

RECONSIDERATION OF ACTION ON DECISION

CC:EBEO:Br7
CC-1988-010

RECONSIDERATION OF ACTION ON DECISION

Subject: Larotonda v. Commissioner
89 T.C. 287 (1987)

Issue:

Whether petitioner's constructive receipt of a Keogh account distribution by virtue of the government's levy on the account causes the Keogh owner to also be liable for the 10 percent early distribution tax under I.R.C. § 72(m)(5).

Discussion:

Petitioner was a self-employed attorney who established a Keogh retirement account for himself in late 1976. Maximum deductible contributions were made for the years 1977-1980 and considerable tax-free interest was earned thereon. A tax deficiency was assessed against petitioner for the 1979 year but only partial payment was made in satisfaction thereof. Respondent proceeded to attempt collection through other means and located petitioner's Keogh account to satisfy the remaining \$22,340 liability.

The Keogh account was levied upon in 1981 and the bank trustee holding the account withdrew this sum and remitted it to respondent. At the time of the withdrawal, petitioner had not attained age 59-1/2, nor was he disabled. The court did not impose the section 72(m)(5) tax (the predecessor to section 72(t)) because "the funds were withdrawn pursuant to respondent's levy, an involuntary act, without any active participation by petitioner...." Larotonda, 89 T.C. 287, 292 (1987).

On April 11, 1988, the Service issued Larotonda v. Commissioner, AOD CC-1988-010, an action on decision stating that the Service will not acquiesce in Larotonda. Recent legislation warrants withdrawing this AOD. The statutory provision effectively at issue in Larotonda was modified by the Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat. 685 (1998), enacted on July 22, 1998. Section 3436 of the Act amends section 72(t) to provide that the early distribution tax does not apply to a distribution made on account of a levy under section 6331 on a qualified retirement plan. In response to this legislation, the Service withdraws its AOD in Larotonda.

Immediately before Congress enacted this legislation, the Tax Court ruled in Murillo v. Commissioner, T.C. Memo. 1998-13 that section 72(t) did not apply to an individual retirement account that was forfeited to the government pursuant to a plea agreement in a civil proceeding. The Service issued an AOD in response to that decision. The AOD states that the Service will not assess section 72(t) tax on distributions made on account of levy on qualified retirement plans, and in addition, will not assess section 72(t) tax under the narrow circumstances of Murillo. However, in all other cases involving early distributions, the Service will continue to assess section 72(t) tax unless a statutory exception applies. See, e.g. In re Kochell, 804 F.2d 84 (7th Cir. 1986) (10 percent early distribution tax applied to a withdrawal made by bankruptcy trustee from an IRA under I.R.C. § 408(f)(1)).

Recommendation:

Withdraw the AOD

Reviewers:

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