100,000 or more. The average contribution was $23,800.

IRA contributions for 2016 totaled $13.62 billion with over 60% coming from individuals with modified adjusted gross incomes in the range of $50,000 - $200,000.

CHART A — SEP/SIMPLE/Profit Sharing Chart

Year	Contribution Amount	Number of Contributors	Average Contribution
2003	$16.9 billion	1.19 million	$14,202
2004	$18.0 billion	1.17 million	$15,385
2005	$19.4 billion	1.20 million	$16,202
2006	$20.2 billion	1.18 million	$17,200
2007	$20.1 billion	1.14 million	$17,720
2008	$18.5 billion	.97 million	$19,072
2009	$17.5 billion	.88 million	$19,780
2010	$17.2 billion	.87 million	$19,776
2011	$17.6 billion	.87 million	$20,256
2012	$19.2 billion	.88 million	$21,843
2013	$20.2 billion	.90 million	$22,364
2014	$20.8 billion	.93 million	$22,438
2015	$22.2 billion	.95 million	$23,234
2016	$22.15 billion	.93 million	$22,798

CHART B — Traditional IRA Chart

Year	Contribution Amount	Number of Contributors	Average Contribution
2003	$10.16 billion	3.46 million	$2,936
2004	$10.20 billion	3.38 million	$3,018
2005	$12.21 billion	3.29 million	$3,707
2006	$12.77 billion	3.29 million	$3,885
2007	$13.19 billion	3.37 million	$3,914
2008	$11.91 billion	2.78 million	$4,284
2009	$11.49 billion	2.64 million	$4,358
2010	$11.71 billion	2.63 million	$4,449
2011	$11.26 billion	2.62 million	$4,302
2012	$12.05 billion	2.61 million	$4,608
2013	$13.30 billion	2.77 million	$4,797
2014	$13.44 billion	2.75 million	$4,896
2015	$13.25 billion	2.67 million	$4,960
2016	$13.62 billion	2.69 million	$5,056

Deductible Traditional IRA Contributions

The number of tax returns claiming a deduction for a traditional IRA contribution increased slightly.

The amount contributed to traditional IRAs increased to 13.62 billion from 13.25 billion. This was a 2.8% increase.

What was the AGI of those who made traditional IRA contributions for 2016?

	Under $15,000	$15,001 to $29,999	$30,000 to $49,999	$50,000 to $99,999	$100,000 to $199,999	$200,000 Or more	Total
Number of Returns	100,899	288,574	528,258	992,899	713,948	162,966	2,694,545
% of Total Returns	3.74%	10.60%	19.60%	33.51%	26.50%	6.05%	100%
Contribution Amt. **(in thousands)**	$341,733	$1,094,648	$2,056,350	$4,416,292	$4,111,318	$1,602,101	$13,622,442
% of Total Contr.	2.50%	8.04%	15.10%	32.42%	30.18%	11.76%	100%
Avg. Contr. Amt.	$3,387	$3,833	$3,893	$4,891	$5,759	$9,931	$5,056

CWF Observations

1. The average IRA contribution, per return, was $5,056 for 2016.
2. 32.42% of all IRA contributions came from individuals with AGI between $50,000-$99,999.
3. 74.36% of all IRA contributions for 2016 came from individuals with AGI of $50,000 or More.

IRA and SEP/SIMPLE/Keogh Deductible Contributions

1. The number of tax returns claiming a deduction for a self-employed person's contributions to a profit sharing, SEP or SIMPLE decreased to .93 million from .95 million.
2. The amount contributed by self-employed individuals to a profit sharing plan, SEP or SIMPLE stayed unchanged at 22.2 billion.

What was the adjusted gross income (AGI) of those who made SEP/SIMPLE/Keogh contributions?

	Under $15,000	$15,001 to $29,999	$30,000 to $49,999	$50,000 to $99,999	$100,000 to $199,999	$200,000 Or more	Total
Number of Returns	10,852	10,503	52,588	133,157	268,904	454,688	930,694
% of Total Returns	1.17%	1.13%	5.65%	14.31%	28.89%	48.85%	100%
Contribution Amt. **(in thousands)**	$70,939	$113,722	$470,667	$1,505,934	$4,588,949	$15,398,714	$22,148,925
% of Total Contr.	.32%	.51%	2.13%	6.80%	20.72%	69.52%	100%
Avg. Contr. Amt.	$6,537	$10,828	$8,950	$71,309	$17,065	$33,867	$23,798

CWF Observations on SEP/SIMPLE/Keogh Contributions for 2016

1. The average contribution per return is $23,794 for 2016.
2. 69.52% of contributions ($15.4 billion) come from individuals with AGI of $200,000 or more.
3. 90.24% of contributions (18.7 billion) come from individuals with AGI of more than $100,000.
4. The average contribution is $33,867 for those with MAGI of $200,000 or more.

Taxable IRA Distributions for 2016

(Based on AGI)

	Under $15,000	$15,001 to $29,999	$30,000 to $49,999	$50,000 to $99,999	$100,000 to $199,999	$200,000 Or more	Total
Number of Returns	1,838,988	1,891,792	2,043,337	4,320,366	3,112,298	1,193,020	14,399,801
% of Total Returns	12.77%	13.14%	14.19%	30.00%	21.61%	8.29%	100%
Distribution Amt. **(in thousands)**	$10,312,662	$15,538,803	$20,835,151	$67,132,944	$83,573,103	$57,070,531	$254,463,193
% of Total Distrib.	4.05%	6.11%	8.19%	26.38%	32.84%	22.43%	100%
Avg. Distrib. Amt.	$5,608	$8,214	$10,196	$15,539	$26,583	$47,837	$17,671

CWF Observations

1. 14.40 million returns reported a taxable IRA distribution.
2. There were taxable IRA distributions of 254.4 billion.
3. The average distribution was $17,671.
4. As one would expect, the average distribution was larger for those with higher incomes.

Pension Distributions for 2016
(Based on AGI)

	Under $15,000	$15,001 to $29,999	$30,000 to $49,999	$50,000 to $99,999	$100,000 to $199,999	$200,000 Or more	Total
Number of Returns	3,774,496	4,336,546	4,513,065	8,519,129	5,333,015	1,578,366	28,054,617
% of Total Returns	13.45%	15.46%	16.09%	30.37%	19.00%	5.63%	100%
Distribution Amt. **(in thousands)**	$26,454,323	$54,111,177	$82,422,730	$231,496,474	$218,256,469	$90,809,524	$703,550,696
% of Total Distrib.	3.756	7.69%	11.72%	32.90%	31.02%	12.91%	100%
Avg. Distrib. Amt.	$7,109	$12,478	$18,263	$27,174	$40,926	$57,534	$25,078

Observations

1. 28.05 million returns reported a taxable pension distribution.
2. There were taxable pension distributions of 703.6 billion.
3. The average distribution was $25,078.
4. As one would expect, the average distribution was larger for those with higher incomes.
5. 76.83% of the taxable distributions ($540 billion) arose from those returns showing AGI of $50,000 or more.

The IRS has recently issued the above discussed preliminary tax data for tax year 2016. These statistics are preliminary statistics in the sense they were devised by an IRS economist using a sample of tax returns to make estimates. The number of filed returns decreased from 150.7 million to 150.3 million. Taxable income increased to $7.3 trillion from $6.9 trillion. An increase of 8%.

We at CWF strongly believe individuals with higher incomes should be making more non-deductible contributions so one day they may convert them into their Roth IRA. More people are going to want to maximize their Roth IRA contributions.

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Email Consulting Guidance

An Inherited Roth IRA is a Highly Valued Gift

Q. My wife (BD 06-04-56) inherited a Roth IRA from her late aunt who passed away this year and was 89 years old. The IRA has a value of roughly 73K.

Will accumulations in the account continue to be tax deferred and will any RMD's from the Roth be untaxed as it would have been for the primary account holder?

I have never dealt with a beneficiary Roth account and thanks for your insight.

A. Your wife has received a very valuable gift. Her inherited Roth IRA may earn tax free income for the next 22.7 years. As you know, there is not much income which is not taxed under our federal income tax laws. She wants to take advantage of the very favorable tax treatment. She wants to instruct the IRA custodian/ trustee that she will be using the life distribution rule to take distributions from the inherited Roth IRA.

Critical point, your wife as a non-spouse beneficiary can transfer an inherited Roth IRA, but a distribution made to her can't be rolled over into another Roth IRA (whether hers or another inherited Roth IRA).

Under existing law, an inherited Roth IRA produces tax-free income for a non-spouse beneficiary as long as the 5 year rule has been met. I assume it has been met.

As a non-spouse beneficiary, she will be required to take a required distribution from the inherited Roth IRA each year commencing with the year after the year the late aunt died. Presumably, most non-spouse beneficiaries will decide they will only withdraw the RMD each year. This will allow maximizing the amount of tax free income to be earned.

Estimate of her first RMD, $73,000/22.7 = $3,215.86. No tax is owed with respect to withdrawing the RMD of $3,215.86 or any subsequent distribution.

If the late aunt died in 2018, then your wife must take her first RMD in 2019. The 22.7 payout period comes from the Single Life table as your wife will be 63 in 2019. In 2020 the divisor would be 21.7. in 2021 20.7, etc. The balance used in the RMD calculation would be the balance as of 12/31/18 rather than the $73,000.

If the late aunt died in 2017, then your wife must take her first RMD for 2018 by 12/31/18. The divisor of 23.5 comes from the Single Life table as your wife would be 62 in 2018.

I suggest she complete a beneficiary designation form to designate her beneficiary(ies) should she die. I suggest doing this relatively soon. After her passing, if she has not withdrawn all of the funds in the inherited Roth IRA, the same RMD distribution schedule applying to her will continue to apply to her beneficiary(ies).

If her inherited Roth IRA could realize earnings greater than 5%, then the inherited Roth IRA's balance would grow for a number of years before starting to decline.

Correcting an Excess HSA Contribution

Q. I got an HSA scenario that I could use your help on. We have a client that has an HSA with us.

It is a family plan and in 2017 she contributed $6,750.00. However, with the combination of her husband's HSA (which is not at OFB) the have an excess of $1,100.00. In 2018 for 2018 the have contributed 2,000.00. The balance as of 12-31-17 was $1,045.27 and the current balance as of today is $1,891.92. So my question is since the balance at the end of 2017 was $1,045.27 and they want to correct a $1,100.00 excess for 2017 is that possible to do since they didn't have $1,100.00 at the end of the 2017 in the account. I know I threw a lot of figures at you so sorry for any confusion. Thank you for your help.

A. Good morning. The IRS has issued very limited guidance on the subject of correcting HSA excess contributions and the IRS reporting for such corrections. The IRS has stated the taxpayer(s) is primarily responsible to·correct an excess contribution situation and to prepare her/their tax forms showing the correction.

I suggest for consideration the following approach. She withdraws the $1,100 (plus any earned income, if any) from her HSA and informs OFB that she is withdrawing an excess for 2017. OFB will report this distribution on her 2018 Form 1099-SA and the reason code in box 3 will be a 2 (excess contribution).

She will need to complete a Form 8889 for 2017 and 2018 and she should explain making the excess in/for 2017 and correcting it in 2018. I don't think the balance

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being only $1,045.27 as of 12/31/17 means this approach cannot be used.

If Two IRA Distributions – Only One May be Rolled Over, Other is Taxable

Q. We are a client of yours and I was wondering if you could clarify a rollover for me. Here is the scenario:

I have a customer that has taken a distribution from us and a distribution from another bank on the same day. On that same day, she deposited those funds as a Rollover into an IRA at another institution. Is this considered one Rollover in the 12 month period, or two?

I believe it would be considered two based on the funds are coming from two different places, but I may be mistaken. If it is considered two, what are the customers options?

Thank you for your time and I look forward to your response.

A. Hi. I don't have any good news. Tax rules are often punitive and this is such a case.

The individual clearly has had two IRA withdrawals. There is no way to argue there was only one distribution.

She as any other taxpayer is only allowed to rollover one distribution during a 12 month period. Presumably, she will decide to rollover the largest distribution. She will be required to include the other distribution in her income and pay tax on that amount.

One learns that in real life certain court cases lead to horrible court decisions. Prior to 2014, the IRS for over 40 years had applied the once per year IRA rollover rule on a per IRA plan agreement basis. The IRS was being taxpayer friendly. In 2014 a married couple was in U.S. Tax Court. He was a tax attorney and possibly she was also. Based on IRS guidance in Publication 590 and a temporary IRS regulation, each had taken two distributions from two different IRAs and then had rolled over these distributions so they weren't taxable.

It appears the tax court judge wanted to rule against this tax attorney. The tax court judge who was quite new to the U.S. Tax Court read the statutory law as not supporting the IRS' position. The judge ruled a person is only able to rollover one distribution during a 12 month period and so the married couple owed a substantial amount in additional taxes.

The IRS has stated it has no authority to grant relief to a person who does not comply with the once per year rule.

Individuals are supposed to know this rule and to know that if they are to avoid this unhappy result they will need to have the IRA funds transferred rather than taking a distribution and then making a rollover contribution.

Note: The fact that because she rollover over both distributions that one of them will be an excess IRA contribution sub subject to the 6% tax unless withdrawn. I would think she will want to correct this excess contribution as she will only compound her tax difficulties should she choose to leave the non-qualifying rollover in the IRA.

If she would choose not to correct it, and the IRS would determine that she had made an excess contribution, she could end up having to include the distribution amount in her income TGWICE. She must include it in her 2018 income and she would have to include the income again when she withdraws it.

Are IRA Transfers Via an ACH Transaction a Prohibited Transaction?

Q. Per our conversation about wires and IRA transfers, I am emailing you to see if there's literature explaining the reason wiring funds for an IRA transfer/rollover is prohibited.

A. Code section 4975 is the source of the PT rules. Code section 4975(c)(1) defines what acts are prohibited transactions. Note a "Transfer to" of IRA or pension funds to a disqualified person is all that is required to have a PT. There is no requirement that the disqualified person must use the funds to benefit itself. The bank as the IRA custodian/trustee is a disqualified person.

You asked, is it best to have a direct rollover check or a direct transfer check sent/mailed to the bank rather than having the payment be made via a wire transfer?

The answer is "yes." These funds must be processed by the bank in its status as being the IRA custodian/trustee and not in its performance of other general banking duties.

Might it be possible the bank could establish a special account/procedures for wire transfers and ACH pay-

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ments associated with IRA and pension distributions? The funds would go into a special segregated account. If so, I believe the bank as the IRA custodian could then accept such payments. I would want/suggest the bank to do further research.

The general tax rule is, if a PT occurs with respect to an IRA, the IRA is deemed distributed as of January 1st of the year the PT occurs. The tax consequences can be horrific for an IRA owner who causes or participates in a PT. I believe the IRS and DOL have adopted the administrative approach (and it might be statutorily based also) that an IRA trustee/custodian who participates in a PT is subject to a 15% excise tax based on the transaction amount rather than requiring there be a deemed/actual distribution to the IRA owner.

It might be time for the banking industry (banking associations) to revisit this issue and see if the DOL would be willing to grant a class exemption so that wire transfer payments and ACH payments could be used as a payment method as long as whatever requirements the DOL would define would be satisfied. It is in the best interest of individuals that the funds are reinvested as soon as possible.

The IRS does not communicate the following very well, but the IRS does communicate it on Form 5330. A party (other the IRA owner) which causes/participates in a PT has a duty to prepare and file Form 5330 and pay the tax amount owing. Penalties and interest owing rules will apply if the form is not prepared and filed when it should have been

Excess SEP-IRA Contributions

Q. A customer contributed $21,835 to his SEP on 2/5/18. He called today that he put in "too much" and needs to withdraw $5,781. Please provide guidance as to what CWF form # to use. I'm not finding any SEP forms available for this type of transaction.

A. IRS guidance on the subject of excess SEP-IRA contributions is not what it should be. Here is my discussion.

1. There is a special tax rule which provides if a person has made an excess SEP-IRA contribution (i.e. made a contribution which exceeded his maximum permissible amount or exceeded 25% of his compensation), then such amount is treated as a regular annual traditional IRA contribution.

2. There is tax rule allowing a person who has made a current year traditional IRA contribution to withdraw it as an excess even though it is not an excess contribution.

3. That type of rule for withdrawing a non-excess contribution does not exist for SEP-IRAs. But, I'm assuming the $5,781 is an excess contribution and not just the amount he settled on contributing to this SEP-IRA.

Does your software allow you to have a contribution into the SEP-IRA of $15,964 and into the traditional IRA of $5,781 rather than a contribution into the SEP-IRA of $21,835?

I don't believe the IRS wants the $21,835 reported as the SEP-IRA contribution in box 8 of Form 5498 if the $5,781 was an excess.

If so, then CWF Form 57, 67 and 67W (???) should be completed to show the withdrawal of the $5781 plus the related interest as the withdrawal of an excess contribution.

Remember the SEP-IRA contribution of $15,964 (even though for tax year 2017 is reported on his 2018 Form 5498) is to be reported on the Form 5498 for the year the bank receives the SEP-IRA contribution.

With respect to his withdrawal of the current year contribution as made in 2018 for tax year 2017 as withdrawn in 2018, the bank will report such on the 2018 Form 1099-R. The interest income, if any is to be reported on his 2018 tax return. The reason code would be an "8."

Moving an Inherited IRA

Q. If a beneficiary inherited an IRA and has been receiving the RMD, is it possible for the beneficiary to stop receiving the RMD and transfer the IRA funds from the inherited IRA into their own IRA and start making contributions to that new IRA?

A. I may need to be provided more specifics.

The IRA beneficiary rules can be complex because they depend on the type of IRA, whether the beneficiary is a spouse beneficiary or a non-spouse beneficiary and whether the IRA owner died before or after his/her required beginning date.

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The general tax rules are - a non-spouse beneficiary is required to pay tax on the amount distributed from an inherited IRA and the beneficiary must take a certain minimum amount each year starting with the year after the year the IRA owner died.

A non-spouse beneficiary does not have the right to treat the decedent's IRA as their own thereby eliminating the duty to take a required distribution. A non-spouse beneficiary does not have the right to combine personal IRAs with inherited IRAs. They must be kept separate.

A beneficiary can take a total distribution, pay the applicable tax liability and then use the net proceeds any way he or she wishes, even making an annual contribution to his/her own IRA. This assumes the beneficiary is eligible to make an annual contribution.

Minors and Roth IRAs

Q. Minor with income has Roth IRA. The Investment is stock. The Stock would have a custodian. Is this type of investment allowed being as the account owner is a minor and has a custodian? It's a Uniform Gift to Minor with Custodian, to hold the stock.

A. A minor is eligible to establish and maintain a Roth IRA as long as he/she meets the two eligibility requirements - must have compensated and his/her MAGI must satisfy the MAGI limits.

Presumably, a bank has minimal concern if a minor wishes to exercise his or her right to void an IRA agreement if the minor's Roth IRA contributions are invested in a time deposit or savings account. The bank is willing to return the amount contributed.

It is the investment in the stock which complicates things. Since the stock could lose value, the bank wants special documentation prepared to make clear that the minor's custodian and the minor acknowledge that they will not seek any type of damages from the bank for any reason (including being a minor) should the stock lose value. If the custodian is acting on behalf of the child and approves the investment, then the bank should have no liability.

The bank's attorney should assist with this. Or, an attorney for the minor/custodian should furnish a document and the bank's attorney should review it.

Inherited IRA - A State Court Orders the IRA Funds Are to Go to a Specific Person

Q. The bank has an IRA customer who had not reached RMD age, and is deceased, the sole beneficiary is also deceased. The bank has received a court order to distribute the IRA to her sole heir, who is age 66. She had been deceased for 2 years. Would it be better to use the five year rule, and distribute it to the next three years since she has been deceased for two years. If we use the life expectancy table for the beneficiary, would we need to catch up on distributions for the last two years?

A. The 5 year rule is required to be used when the IRA owner has designated a non-person (i.e. her estate) to be her IRA beneficiary. This is an IRS/IRC rule. The fact a state court judge has now ruled that a 66 year old person is to receive these IRA funds does not mean the life distribution rule is a distribution option for this person.

You should set up an inherited IRA with the titling - name of the court appointed beneficiary as beneficiary of the decedent's name IRA. That is, you can replace her estate as being the IRA beneficiary.

Under the 5 year rule, the IRA must be closed by December 31st of the year containing the 5th anniversary of the IRA owner's death.

The general rule is - a living non-spouse beneficiary of an IRA owner who has died before her required beginning date will use the life distribution rule unless such beneficiary elects to use the 5 year rule. He can take as many or as few distributions as he wants over the next 3 years as long as the IRA is closed in that 3rd year.

In your situation (the estate is the default IRA beneficiary), it is mandatory that the 5 year is used. The law does not permit the use of the life distribution rule as there was no living person who was the IRA beneficiary as of the time the IRA died owner.