



# THE Pension Digest

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## Understanding the 10-Year Rule Which Will Apply to Most IRA Beneficiaries of an IRA Owner Who Dies in 2020

The SECURE Act states that 10 years is to be substituted for 5 years when the beneficiary is an individual who is not an EDB and the IRA owner dies in 2020. Children and grandchildren will not be an EDB. If a person dies in 2020 and the 10-year rule applies, the RMD deadline is 12/31/30 and not 12/31/29.

The IRA beneficiary must take sufficient distributions to close the inherited IRA by December 31 of the 10th year containing the anniversary of the accountholder's death. There is no requirement to take out any specific amount in any year. The distributions may be periodic or non-periodic. In actuality, the beneficiary is allowed eleven calendar years to take his or her RMDs.

	Year	Sched #1	Sched #2	Sched #3	Sched #4	Sched #5
Year of Death Subsequent Years	2020	0%	0%	10%	20%	100%
1	2021	10%	0%	10%	20%	N/A
2	2022	10%	0%	0%	20%	N/A
3	2023	10%	0%	30%	20%	N/A
4	2024	10%	0%	0%	20%	N/A
5	2025	10%	0%	15%	N/A	N/A
6	2026	10%	0%	5%	N/A	N/A
7	2027	10%	0%	15%	N/A	N/A
8	2028	10%	0%	15%	N/A	N/A
9	2029	10%	0%	N/A	N/A	N/A
10	2030	10%	100%	N/A	N/A	N/A
Total		100%	100%	100%	100%	100%

The inherited IRAs must have a zero balance by 12/31/30 if the accountholder dies in 2020.

The 10-year rule applies to a designated beneficiary who must be an individual and who is not an EDB. The 5-year rule continues to apply if the beneficiary is a charity, an estate or a non-qualified trust.

## Observations .

1. The beneficiary may take periodic distributions or non-periodic distributions.
2. If the decedent's IRA was a traditional, SEP, or SIMPLE IRA the beneficiary generally will have to include the distribution in their income for the year of withdrawal and pay the associated tax. Therefore, a beneficiary may well want to establish a periodic distribution schedule.
3. If the decedent's IRA was a Roth IRA the beneficiary generally will not want to take a periodic distribution. In order to maximize the amount of tax free income to be earned during the 10-year period, the beneficiary may elect to take only one distribution in the last year. That is, 2030.
4. Note the 10-year distribution schedule is much shorter than if the beneficiary would have been able to use the life distribution rule.

5. A non-EDB wants to designate their own beneficiary(ies) should they die during the 10-year period. This successor beneficiary would continue the same 10-year period.
5. See Form 206 for a traditional, SEP or SIMPLE IRA.
6. See Form 206R for a Roth IRA.

### Beneficiary's Distribution Notice and Certification Form and Payment Instruction The Beneficiary is not an EDB or is Subject to the 10-Year Rule

<b>Beneficiary Information</b> Name _____ Address _____ City _____ State _____ Zip _____ Date of Birth _____ Phone: _____ SSN _____ Plan No. _____	<b>Purpose of Form</b> An IRA beneficiary who acquires an ownership share in an account holder's IRA upon the death of the IRA account holder (i.e. inherits) is required by law to commence withdrawing such IRA funds within certain time deadlines. I am to use this form to instruct the Custodian/Trustee how and when to make distributions to me to comply with the rules. Rules for the year of death. If the IRA account holder died before his or her required beginning date, there is no RMD which must be distributed for such year. If the IRA account holder died after his or her required beginning date, the RMD as determined for the IRA account holder must be distributed for such year unless the special rule applies for when a surviving spouse is the sole beneficiary. To the extent this amount was not paid out to the IRA account holder before his or her death, the beneficiary(ies) will need to be paid their proportionate share of the RMD by December 31, or the 50% tax will apply.
<b>Deceased IRA Accountholder Information</b> Name _____ SSN _____ Date of birth of IRA accountholder _____ Date of death of IRA accountholder _____ Required beginning date of IRA accountholder _____	<b>Custodian/Trustee Information</b> Name _____ City _____ State _____ Zip _____
<b>Beneficiary's Instruction/Acknowledgment</b> I hereby instruct you that I am not an EDB (eligible designated beneficiary) for purposes of the beneficiary RMD rules. In order to be an EDB, I must be disabled, chronically ill, a minor or I am not more than 10 years younger than the deceased IRA owner. I have consulted with my adviser (attorney, accountant or financial planner) or I have determined that such consultation is not needed. I understand that the tax rules require me to close the inherited IRA by December 31 of the year containing the 10th anniversary of the IRA account holder's death. If I fail to do so the 50% excise tax as authorized by IRC section 4974(a) may be assessed. Under the 10-year rule I may establish a periodic distribution schedule so that I may take periodic distributions over the 10/11 year time period, but I am not required to establish such a schedule. I may take nonperiodic distributions.	
<input type="checkbox"/> By checking here I am informing you I want to close this inherited IRA. The balance to be paid to me is \$_____. If I am a nonspouse beneficiary, I understand any distribution to me is ineligible to be rolled over. The general tax rule is, I will be required to include the distribution amount in my income unless there is some basis. <input type="checkbox"/> By checking here I am informing you (the IRA custodian) that I plan to take nonperiodic distributions from this inherited IRA. I will contact you to take these nonperiodic distributions. I have not scheduled to take any periodic distributions. I will need to complete an IRA distribution form for each nonperiodic distribution. <input type="checkbox"/> By checking here I am informing you (the IRA custodian) that I plan to take periodic distributions from this inherited IRA as instructed below. I reserve the right to modify this schedule including terminating it. <input type="radio"/> A. Pay me the amount of \$_____ per _____ until the IRA's balance is \$0.00. This distribution is to commence on _____. <input type="radio"/> B. Pay me the amount of \$_____ once per calendar year. This distribution is to commence on _____. <input type="radio"/> C. Other/Define _____ This distribution is to commence on _____.	
<b>I instruct you to make payments to:</b> <input type="checkbox"/> Me directly by mail to: <input type="checkbox"/> the address given above; or <input type="checkbox"/> My regular savings account or share account # _____ <input type="checkbox"/> My checking account # _____ <input type="checkbox"/> Other/Special Instruction _____	
<b>Beneficiary's Certification</b> I certify that I am a designated beneficiary of the referenced deceased IRA account holder and that I am not an EDB. I understand I have inherited _____% of the referenced IRA. I have furnished you with a certified copy of the death certificate or other documentation verifying that the account holder has died. I have instructed you above as to how to distribute my share of this IRA (I certify that my tax identification number (social security number) and other information are correct). When signing the withholding certification, I signify that I understand that the initial distribution is subject to federal income tax withholding unless I elect to not have it apply. I also understand that my initial withholding instruction will stay in effect until I change it, and that this distribution may have income tax consequences; therefore, I should consult a tax advisor as necessary. If I do not have sufficient income tax withheld, then I realize that I may have to pay additional tax penalties under the withholding and estimated tax payment rules. I am aware that if I am a nonspouse beneficiary I am not eligible to roll over any portion of a distribution from this inherited IRA to any other IRA, including another inherited IRA. I would be able to transfer an inherited IRA if both IRA custodians/trustees complete an inherited IRA transfer form agreeing to the transfer. I acknowledge that I should complete CWF's Form 61-L, or a similar form, to designate the beneficiaries that will inherit these funds in the event of my death. If I die during this 10-year period, my beneficiary must close my inherited IRA by continuing the 10-year period applying to me.	
<b>Withholding Certificate for IRA Pension or Annuity Payments</b> OMB NO. 1545-0074 Department of the Treasury (IRS) The instructions to this substitute Form W-4P are on the reverse side, as well as additional discussion of special withdrawal topics. Select #1, #2, or #3. 1. <input type="checkbox"/> I elect not to have income tax withheld from this IRA distribution. 2. <input type="checkbox"/> I elect to have income tax withheld from this IRA distribution equal to 10% of the amount withdrawn. 3. <input type="checkbox"/> I want the following additional amount withheld from each IRA payment. \$_____	
Signature of IRA Beneficiary _____ Date _____ Custodian/Trustee (Payer) _____ Date _____ IRA #206 (2/20)* White — Custodian/Trustee Yellow — Accountholder Pink — Administrator © 2020 Colin W. Fritz & Associates, Ltd.	

### Beneficiary's Distribution Notice and Certification Form and Payment Instruction The Roth IRA Beneficiary is not an EDB or is Subject to the 10-Year Rule

<b>Beneficiary Information</b> Name _____ Address _____ City _____ State _____ Zip _____ Date of Birth _____ Phone: _____ SSN _____ Plan No. _____	<b>Purpose of Form</b> A Roth IRA beneficiary who acquires an ownership share in an account holder's Roth IRA upon the death of the Roth IRA account holder (i.e. inherits) is required by law to commence withdrawing such Roth IRA funds within certain time deadlines. I am to use this form to instruct the Custodian/Trustee how and when to make distributions to me to comply with the rules. Rules for the year of death. If the Roth IRA account holder died before his or her required beginning date, there is no RMD which must be distributed for such year. If the Roth IRA account holder died after his or her required beginning date, the RMD as determined for the Roth IRA account holder must be distributed for such year unless the special rule applies for when a surviving spouse is the sole beneficiary. To the extent this amount was not paid out to the Roth IRA account holder before his or her death, the beneficiary(ies) will need to be paid their proportionate share of the RMD by December 31, or the 50% tax will apply.
<b>Deceased Roth IRA Accountholder Information</b> Name _____ SSN _____ Date of birth of Roth IRA accountholder _____ Date of death of Roth IRA accountholder _____ Required beginning date of Roth IRA accountholder _____	<b>Custodian/Trustee Information</b> Name _____ City _____ State _____ Zip _____
<b>Beneficiary's Instruction/Acknowledgment</b> I hereby instruct you that I am not an EDB (eligible designated beneficiary) for purposes of the beneficiary RMD rules or I am a Roth IRA beneficiary subject to the 10-year rule. In order to be an EDB, I must be disabled, chronically ill, a minor or I am not more than 10 years younger than the deceased Roth IRA owner. I have consulted with my adviser (attorney, accountant or financial planner) or I have determined that such consultation is not needed. I understand that the tax rules require me to close the inherited Roth IRA by December 31 of the year containing the 10th anniversary of the Roth IRA account holder's death. If I fail to do so the 50% excise tax as authorized by IRC section 4974(a) may be assessed. Under the 10-year rule I may establish a periodic distribution schedule so that I may take periodic distributions over the 10/11 year time period, but I am not required to establish such a schedule. I may take nonperiodic distributions.	
<input type="checkbox"/> By checking here I am informing you I want to close this inherited Roth IRA. The balance to be paid to me is \$_____. If I am a nonspouse beneficiary, I understand any distribution to me is ineligible to be rolled over. The general tax rule is, I will not be required to include the distribution amount in my income as long as the 5-year rule has been met. <input type="checkbox"/> By checking here I am informing you (the Roth IRA custodian) that I plan to take nonperiodic distributions from this inherited Roth IRA. I will contact you to take these nonperiodic distributions. I have not scheduled to take any periodic distributions. I will need to complete an Roth IRA distribution form for each nonperiodic distribution. <input type="checkbox"/> By checking here I am informing you (the Roth IRA custodian) that I plan to take periodic distributions from this inherited Roth IRA as instructed below. I reserve the right to modify this schedule including terminating it. <input type="radio"/> A. Pay me the amount of \$_____ per _____ until the Roth IRA's balance is \$0.00. This distribution is to commence on _____. <input type="radio"/> B. Pay me the amount of \$_____ once per calendar year. This distribution is to commence on _____. <input type="radio"/> C. Other/Define _____ This distribution is to commence on _____.	
<b>I instruct you to make payments to:</b> <input type="checkbox"/> Me directly by mail to: <input type="checkbox"/> the address given above; or <input type="checkbox"/> My regular savings account or share account # _____ <input type="checkbox"/> My checking account # _____ <input type="checkbox"/> Other/Special Instruction _____	
<b>Beneficiary's Certification</b> I certify that I am a designated beneficiary of the referenced deceased account holder's Roth IRA. I understand I have inherited _____% of the referenced Roth IRA. I have furnished you with a certified copy of the death certificate or other documentation verifying that the account holder has died. I have instructed you above as to how to distribute my share of this Roth IRA. I will also complete Form 57-R2, Distribution to a Roth IRA Beneficiary so that IRS Form 1099-R (IRA Distributions) will be prepared. I understand that this distribution has income tax consequences; therefore, I should consult a tax advisor. A beneficiary is able to be paid an amount larger than his or her Required Minimum amount, including closing the account by taking a lump-sum distribution. However, by doing so the special tax benefits associated with the Roth IRA (right to earn tax-free income) will be ended. I am aware that if I am a nonspouse beneficiary, then I am ineligible to roll over any portion of a distribution from an inherited Roth IRA to my own Roth IRA or another inherited Roth IRA unless the IRS levy exception applies. I would be able to transfer an inherited IRA if both IRA custodians/trustees complete an inherited IRA transfer form agreeing to the transfer. If I am a spouse beneficiary, I certify to you that I understand I am eligible to roll over funds from a deceased spouse's IRA to my IRA only if I comply with the 60-day rule and the one year rule. I understand that I am not eligible to roll over any required distribution for the current year or prior year to the extent it has not been distributed. I acknowledge that I should complete CWF's Form 61-L, or a similar form, to designate the beneficiaries that will inherit these funds in the event of my death. Upon my death, the 10-year rule will apply to my beneficiary.	
Signature of IRA Beneficiary _____ Date _____ Custodian/Trustee (Payer) _____ Date _____ IRA #206-R (2/20)* White — Custodian/Trustee Yellow — Accountholder Pink — Administrator © 2020 Colin W. Fritz & Associates, Ltd.	

## Rolling Over an RMD Which is No Longer an RMD

An IRA to IRA rollover is really two transactions. First there is a withdrawal from an IRA followed by a rollover contribution into an IRA.

The CARES Act was enacted on March 27, 2020. The CARES Act waived all RMDs for 2020.

In late December of 2008 a law (Worker, Retiree, and Employer Recovery Act of 2008) was enacted waiving RMDs for 2009. Many IRA accountholders received 2009 IRA distributions and did not understand they could roll them over because these distributions were not RMDs. Therefore, the IRS granted the following relief in Notice 2009-82: if a person was paid his or her RMD during the period of January 1 to October 1, 2009, then he or she has until November 30, 2009, to roll over all or some portion of the distribution. We expect the IRS will be issuing similar relief in 2020.

However, most IRA accountholders who have already received their 2020 RMD distribution can immediately rollover their distribution. They don't need to wait or hope for the IRS to grant additional relief.

That is not the case for those IRA accountholders who attained age 70 and 70½ in 2019 or age 70½ and 71 in 2019 and who now because of the CARES Act have no RMD for 2019. Many were distributed their 2019 RMD in 2019. They are ineligible to rollover such distributions. However, if a person was not paid the 2019 RMD in 2019, then the person is eligible to rollover any distribution occurring in 2020.

A cardinal rollover law is, a person is ineligible to rollover an RMD. Attached at the end of this memorandum is a sheet summarizing the 5 basic rules of rolling over an IRA distribution.

There are IRA accountholders who were paid their 2020 RMD prior to March 27, 2020, who are now asking, "am I able to rollover the RMD distribution which was made to me because it no longer is an RMD?"

Our answer is yes as long as the basic IRA rollover rules are met or in some cases if the special rules for late rollovers are met or the special rules for rolling over a disaster distribution are met.

The IRS has instructed that there are three different

ways to report a rollover on Form 5498:

1. A standard rollover is reported in box 2;
2. A certified late rollover is reported in boxes 13a and 13c; or
3. A rollover repayment of a disaster distribution is reported in boxes 14a and 14b.

It is best if the IRA accountholder who received their 2020 distribution complies with the standard 60-day rule. If the IRA accountholder fails to comply with the 60 day rule, the person will need to decide between using the certified late rollover approach or the special rules applying to a disaster distribution. Almost all distributions from January to March 31, 2020 will qualify as a disaster distribution. Or the individual may need to wait to see if will grant similar relief as granted in Notice 2009-82.

An IRA accountholder must comply with the once per year rule. Some IRA accountholders may have had a prior distribution within the preceding 365 days and so the individual will have to wait until the one year period has expired. This waiting will result in that the rollover will be made outside of the 60 day deadline. These individuals will need to decide between using the certified late rollover approach or the special repayment rollover rules applying to a disaster distribution. Or, the individual may need to wait to see if the IRS will grant similar relief. In 2009 the once per year rule was applied on a per IRA plan agreement basis and in 2020 it is applied on a per person basis.

What are the special rules for a disaster distribution? A disaster distribution(s) on an aggregate basis cannot exceed \$100,000. A person is permitted to take multiple distributions during the disaster relief period. This means there is no once per year rule. There is also no 60 day rule. A person who takes a disaster distribution has three years in which to complete the rollover repayment commencing on the date after day of the distribution. These expanded time periods give a person great flexibility in taking distributions and when taxes must be paid and when a rollover can be completed so the distribution or distributions become non-taxable. The person has great flexibility in using their IRA funds during their recovery period. IRS Form 8915 and instructions should be

reviewed because they present the IRS' understanding of the disaster laws.

For discussion purposes it is assumed that John Doe had his 2020 IRA RMD of \$200,000 distributed to him on February 15, 2020. He had instructed to have 30% or \$60,000 withheld for federal income tax purposes and 5% or \$10,000 withheld for state income tax purposes. \$130,000 was deposited into his checking account. It is now early April and he is still within his 60 day period. He meets the once per year rule because he not had any other IRA rollover within the last four years. He decides now to make a rollover contribution of \$200,000 with respect to this \$200,000 distribution. He will have to raise from personal funds or loans the \$70,000 which had been withheld.

Assuming other tax matters are equal, he would receive a refund of \$70,000 when he files his 2020 tax return or have his credit balance applied to 2021 taxes.

We suggest that the IRA custodian/trustee have John Doe complete CWF's rollover certification Form 65A or a similar form. Form 65C is to be used for a certified late rollover. We need to create the rollover repayment form for a disaster distribution.

An inheriting beneficiary may ask a similar question. "I was paid my 2020 RMD prior to the CARES Act, am I able to return the funds to the inherited IRA?" The answer is no because the law expressly defines a non-spouse beneficiary as being ineligible to make a rollover contribution. In normal times I would not see the IRS granting relief to a beneficiary. In Notice 2009-82 the IRS expressly stated that the special rollover relief does NOT apply to nonspouse beneficiaries. Time will tell if the IRS grants some sort of relief. The IRS' problem, there really is no Internal Revenue Code authority supporting the granting of such relief.

We expect the IRS will issue guidance discussing the waiver of RMDs for 2020 and related rollovers. It will most likely will follow the approach of Notice 2009-82.

In summary, there are going to be IRA accountholders who received their 2020 RMD and now want to rollover that distribution. They can do so as long as the applicable IRA rollover rules are met. We expect the IRS will be issuing additional guidance on this subject.

## **The 5 basic IRA rollover rules:**

1. RMDs cannot be rolled over. They are ineligible for rollover treatment.
2. The 60 day rule. There are exceptions.
3. The once per year (365 day) rule. An IRA owners who withdraws an IRA distribution and rolls over such is eligible to rollover a subsequent distribution only if that distribution is one year or longer after the distribution which was rolled over. For example, Jane Doe takes a distribution on April 1, 2020, and rolls it over within the 60 day period. Jane Doe must wait until at least April 1, 2021 before any subsequent distribution is eligible to be rolled over.
4. The same property rule. If an IRA distribution is comprised of an in-kind asset, that same asset must be comprise the rollover contribution. The asset cannot be sold and the proceeds rolled over. This is an IRA rule. It does not apply to distributions from 401 (k) plans.
5. A distribution from an inherited IRA to a nonspouse beneficiary is always ineligible to be rolled over. The only exception, if the IRS has had to return IRA funds it levied, then the beneficiary has until the April 15th following the year the IRS repaid the levied funds to make his or her rollover contribution.



## Completing Box 11 on the 2019 Form 5498

Box 11 on the 2019 Form 5498 is titled, "Check if RMD for 2020".

IRS instructions are clear, box 11 is to be checked if an IRA owner has an RMD for 2020. Otherwise, box 11 is not to be checked. Due to the CARES Act's total waiver of RMDs for 2020, box 11 on the 2019 Form 5498 should not be checked.

Box 12a (RMD date) and 12b (RMD amount) should also not be completed.

An IRA custodian will wish to check with its core service provider. We recommend an IRA custodian include a short note informing affected IRA accountholders of the RMD waiver for 2020 and what they should do if they wish to terminate their scheduled RMD for 2020.

We will be contacting the IRS for guidance. We expect the IRS will issue additional guidance on the RMD topic in the near future. However, the IRS presently does not have any "live" help until further notice.

Unless the IRS issues additional guidance an IRA custodian must file its 2019-5498 forms by June 1, 2020.

IRA contributions (other than amounts in boxes 2-4, 8-10, 13a, and 14a)	OMB No. 1545-0747		<b>IRA Contribution Information</b>
	<b>2019</b>		
Rollover contributions	Form <b>5498</b>		
Roth IRA conversion amount	<b>4</b> Recharacterized contributions		<b>Copy A</b>  <b>For Internal Revenue Service Center</b> <b>File with Form 1096.</b>
	\$		
FMV of account	<b>6</b> Life insurance cost included in box 1		
	\$		
IRA <input type="checkbox"/> SEP <input type="checkbox"/> SIMPLE <input type="checkbox"/> Roth IRA <input type="checkbox"/>			
SEP contributions	<b>9</b> SIMPLE contributions		For Privacy Act and Paperwork Reduction Act Notice, see the <b>2019 General Instructions for Certain Information Returns.</b>
	\$		
Roth IRA contributions	<b>11</b> Check if RMD for 2020 <input type="checkbox"/>		
RMD date	<b>12b</b> RMD amount		
	\$		
Postponed/late contrib.	<b>13b</b> Year	<b>13c</b> Code	
Repayments	<b>14b</b> Code		
FMV of certain specified	<b>14c</b> Code(s)		

## Email Guidance – HSAs

**Q-1.** As I spoke with my HSA customer she told me she has already signed up for Medicare but it does not take effect until July 1, 2020. In that case can she contribute to her Health Savings for the first 6 months of the year 2020?

**A-1.** A person is ineligible to make an HSA contribution for any month she is "enrolled" in Medicare and all subsequent months.

I understand a person is enrolled even if coverage starts later. A person's enrolling "early" in Medicare does have negative consequences.

Was she enrolled in February? If not, she is eligible to contribute 2/12 or 1/6 of her contribution amount.

**Q-2.** We here at the bank have several HSA account that are going to be escheated to the State Of Michigan (3 Years no activity). We have sent out numerous letters notifying the customer of this action and will also call them. What is the ruling on escheated HSA's?

**A-2.** This is a be careful situation for an HSA custodian. I will need to do further research.

The individual will incur harsh tax consequences. The bank will prepare the Form 1099-SA using the individual's name and not the state's name even though the state is the payee. The individual will be required to include the distribution in income, and if under age 65, the person will owe the 20% penalty tax.

What exceptions apply for the 3 year rule? I realize many states are "hungry" for revenues, but an HSA is a special tax preferred account with the basic concept that it is to be lifetime account. It is not a standard account. To what extent, if any, does the state of Michigan have special rules for HSA's?

Has other mail reached the person?

**Q-3.** We have employer whose accountant has called us. She explained the employer had contributed too much to an employee's HSA. The accountant wants this "excess" amount returned to the employer. Can we do that? Should we do that? The accountant sent me a copy

of a letter written by an employee in the US Treasury indicating that there could be mistaken contribution which could be corrected in addition to the general two situations.

**A-3.** Only partially. An employer is not a party to the HSA plan agreement.

When was the mistaken contribution made? In 2019 or 2020?

When was it determined there was a mistaken contribution?

This is a situation which should be primarily be settled between the employer and the employee.

Have you discussed this situation with the HSA owner? What are her thoughts?

Has the employer discussed the situation with the employee/HSA owner and what were you told?

What are your thoughts at this point on the IRS reporting aspects of the contribution and the distribution? Has the employer, an accountant or an attorney or another adviser requested that the bank have her contribution and her distribution be non-reportable?

Has any one cited you any authority that her contribution and her distribution need not be reported to the IRS?

IRS rules require all non-transfer contributions and distributions to be reported on the Form 5498-SA and Form 1099-SA with limited exceptions. The limited exceptions do not apply to this situation.

Has the employer or an adviser offered to hold the bank harmless if the bank would adopt the employer's requested action?

In general I believe the IRS letter has little value to the bank in defending itself in a court action if it withdraws money from her HSA without her consent. Again, an employer is not a party to the HSA plan agreement.

### **Follow-up**

The contribution was made in Aug 2019. Just identified yesterday when the one employee's W-2 HSA contribution amount didn't match our records. I have explained to the employer that this error is not one of the two allowed by the IRS to let them dip into the employee's account so they will be making it right with the employees themselves. All I will have to do is accept

a 2019 HSA contribution for my account holder and post as such.

Everyone seems okay to move forward with it this way as all parties seem to understand the mistake. Just much less paperwork and headache for us since they all agree to handle themselves.

**Q-4.** We have an HSA customer who recently turned 65 and is ineligible to contribute to his HSA any longer. He wants to take a final distribution of \$705.08 and contribute that amount into his wife's HSA.

Is this something he can do?

We have told him no, but he is pushing back saying he has researched it at another branch and believes it is acceptable.

**A-4.** It is never good to argue with a customer, but hopefully he is willing to consider my discussion.

It may be he has had the HSA, but now his wife will have an HSA also. He should not feel he needs to close his HSA in order to open hers. Sometimes it is best if there are two HSAs.

It may well be that he can do what he is proposing (take a distribution), but for tax/financial reasons I don't believe he will want to.

### **My discussion:**

1. It is for him to take a distribution and make the distribution non-taxable by making a rollover contribution into his wife's HSA. I have never seen any authority saying such a rollover can be done. If he has research explaining it can be done I would like to review it.
2. If he withdraws the \$705.08 he will be required to include it in his income because it will not be used to pay a qualified medical expense. Although a 20% tax penalty is normally assessed a withdrawal not used to pay a medical expense, the 20% tax is not assessed when the person is age 65 or older.
3. The \$705.08 which is withdrawn could be the source of cash to be used to be part of her annual contribution. But by doing this there is no tax benefit with respect to the \$705.08 - the contribution of the \$705.08 is offset by his withdrawal of the \$705.08.

Tax Consequences,  
Continued from page 6

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4. He should keep the \$705.08 in his HSA. There should be no rush to close his HSA.

5. It may be a strange law, but when each spouse has their own IRA, a spouse is not required to pay their medical expense from their HSA. A husband has the right to pay his wife's medical expense as well as his own medical expenses and she vice versa. Obviously, the same medical expense cannot be paid by both HSAs.

If he wishes to close his HSA because he can no longer make contributions, he can achieve this result by paying her medical expenses until his HSA is closed.

**Q-5.** If we have a spouse who had an HSA at another F.I. but is now covered under his wife's medical plan can we transfer his HSA to his wife's HSA account with us since he's now covered under her high deductible plan?

**A-5.** No. His HSA funds cannot be transferred into her HSA.

An HSA is an individual account. It benefits a specific person. It is "owned" by a specific person.

HSA funds may be transferred from one spouse to the other spouse only in two situations - divorce pursuant to a court order and after a person's death. Other transfers while alive are not authorized.

To have and to make contributions to an HSA a person at one time must be covered by a HDHP. That HDHP could have single coverage or family coverage.

The law limits the maximum contribution of a married couple to \$7,100 for 2020 as long as one or both spouses have family coverage. Each spouse has the right to contribute for 2020 50% or \$3,550 to their respective HSA unless they agree to split it differently. The fact that she is the source of the HDHP does not mean she has superior rights to him. That is, she can't require that \$7,100 of contributions will go into her HSA. He can agree that any 2020 contributions will go into her HSA. Any contribution made by her employer must go into her HSA. Otherwise, contributions may go into his HSA.

They may prefer to have only one HSA. They can achieve that goal by withdrawing funds from his HSA

to pay his medical expenses and to pay her medical expenses.

**Q-6.** I have a customer who is wanting to max out his HSA contribution for the current year (2020). He is eligible for the HSA and will remain eligible but intends to drop the HSA with his employer July 1. His age is 39 and has in individual HSA. Can he put the full \$3,550 in the account prior to him discontinuing the HSA?

**A-6.** Is he dropping his single HDHP coverage? Has his employer initially chosen the financial institution which has his HSA?

A person must have HDHP coverage in order to make an HSA contribution. Is he married so he would maintain coverage via his spouse's employer's HDHP?

If he has no HDHP coverage after 6/30/20, that will certainly affect his maximum contribution amount for 2020. He would only be eligible to contribute 50% of the \$3,550 or \$1,775. Any amount contributed in excess of the \$1,775 will be an excess contribution. The general rule is, a person is eligible to contribute 1/12 of the annual amount for each month (determined on the first day of the month) they have coverage. There is the exception of the last month rule but it won't apply if he is not covered in December.

Technically, he can contribute the full amount, but he will have an excess contribution situation. Making the contribution prior to dropping the coverage does not make any contribution in excess of \$1,775 permissible or deductible.

**Q-7.** I had my first ever HSA accountholder pass away. His beneficiary is his elderly father.

I understand only a spouse can continue an HSA account in their own name so am I to simply do a distribution (death distribution to non-spouse) and cut a check to the father?

**A-7.** Yes, you should cut a check to the father.

Will any of the funds be used to pay some of the decedent's medical expenses? If so, such distributions would reduce the amount he must include in his income.

**Q-8.** I need a little clarification in regards to the death of an HSA owner.

If the sole Beneficiary of an HSA is the spouse does the spouse have to put the HSA funds into an HSA in their name prior to withdrawing the funds or can they simply close the HSA without putting the funds into their name first if they choose to no longer have an HSA?

**A-8.** If the HSA owner has designated their spouse to be their beneficiary, the surviving spouse becomes the Hsu new owner upon the HSA owner's death. This happens as a matter of law. There is no right to not treat the decedent's HSA as his or her HSA.

This rule means the surviving spouse will want to use the HSA as any other HSA owner to pay medical expenses not covered by other insurance. An HSA must be established for the surviving spouse.

The surviving spouse, of course, has the right to close the HSA by taking a distribution. However, if the distribution is not used to pay a qualified medical expense, he or she is required to include the distribution in income (and pay tax) and he or she will also owe the 20% penalty tax unless age 65 or disabled.

The HSA custodian is required to prepare a final Form 5498-SA for the deceased spouse and must prepare a Form 5498-SA and/or Form 1099-SA for the surviving spouse, as applicable.

## Email Guidance – SEP-IRA

**Q-1.** We have a few questions regarding SEP-IRA.

When a SEP contribution is made in a Traditional IRA, is a form required to be signed? I see the CWF #54 and believe it is a good idea to have on file but am wondering if it or anything else is required.

When opening a SEP-IRA, is CWF #700 or CWF #702 required? If so, which one or both? Can you tell me when each one would be used?

**A-1.** The standard IRA plan agreement as written by the IRS authorizes the making of an annual contribution, a SEP-IRA contribution, a rollover contribution and/or a recharacterized contribution.

I believe a person must designate that a SEP-IRA contribution is being made and for which tax year. The SEP-IRA contribution must be distinguished from other types

of contribution types - a rollover, a recharacterization, a SIMPLE-IRA contribution or an annual contribution.

In order for a business to establish a SEP-IRA plan the employer must complete Form 5305-SEP. This is CWF's form #700.

The business owner completes this form. It only needs to be done once. The owner should retain the original and give each eligible employee a copy and each IRA custodian a copy. Note the IRA custodian/trustee is not a party to the Form 5305-SEP.

In addition to completing Form 5305-SEP, each eligible employee must have a SEP-IRA. Unfortunately, each employee can choose where they will establish their SEP-IRA to receive the employer's contribution. However, there may be times when you will service an employee who is not the business owner. That business owner should have furnished the employee (your client) with a copy of the Form 5305-SEP. Ask your client for a copy.

The above applies to one person plans and multiple person plans.

An IRA trustee wants a file for each SEP-IRA client. In the file would be a copy of the Form 5305-SEP as completed by the business and there would be Form 41-T indicating a SEP-IRA contribution was made. Subsequent SEP-IRA contributions should be reflected on a standard IRA contribution form. SEP-IRA contributions are to be reported in box 8 of the Form 5498. Standard traditional IRA contributions get reported in box 1 of the Form 5498.

We furnish the Form #702 because we believe it important that the business owner understands this is a retirement plan and there are administrative duties to be performed. We don't want the business to be able to argue, "but I thought ABC Bank was assisting me and would be performing these duties." Use of Form #702 is certainly optional on the part of the IRA trustee.

Many financial institutions do not want to perform these administrative duties. That may not be the case for a trust entity. I expect some employers would appreciate and be willing to pay an annual administrative fee for assisting with the SEP plan.if there are

Please contact me if there are additional questions. As you know, SEP contributions can be substantial. The maximum amount for 2019 is \$56,000 and is \$57,000 for 2020.