Proposed IRA Law Changes by Senator Hatch
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On July 8th, Senator Hatch introduced a tax bill which would change many IRA and pension laws. Set forth is a summary of the IRA changes. The pension plan changes are discussed in a separate article. The insurance industry and the securities industry are suggesting changes benefiting their members to the detriment of banks, credit unions and trust companies.

In general these changes would apply to 2014 (i.e. plan years commencing in 2014). Some changes would be effective as of July 8, 2013.

Considering the political situation, the fate of these proposals is uncertain. It may be possible that some will be enacted to show there can be bi-partisanship between Republicans and Democrats.

1. **Mortality Tables for RMDs Must be Updated.** Within one year of enactment the IRS shall either update the existing mortality tables or provide new tables. Any "new" table shall apply to plan years beginning after the date which is one year after publication. The IRS is to issue new tables at least every five years thereafter.

2. **RMD will be Eligible to be Converted to Roth IRA.** Under current law a person is ineligible to convert funds within a traditional IRA to a Roth IRA since the law does not permit a person to rollover a required distribution. The proposal would allow RMDs to be rolled over or converted to a Roth IRA.

3. **Expand Law on Correcting Errors to Include IRAs**. Except for the special letter program for missed rollovers the IRS has not developed any procedures to correct errors occurring with respect to traditional IRAs and Roth IRAs. Substantial filing fees apply to use the rollover letter program ($500-$3,000). The IRS has adopted procedures for SEP-IRAs and SIMPLE-IRAs. For its own reasons the IRS has not been proactive in providing additional guidance on correcting IRA mistakes. The IRS seems to forget that IRAs hold 27% of retirement assets while pension plans hold 22%.

   The proposed law would be, as for pension plans, any inadvertent RMD error with respect to an IRA shall be able to be self-corrected, without the imposition of the 50% tax as long as the late distribution is distributed no more than 180-days after it was required to be made.

   In addition the IRS is to amend its EPCRS program to provide that inadvertent IRA errors may be corrected as long as such errors were not the fault of the IRA owner. Some of the errors which may be corrected are those discussed below, but it is intended that additional errors may also be self-corrected.

   There needs to be a waiver of the 60 day deadline for a rollover where the deadline is missed for reasons beyond the reasonable control of the accountholder.

   A non-spouse beneficiary will be allowed to return a distribution from an inherited IRA if the distribution was caused by the inadvertent error of the IRA custodian which gave the beneficiary the reasonable belief he or she could rollover such distribution so that the distribution would not be taxable.

4. **New Joint Authority for the IRS and the DOL Regarding Prohibited Transactions Associated with IRAs and Pension Plans.** Under current law the authority to grant exemptions for prohibited transactions related to pension plan and IRAs is held by the DOL.

The proposed law would give joint authority to the IRS and the DOL. The IRS and DOL would be required to issue joint rulings. This change would be effective as July 8, 2013.

The securities industry does not like how it is being treated by the DOL. The DOL has agreed to only offer a limited prohibited transaction exemption and the securities industry finds this unacceptable. The power of the DOL will be reduced.

5. **Authorize an Employer to Substitute a Safe Harbor 401(k) Plan for a SIMPLE-IRA Plan.** Under current law an employer sponsoring a SIMPLE-IRA plan is not allowed to terminate the plan before January 1 of the following year. An employer would be authorized to terminate the SIMPLE-IRA plan during the current year as long as the employer substitutes a safe harbor 401(k) plan as of the date of termination. A combined elective deferral limit would apply.

6. **Authorize New Rollover to an IRA.** Under current law, if a qualified plan holds on behalf of a participant a qualifying insurance contract, such contract is not eligible to be directly rolled over into a traditional IRA. The insurance contract either must be liquidated for cash or distributed to the individual in-kind. This law would be changed to allow the rollover or direct rollover of an insurance contract within a qualified plan into a traditional IRA even though the general rule is that IRA funds may not invest in life insurance contracts.

7. **New Type of Deemed IRA.** Current law authorizes funds within a 403(b) custodial account then the custodial account will become a deemed IRA with the financial institution holding the 403(b) assets as of the date of the termination. The deemed IRA will be created only if the financial institution holding the assets has demonstrated to the IRS that it is qualified to serve as a IRA trustee/custodian.

8. **Required Distribution Rules Modified for IRAs, 403(b) and Defined Contribution Plans When a Deferred Annuity is Bought Prior to Age 70½.** It is ironic. The IRS cannot be persuaded to voluntarily update the RMD tables so people will be allowed to take smaller RMDs, but the IRS and the DOL are enamored with the planning features of deferred annuities. The argument being made by insurance companies and people who sell annuities is that people are living longer. Therefore, to ensure they will have money when they are in their 80's they should be able to reduce their RMDs when in their 70's.

The RMD proposal would be that amount invested in a deferred annuity would not be counted as part of the IRA's fair market value for the RMD calculating. In order to receive this treatment the following rules must be met.

1. Under such an annuity, payments are deferred past age 70½ but such payments must commence no later than the date the individual attains the age of 85.

2. The annuity must be a commercial annuity, a single life annuity for the life of the individual, providing substantially equal periodic payments at least annually. Or the annuity may be a qualified joint and survivor annuity which is the actuarial equivalent of the singe life annuity.

3. The annuity must be purchased on or before the individual's required beginning date.

4. The individual's investment in the annuity cannot exceed 25% of the individual's entire interest in all plans (defined contribution, IRA and 403(b)) determined as of the close of the calendar year preceding the calendar year in which the purchase occurs. A special rule applies

if the individual dies before his or her required beginning date and he or she does not purchase a qualified deferred annuity and the designated beneficiary is his or her spouse. In this case, the surviving spouse may invest any portion of the entire interest (not 25%) in the same manner as the spouse who died, but the required beginning date and the deferral period will be based on the dates the deceased spouse would have attained age 70 1/2 or 85.

The deferred annuity has features very similar to those found in a lifetime income investment. A lifetime income investment is to have a lifetime income feature. This means a feature that guarantees a minimum level of income at least annually for the remainder of the employee's life (or the remainder of the employee's life along with his or her designated beneficiary) or an annuity where the payments are made in substantially equal periodic payments over the employee's life (or the remainder of the employee's life along with his or her designated beneficiary).