The Pension Digest

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ALSO IN THIS ISSUE –

Collin W. Fritz and Associates, Inc.,
"The Pension Specialists "

The IRS Grants Additional 2023 RMD and Rollover Relief

The IRS released online Notice 2023-54 on July 14, 2023. The IRS has issued relief to certain IRA accounholders, IRA Custodians/Trustees and certain IRA beneficiaries.

The IRS had released Notice 2022-53 in October of 2022. These two notices are similar in that the IRS grants special tax relief to certain taxpayers in both notices. An article on Notice 2022-53 is set forth on page 2 of this newsletter.

The SECURE Act 2.0 as enacted on December 29, 2022 changed the mandated age for commencing required minimum distributions (RMDs) from age 72 to age 73 and this change was effective immediately for 2023.

Prior to the law change, a person attaining age 72 in 2023 would have been required to take an RMD for 2023. The requirement to take an RMD for 2023 was repealed for those individuals who would have attained 72 in 2023.

IRS rules and procedures required that an IRA custodians/trustee furnish by January 31, 2023 an RMD notice to individuals who had to take an RMD for 2023. The RMD Notice for each such IRA accountholder who has a FMV balance as of 12/31/2022 must contain three items of information: (1) be informed of the amount of the RMD for 2023; (2) be informed of the applicable deadline for withdrawing the RMD and be informed that when the IRA custodian/trustee files their 2022 Form 5498 that the IRS will be informed that the person must take an RMD for 2023.

Some IRA custodians/trustees commented to IRS that they or their core vendors had insufficient time to change their computer programs. Their computer programs had been written to comply with the fact that the RMD mandatory age was 72. So certain IRA accountholders were mistakenly sent 2023 RMD Notices which informed them that they had to take an RMD for 2023.

Any IRA accountholder who receives or withdraws an RMD is ineligible to rollover the RMD distribution. These IRA accountholders did not rollover their distributions because they correctly understood that an RMD could not be rolled over. However, the distributions they had received were NOT RMDs under the law so they were eligible to be rolled over. Once these individuals learned their distributions were not RMDs and were eligible to be rolled over, the 60 day period had expired and the distributions were no longer eligible to be rolled over.

So, what special tax relief has been granted or extended by the IRS and to whom?

In March of 2023 the IRS had issued Notice 2023-23. It stated, "The IRS will not consider an RMD statement provided to an IRA owner who will attain age 72 in 2023 to have been provide incorrectly if the IRA owner is notified by the financial institution no later than April 28, 2023 that no RMD is required for 2023."

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RMD and Rollover Relief,
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The IRS is now in Notice 2023-54 clarifying certain tax rules and also granting tax relief to certain individual IRA accountholders and also to certain beneficiaries.

First, the IRS states that the final regulations regarding RMDs will apply for calendar years beginning no earlier than 2024. Previously, the IRS had stated that the final regulations regarding RMDs will apply for calendar years beginning no earlier than 2023. That is, the final regulations would apply for 2023. So, the final RMD regulations will not apply for 2023. The IRS fails to issue any further guidance.

Second, when an individual fails to take their entire RMD for the year by the applicable deadline there will be due an excise tax equal to 25% of the missed RMD. However, there is a large exception and the 25% rate is reduced to 10% if the person withdraws their missed RMD by the end of a correction period which is generally the end of the second year that begins after the year of the missed RMD. So, an individual who corrects it by this deadline is subject to the 10% tax rate and not the 25% tax rate. A lengthy correction period is provided by the law and the IRS acknowledges this.

Third, the tax relief granted by Notice 2022-53 with respect to certain beneficiary RMD distributions which should have occurred in 2021 and 2021 has been extended to include distributions which should have occurred in 2020, 2021 and/or 2022.

Fourth, the IRS states the 60-day rule will not apply to an IRA owner who received in a single transaction an RMD because he or she attained age 72 in 2023 and thought it was ineligible to be rolled over since it was an RMD. The IRS has stated that the individual may rollover such amount by September 30, 2023. This rollover is permitted even if the IRA owner or the surviving spouse has rolled over a distribution within the last 12 months. However, the making of such a rollover contributions must be considered when determining if a subsequent distribution is eligible to be rolled over. Twelve months would need to elapse before a later distribution would be eligible to be rolled over.

The current actions taken by the IRS are certainly welcomed by both IRA custodians/trustees, the core data processing vendors and IRA beneficiaries. There is no doubt that the IRS is behind in adopting its revised RMD regulations and related regulations. One wonders if the final regulations will be issued in 2023 or 2024. The IRS appears to not be adopting an approach of trying to keep things simple.

IRS Grants Welcome Relief For 2021 and 2022 For Certain IRA Beneficiaries

The IRS released Notice 2022-53 late on Friday, October 6, 2022.

There are 2 purposes to the Notice:

1. The IRS announces that the to-be-issued final RMD regulations will apply to 2023 and subsequent years.

2. The IRS has stated it won't assess the 50% tax for 2021 and 2022 for the beneficiaries of IRA owners who died in 2020 and 2021 and who had died after their required beginning date.

The IRS has adopted he position that a beneficiary of an IRA owner who dies after their required beginning date must use the applicable life distribution rule applying to the beneficiary and also comply with the 10-year rule, if applicable. That is, a beneficiary is unable to use just the 10-year rule when the IRA owner has died after their required beginning date.

Until Friday the IRS had stated this RMD rule applied for 2021 and 2022 and the 50% tax would be owed, If applicable, if a beneficiary missed their annual RMD. For example, Julia is 48 and the beneficiary of an IRA owner who died in 2021 at age 76. Julia is not an EDB. She must withdraw her first RMD in 2022, withdraw her RMD for subsequent years and she must close the IRA by 12/31/2031.

The IRS will be issuing additional RMD guidance and we will discuss it when available. There is no indication of what other changes, if any, will be made in the final regulations. The IRS did not discuss whether the IRA custodian/trustee has any duty to notify such beneficiaries. There is no discussion of RMDs for 2020 because RMDs were waived for 2020 by the CARES Act.

There is no indication that the IRS will be seeking additional public comments.

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Relief for 2021 and 2022,
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We at CWF, have revised our MINCAL software to perform these calculations as we were unsure if the IRS would be granting any relief for 2021 and 2022. Please contact us if you have any questions. Although we prefer an email, you may call us at 800-346-3961.

How Should IRA Administrative Fees Be Paid?

By the Individual or Withdrawn From the Traditional IRA or the Roth IRA?

It is best for an IRA custodian/trustee to have the authority to withdraw from an IRA (traditional or Roth) any fees owed to the IRA custodian trustee. The CWF IRA plan agreements provide such authority. However, as discussed in this article, the Roth IRA accountholder will benefit if the Roth IRA custodian/trustee will accommodate a client and allow him or her to pay administrative expenses with personal (non-IRA) funds rather than having the fees deducted from the Roth IRA.

The answer depends upon the type of IRA. John Doe has a traditional IRA with Bank Ten and a Roth IRA with Bank Ten. Bank Ten will charge $100 for transferring the two IRAs or $50 for each transfer. The two IRAs are being transferred to Bank Eight. For the reasons discussed below, John Doe wants to have the $50 transfer fee deducted from the traditional IRA, and wants to pay with personal funds the $50 fee to have the Roth IRA transferred.

We recently furnished the following Email guidance to an IRA trustee. The customer wanted his traditional IRA to pay the fees of his Roth IRA? This cannot be done and the customer needs to be so informed.

Q-1. Hello - is John Smith's IRA able to pay the fees for John Smith's Roth IRA? Or vice versa?

A-1. This is a be careful area.

The conservative answer is - a person cannot pay the fees related to the Roth IRA from the traditional IRA. To do so, creates a tax and financial benefit for the Roth IRA owner.

The IRS a long time ago issued guidance for fees related to traditional IRAs, but IRS guidance on fees for Roth IRAs has been minimal. An individual is permitted to pay for "administrative" expenses with personal funds and such fees need not be paid by the IRA be it a traditional IRA or a Roth IRA.

Fees intrinsic to the IRA investments must be paid by the IRA and cannot be paid by the individual. If the individual uses personal funds to pay such fees, such payments must be considered a reportable IRA contribution.

I believe the IRS and the DOL will take the position - a prohibited transaction occurs when a traditional IRA pays the fees related to the Roth IRA. I don't think it would be the case very often, but there would also be a prohibited transaction if the situation was vice versa. I am not sure whether the IRS would look to the IRA trustee or the IRA grantor as the party responsible for the PT.

A person wants his or her traditional IRA to pay the administrative expenses of the traditional IRA because it will lessen the amount to be included in income for tax purposes. That is, the person should be agreeable to having the traditional IRA custodian/trustee withdraw the funds from the traditional IRA.

A person wants to pay any administrative expenses associated with his or her Roth IRA with personal funds. The person does not want the Roth IRA to pay such expenses. The person does not want the Roth IRA custodian/trustee to withdraw the fees from the Roth IRA. Even though a person is no longer eligible to deduct as a miscellaneous deduction his or her payment of these fees, a person will still want to pay these administrative fees with personal funds because the Roth IRA balance will increase more. A person wants to maximize his or her Roth IRA balance. If the individual uses personal funds to pay such administrative fees, such payments need not be considered a reportable Roth IRA contribution.

The IRS and the DOL should be furnishing additional guidance on the fee subject(s). The IRS of 2023 is not the IRS of 2000. However, taxpayers may be benefiting because the IRS has not issued new guidance.

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SEPs Are So Simple – Be Eagar to Seek and Accept SEP-IRA Contributions

Establishing a SEP

Who can establish a SEP?

Any employer, including self-employed individuals, can establish a SEP.

Is there a deadline to set up a SEP?

You can set up a SEP plan for a year as late as the due date (including extensions) of your business's income tax return for that year.

If I have a SEP, can I also have other retirement plans?

You can maintain both a SEP and another plan. However, unless the other plan is also a SEP, you cannot use Form 5305-SEP; you must adopt either a prototype SEP or an individually designed SEP.

Can I set up a SEP for my self-employment income if I participate in my employer's retirement plan?

Yes, you can set up a SEP for your self-employed business even if you participate in your employer's retirement plan at a second job.

Can each partner in a partnership maintain a separate SEP plan?

No, only an employer can maintain and contribute to a SEP plan for its employees. For retirement plan purposes, each partner or member of an LLC taxed as a partnership is an employee of the partnership.

Participation

Which employees are eligible to participate in my SEP plan?

Employees must be included in the SEP plan if they have:

- attained age 21;
- worked for your business in at least 3 of the last 5 years; and
- received at least $650 in 2021, 2022 or 2023;

Your plan may use less restrictive requirements, for example age 18 or three months of service, to determine which employees are eligible.

Are the eligibility requirements the same for all employees in a SEP plan, including owners?

Yes. The eligibility provisions stated in the SEP plan document must apply equally to owners and employees.

Contributions

How much can I contribute to my SEP?

The contributions you make to each employee's SEP-IRA each year cannot exceed the lesser of:

1. 25% of compensation, or
2. $66,000 for 2023 ($58,000 for 2021; $61,000 for 2022 and subject to annual cost-of-living adjustments for later years).

These limits apply to contributions you make for your employees to all defined contribution plans, which includes SEPs. Compensation up to $330,000 in 2023 ($305,000 in 2022; $290,000 in 2021 and subject to cost-of-living adjustments for later years) of an employee's compensation may be considered. If you're self-employed, use a special calculation to determine contributions for yourself.

Contributions must be made in cash; you cannot contribute property.

If you've contributed more than the annual limits to your SEP plan, find out how to correct this mistake.

How much can I contribute if I'm self-employed?

The same limits on contributions made to employees' SEP-IRAs also apply to contributions if you are self-employed. However, special rules apply when figuring the maximum deductible contribution. See Publication 560 for details on determining the contribution amount.

Must I contribute the same percentage of salary for all participants?

Most SEPs, including the IRS model Form 5305-SEP, require you to make allocations proportional to your employees' salary/wages. This means that everyone's contribution is the same percentage of salary.

If you are self-employed, base your contribution on net profit - minus one-half of the self-employment tax - minus your SEP contribution. See IRS Publication 560 on determining the contribution amount.

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SEPs,
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If I participate in a SEP plan, can I also make tax-deductible traditional IRA contributions to my SEP-IRA?

If the SEP-IRA permits non-SEP contributions, you can make regular IRA contributions (including IRA catch-up contributions if you are age 50 and older) to your SEP-IRA, up to the maximum annual limit. However, the amount of the regular IRA contribution that you can deduct on your income tax return may be reduced or eliminated due to your participation in the SEP plan.

Must I contribute to the SEP every year?

No, you are not required to contribute every year. In years you do contribute to the SEP, the contributions must be made to the SEP-IRAs of all eligible employees.

Do I have to contribute for a participant who is no longer employed on the last day of the year?

Yes, you do, if they are otherwise eligible for a contribution. A SEP cannot have a last-day-of-the-year employment requirement. If the employee is otherwise eligible, they must share in any SEP contribution. This includes eligible employees who die or quit working before the contribution is made. If you haven't made a contribution for an eligible employee in your SEP plan, find out how you can correct this mistake.

Can I contribute to the SEP-IRA of a participant over age 73?

You must contribute for each employee eligible to participate in your SEP, even if they are over age 73. The employee must also take minimum distributions.

When must I deposit the contributions into the SEP-IRAs?

You must deposit contributions for a year by the due date (including extensions) for filing your federal income tax return for the year. If you obtain an extension for filing your tax return, you have until the end of that extension period to deposit the contribution, regardless of when you actually file the return.

How much of the SEP contributions are deductible?

The most you can deduct on your business's tax return for contributions to your employees' SEP-IRAs is the lesser of your contributions or 25% of compensation. (Compensation considered for each employee is limited and subject to annual cost-of-living adjustments). If you are self-employed and contribute to your own SEP-IRA, there is a special computation to figure the maximum deduction.

Are employer contributions taxable to employees?

No, contributions to employees' SEP-IRAs are not included in their gross income, unless they are excess contributions.

If my SEP plan fails to meet the SEP requirements, are the tax benefits for me and my employees lost?

Generally, tax benefits are lost if the SEP fails to satisfy the Internal Revenue Code requirements. However, you can retain the tax benefits if you use one of the IRS correction programs to correct the failure. In general, your correction should put employees in the position they would have been had the failure not occurred.

Reporting Requirements

Why is last year's contribution that was made this year for the SEP-IRA shown on this year's Form 5498 instead of last year's Form 5498?

The IRS requires contributions to a SEP-IRA to be reported on the Form 5498 for the year they are actually deposited to the account, regardless of the year for which they are made.

Why is the IRS Downplaying COVID-19?

On June 22, 2023, the IRS issued new HSA guidance in Notice 2023-37.

The IRS has announced that the COVID-19 guidance and tax relief set forth in Notice 2020-15 will no longer apply except for a limited time period. The IRS also discusses new relief rules.

In general, the past few years a HDHP plan has been allowed to pay almost all medical expenses related to preventive care with respect to COVID-19 even though a person had not met the HDHP's minimum deductible limit. The IRS is changing the rules so that now such expenses would need to be paid by the individual or from the individual's HSA before the HDHP paid these expenses. The IRS is limiting the tax relief.

First, if the HDHP plan has a plan year which ends on or before December 31, 2024, then relief continues to apply. However, there is no relief if the HDHP's plan year ends on or after January 1, 2024. This means there will be no relief if the plan year runs from February 1, 2024 to January 31, 2025. However, relief still applies if the HDHP has a fiscal calendar year plan year of July 1, 2023 to June 30, 2024, then the relief provided by Notice 2020-15 ends on June 30, 2024.

Second, the preventive care safe harbor as set forth in Notice 2002-23 does not include COVID-19 testing or screening effective as of the effective date of this notice which is June 22, 2023.

Third, the IRS changes the definition of what purchases of medical services or products are defined to be preventive care. Preventive care does not generally include any service or benefit intended to treat an existing illness, injury or condition. For example, screenings for common illnesses such as flu are not included in the safe harbor. However, the Appendix to Notice 2004-23 includes as being entitled to safe-harbor status the Infectious Diseases Screening Services for the following infections: Bacteriuria, Chlamydia Infection, Gonorrhea, Hepatitis B Virus Infection, Hepatitis C, Human Immunodeficiency Virus (HIV) Infection, Syphilis and Tuberculosis Infection.

The IRS considers COVID-19 to be sufficiently different from these infections so the testing or screening for COVID-19 no longer qualifies for safe harbor treatment. This change is effective as of the date of publication of this notice which is June 22, 2023.

The IRS is being inconsistent - COVID-19 certainly is not a common illness, COVID-19 is more like those other serious viruses rather than the flu.

Fourth, the IRS acknowledges that its decision that the medical expenses related to COVID-19 if incurred after March 23, 2010 may be treated as preventive care for HSA purposes regardless of whether these services and items must be subject to cost sharing under Public Health Services Act (PHS Act) section 2713 if the USPSTF rates COVID-19 testing with an "A" or"B" rating, then that testing would be treated as preventive care.

HSA Telehealth Exception for 2023 and 2024

The general rule is a qualifying HDHP must not pay for an HSA owner's medical expense until the HDHP's deductible limit has been met. The minimum deducible for self-only coverage is $1,400 for 2022, $1,500 for 2023 and $1,600 for 2024.

Due to COVID-19, the law was changed to provide that an HSA owner could receive medical services via telehealth and the receipt of these services would qualify as a qualified medical expense for HSA purposes even though the deductible requirement had not been met.

The CARES Act had authorized this special treatment for 2021 and the 2022. Consolidated Appropriations Act had extended for 2022. The 2023 Consolidated Appropriations Act as enacted on December 29, 2022 extends it for two more plan years beginning after December 31, 2022. An HSA owner must rely on their tax year as there may be some drafting issues regarding calendar year coverage and plan year coverage.

Email Guidance – Most Exceptions to 10% Tax Are Still to be Coded a "1"?

Q-1. I received an email from a customer that wants to make a withdrawal from her IRA for her son's first-time home purchase. The little research that I did says you can withdrawal up to $10,000 from your IRA for YOUR first-time home purchase. Does that carry through to your kids? I could not find that it does anywhere.

A-1. An IRA owner under age 59½ may take a distribution and claim on Form 5329 that he or she meets the requirements for the first-time home buyer exception.

The IRA owner may give the funds to a son so he may use it for his first home. The son is subject to the 2-year rule and not the IRA owner.

Q-1A. So, do we just do this as a normal distribution? Or do we' code it some special way?

A-1A. The bank codes it as a general distribution to a person who I assume is under age 59½.

Code "1" is to be used on the Form 1099-R in box 7.

The individual is responsible to complete Form 5329 and claim the exception from the 10% additional tax.

Email Guidance – Is it a Rollover or a Transfer?

Q-1. We have a customer who wants to rollover an annuity from Bankers Life to an IRA here at the bank. Bankers life Is saying we need to send them a Letter of Acceptance in order to do that. Do you have an example of a Letter of Acceptance?

A-1. Is this a rollover or transfer situation?

What type of plan or IRA is making the distribution?

Is it an IRA annuity or is it an annuity related to an employer sponsored retirement plan?

If it is an IRA annuity, will Bakers Life accept an IRA transfer form? The transaction would be structured as a transfer rather than as a rollover. Use the standard transfer form.

It is questionable whether Bankers Life in a direct rollover situation from an employer sponsored retirement plan has the right to require the IRA custodian/trustee to furnish a letter of acceptance when the customer has certified that she or he has an IRA with you. But you can use CWF Form 66 or 66A. The IRS in its guidance of direct rollovers from a 401(a) plan or a 403(b) has never discussed a requirement the IRA custodian must furnish a letter of acceptance.

Email Guidance – Procedures for Roth IRA Conversion Contribution

Q-1. I have a customer that wants to take $100,000.00 out of her traditional IRA and put it into a ROTH IRA. Would this be coded as a transfer?

A-1. Your customer is wanting to make a Roth IRA conversion contribution. Hopefully the customer understands that her conversion is irrevocable. She will be required to include the $100,000 in her income for 2023 income tax purposes.

This special type of transfer distribution is not to be coded as a transfer. It must be a code a "2" if the person is under age 59½ and a "7" if the person is over age 59½. She should sign a standard IRA distribution form and furnish her withholding instruction. I presume she will instruct to have no federal income tax withheld. However, she may instruct to have withholding.

Our IRA FormSystem does have Form 56TC where a customer instructs that he or she is making a conversion.

The $100,000 will be converted/added to her Roth IRA. Her Roth IRA conversion contribution is to be reported as a conversion contribution in box 3 on the 2023 Form 5498 for the Roth IRA. You should check with your Core vendor as what transaction code you need to use to get it reported in box 3.

Q-2. We have a customer who wants to roll funds from her Traditional IRA to a new ROTH. She is 76 years old. She has been advised by her accountant to do so.

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Roth IRA Conversion,
Continued from page 7

I just want to verify the coding, so I don't mess it up! This is what I think it should be:

- The initial distribution out of her Traditional IRA would be coded as a "Distribution" in our system and then we would put as a "2 - Early Distribution with exception" the following day.
- The contribution to her new ROTH would be coded as a "rollover credit".

Is this what you would advise?

A-2. She is making a Roth IRA conversion contribution to her Roth IRA from her traditional IRA.

She is over age 59½, so the bank should code the distribution as a normal "7". The "2" is to be used if she would be under age 59½. A person does not have the 10% additional tax even if she is younger than age 59½.

Check your transaction codes. This is not a normal rollover which is reported in box 2 of the Form 5498. This conversion contribution needs to be reported in box 3. This is a special rollover - going from a traditional IRA to a Roth IRA.

HSA Report by Congressional Research Service

In August of 2022 the Congressional Research Service updated its report on Health Savings Accounts.It was prepared for members and committees of Congress. This report is 24 pages. It discusses in detail HSAs. We have chosen to reprint its discussion on allowable contributors to an individual's HSA. An employer may be a contributor, but is not required to be a contributor. Tax statistics do show many employers do make HSA contributions. This discussion is set forth below.

Allowable Contributors

Eligible individuals may make direct contributions to their HSAs, and employers, family members, and other individuals may make contributions to an individual's HSA on the individual's behalf. Contributions by one individual or entity do not preclude contributions by others, provided the total amount of contributions does not exceed annual contribution limits.

Employed individuals may make HSA contributions through cafeteria plans-that is, benefit arrangements established by employers under which employees accept lower take-home pay in exchange for the difference being deposited in their HSA account. Because these types of individual contributions are excluded from gross income, they are not tax deductible. The IRS has determined that salary reduction agreements must allow employees to stop, increase, or decrease their HSA contributions throughout the year as long as the changes are effective prospectively; however, employers may place restrictions on HSA contribution elections under this type of arrangement if the restrictions apply to all employees. The IRS also has determined that under these agreements, employers are allowed to make an employee's annual expected HSA contribution available to the employee so that the employee may cover medical expenses that exceed his or her current HSA balances, provided the employee repays the accelerated contributions before the end of the year.

HSA contributors cannot restrict how HSA funds are used. For example, employers may not limit HSAs to certain medical expenses (or medical expenses only), even for funds they contribute. Therefore, account owners may make withdrawals from their HSA for any purpose, though nonqualified withdrawals are subject to taxation, as discussed in the section "Nonqualified Expenses."

Eligible individuals may use other tax-advantaged accounts to increase the amount of resources available in their HSAs. Specifically, individuals may make one rollover contribution to an HSA from an Archer MSA or another HSA during a one-year period. Individuals also may make once-in-a-lifetime distribution from their traditional or Roth IRA and deposit it into an HSA, which is factored into the annual contribution limits described in the "Contribution Limits" section. These types of HSA contributions are subject to different tax rules than individual HSA contributions, as discussed in the "Tax Advantages of HSAs" section.