

Transcript for the Basics of Roth Conversions Retirement Planning Employee Plans  
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Moderator: Ladies and gentlemen, thank you for standing by. Welcome to the Basics of Roth Conversions Retirement Planning Employee Plans Phone Forum.  
As a reminder, today's conference is being recorded. I would now like to turn the conference over to your host, Mr. O'Donnell. Please go ahead, sir.

M. O'Donnell: Hello, everyone. I'm Mark O'Donnell, the Director of Customer Education and Outreach for Employee Plans at the IRS. Thanks for dialing into our phone forum today on the basics of Roth conversations retirement planning. Today we'll be hearing from Greg Nix, IRS Employee Plan's Customer Education and Outreach Area Analyst in Gulf Coast. He represented the Employee Plans Office at the 2010 Nationwide Tax Forum. This Roth topic was one of the presentations he gave at the tax forum.

We'll also be hearing from Kathy Herman, Tax Law Specialist EP Technical Guidance and Quality Assurance. Kathy has worked on various pieces of guidance, including those dealing with rollovers and conversion.

We will email a certificate of completion to everyone who registered for this session and who attends the full session. Enrolled agents and enrolled retirement plan agents are entitled to continuing professional education credit for this session. For other tax professionals, consult with your licensing organization to see if it will provide continuing professional education credits for this session.

Our retirement plans community Web site at [www.irs.gov/ep](http://www.irs.gov/ep) has information regarding Roth's. You can also get there by going to the main IRS Web page and clicking on the retirement plan community tab at the top. Look to the left hand navigation bar; click on types of plans and then select Roth IRAs.

Also you might want to subscribe to one of our free electronic newsletters. The link for newsletters is in the left hand navigation bar. We have two newsletters, the *Retirement News from Employers* is directed at employers sponsoring a retirement plan. The *Employee Plan News* is directed at professionals who practice in the retirement area. Check out our Web page and subscribe to our newsletters.

So without further ado, here are our speakers, Greg Nix and Kathy Herman.

K. Herman: Good afternoon. Today we're going to be talking about the new 2010 Roth conversion rules, as well as other hot retirement plan topics. We all know that life events, such as marriage, death, divorce can affect your retirement plan. We will discuss how losing a job, having a hardship and retirement to name a few of these life events can impact your retirement savings.

G. Nix: Let's start our discussion today with a hot topic, Roth IRA conversion. We'll cover two aspects of Roth conversions, first the rules and then second, some areas that may cause you some headaches you need to be aware of. Even though we know that headaches are part of life, we always like to avoid them, especially when they involve taxes and the IRS.

First the rules, Roth IRAs are not new, but I want to give you a brief overview of what they are and how they work. A Roth IRA is an account or an annuity that's designated as a Roth IRA. Although you cannot deduct contributions to a Roth IRA, qualified distributions from it are tax free. Some reasons for the popularity are that unlike a traditional IRA, you may continue to contribute even after you turn age 70.5. And the original account owners are not subject to required minimum distributions during their lifetime. Some people even use a Roth IRA as in estate planning tools since not only are qualified distributions tax free to you as the original account owner, but also to your beneficiary.

Now there have been some recent changes made to the rules for rollovers to Roth IRAs. Prior to January 1<sup>st</sup> of 2010, rollovers or conversions from a traditional IRA, a SEP IRA, a SIMPLE IRA or from a qualified retirement plan into a Roth IRA were only allowed if your modified adjusted gross income was \$100,000 or less and your filing status was not married, filing separate. So if you met those conditions, conversions to a Roth IRA were taxable during the year of the rollover.

But it's a new day. For Roth conversions only, there are no longer any income or filing status conditions for 2010 and beyond. However, there is a special rule for conversions to a Roth IRA in 2010 only. You report half the taxable portion of your conversion in 2011 and the other half in 2012. Or you may elect out of that treatment and pay all of the tax in 2010. This selection is made on your 2010 tax return and is considered an irrevocable election.

If your client is paying the tax in 2011 and 2012, but they died during 2011, the entire tax bill is due in 2011 unless there's a surviving spouse who acquires the entire interest in the IRA. The surviving spouse may then elect to include income in 2011 and 2012 just as the deceased would have.

Estimated taxes are still required on the conversions and after the 2010 calendar year, we go back to the rule that taxable portions of the conversion must be included in gross income in that conversion year. So let me talk for a minute about recharacterizing and reconversion.

If you made a conversion from a qualified plan or a traditional IRA to a Roth IRA, you're able to change your mind and do a recharacterization. A recharacterization allows you to treat a contribution made to one type of IRA as if it had been made to a different type of IRA. If you recharacterize, the entire amount in the Roth must be recharacterized. You cannot pick and choose assets to move. So for that reason many people convert their IRA into several different Roth IRAs since that would allow you to only recharacterize the Roth IRA accounts that held the losers.

Remember, a recharacterization must be done via a trustee-to-trustee transfer. If you recharacterize by your tax return due date, including extensions of the year for which the contribution conversion was made, you may then elect to treat the contribution as having been made originally to that second IRA instead of the first. And if you do recharacterize the contribution, I'm going to give you three things to keep in mind.

The entire account is recharacterized, including any income or loss. You report the recharacterization on your tax returns for the year during which the original conversion was made. If you recharacterize an amount from a Roth to a traditional IRA, you treat the amount as if it had been originally made to the traditional IRA on the date it was converted to the Roth. Let's say you converted an amount from a traditional IRA to a Roth IRA and then later recharacterize that rollover back to the traditional IRA.

Can you then later convert that amount from the traditional IRA back the Roth IRA? The answer to that is yes, but these rules for reconversions are that you cannot convert and reconvert an amount during the same tax year or if later during the 30 day period following a recharacterization. If you reconvert during either of these periods, it will be considered a failed conversion.

K. Herman: So we know now that any taxpayer who has a regular IRA can convert it to a Roth IRA. But just because a taxpayer can convert doesn't necessarily mean that the taxpayer should convert. Each individual needs to look at their own situation and decide what's best for them. We at the IRS are not in a position to give advice on whether or not to convert. However, we can provide some information on the things that you can advise taxpayers to consider before making such a decision.

As Greg said in discussing the previous slide, Roth IRAs do have advantages. Two of the biggest advantages are that qualified distributions from a Roth IRA are tax free. This is important because future distributions from IRAs could affect the taxpayer's tax bracket. Since a qualified distribution from a Roth IRA is tax free, while a distribution from a traditional IRA is included in income, the conversion could have the effect of keeping the taxpayer's tax bracket lower.

And having a lower tax bracket is important because it could make a difference in whether Social Security benefits are taxable and it also could impact AGI-based tax deductions. The second major benefit of Roth IRA is that Roth IRAs are not subject to

minimum distributions rules, which means that taxpayers will not be required to take out any money during their lifetime.

So what should your client consider before making a conversion from their traditional IRA to a Roth IRA? A major consideration is whether the client can afford to pay the taxes due on the conversion either this year or if they make the conversion in this year and spread over 2011, 2012. As discussed earlier, the tax portion of a conversion is includable in income. Depending on the value of the IRA account, the tax bill could be substantial and if the only way to pay the bill is to use some of the funds out of the converted IRA or to borrow funds, it might not make sense to convert.

Another consideration is the value of the account. If the IRA took a big hit in the market decline, it might make sense to convert it now and pay taxes on that lower value and then enjoy tax free earnings as the value bounces back in the future, hopefully. Another consideration is what a taxpayer's tax bracket will be when they retire. Taxpayers often don't know what their tax bracket will be in the future, but many people have a much higher tax bracket during their working years than they do in retirement.

So they need to decide whether it makes sense to pay taxes now by doing a conversion when the highest tax bracket right now are 35% and without further action by Congress will be even higher next year. No one really knows what the tax rates will be in the future, but it's something that a taxpayer should consider when they decide to convert.

Another thing to consider is whether the client needs the money in retirement or whether they plan to pass the vast majority of it onto their heirs. Since there are no lifetime distributions from Roth, a taxpayer may want to just maximize the amount in the Roth IRA and pass it on to their heirs.

There are potential problems for clients who decide to convert. One thing they should consider is that the conversion limit, the income limits which have now been eliminated are the same as contribution limits to Roth IRAs. The income limits to contribute to a Roth IRA is still in place. In 2010 an individual can make a Roth IRA contribution if the individual's modified adjusted gross income is greater than—cannot make a Roth IRA contribution, I'm sorry, if it's greater than \$177,000 and he's married, filing jointly or a qualifying widower. The limit is \$120,000 for single filers or \$10,000 for filers who are married filing separately.

If a taxpayer contributes to a Roth IRA and has modified adjusted gross income above these limits, there's an excise tax of 6% on the excess contributions, so a taxpayer shouldn't make contributions to an IRA if it's not eligible. Required minimum distributions cannot be converted to a Roth and the first dollars withdrawn in any year are deemed to be required minimum distributions.

So taxpayers who are required to take minimum distributions for a year need to do that before they make a conversion. If they convert required minimum distributions and don't

withdraw them by the tax filing return date, they will also have excess contributions to the Roth IRA, which will be subject to the excise tax of 6%.

There are also rollover rules that need to be considered. An IRA does not have the mandatory income tax withholding, however the taxpayer has to elect out of that withholding. If the taxpayer doesn't elect out, there is a 10% federal income tax withholding and that can affect the conversion. We can do a little example of that.

If your client is 40 years old and wants to convert \$100,000 traditional IRA to a Roth IRA, the client doesn't have any IRAs with after tax contributions, so all the IRAs are pretax rather than doing a direct transfer, they want to take a distribution and roll it into a different financial institution.

However, when they complete the paperwork, they forget to check the box that says they don't want taxes withheld. When the taxpayer gets the check, the check will have 10% withheld. And if the taxpayer discovers this within a 60 day period, they can come up with the extra 10% money and roll it over and then receive a refund on their tax return. If they don't, then that extra 10% that was withheld will be subject to income tax and will also be subject to excise tax for an early distribution.

This becomes even a greater problem if the client only rolls over the 90% that they actually received into the Roth IRA and then they decide to convert it or recharacterize it back to the traditional IRA because they will only be able to recharacterize the 90% that they actually. And they'll still owe the tax on the 10% and won't be able to get that back into their traditional IRA. Conversions when a taxpayer has both deductible and nondeductible contributions can also present a problem. If the taxpayer decides to convert an IRA made up entirely of nondeductible contributions, on the surface that sounds really good, because it can grow tax free and the qualified distributions at a later date will be tax free. But if the taxpayer also has IRAs that are made up of deductible contributions, a pro rata rule applies. This means that the taxable portion of the conversion is determined by using a percentage of all of the IRA accounts.

This we can do another example to explain this. Let's say, a client has two IRAs, one with nondeductible contributions and one with deductible contributions. The nondeductible contribution IRA has a balance of \$10,000 and there are no earnings. The deductible contribution IRA has a total of \$30,000 and that includes taxable earnings. When the taxpayer decides to do a conversion of the IRA that only has nondeductible contributions, \$10,000, you need to determine how much of the conversion will really be taxable. Under the pro rata rule, you divide the total of the taxable amount in all of the IRAs by the total of all of the IRAs.

In this example, the taxable amount in the taxpayer's IRAs total \$30,000. You divide that by the total of all the IRAs, which is the \$40,000, which is nondeductible and the \$30,000, which is deductible for a total of \$40,000; \$30,000 divided by \$40,000 equals 75%. So in this example 75% of the amount converted or \$7,500 is considered taxable, even though the taxpayer thought he was only converting his nondeductible contribution.

You can look at Form 8606 and the instructions and this will explain how to determine the percentage of conversion subject to taxes.

Another thing to consider is that when an amount is converted from a traditional to a Roth IRA, the taxpayer has to complete a new beneficiary form. If the Roth IRA doesn't have a designated beneficiary, then the Roth IRA must be distributed within five years after the account owner's death, which would be different—the designated beneficiary would have a different distribution rule.

This is just a sampling of the area where clients can run into trouble with Roth conversions. Although many articles have been written indicating that a conversion is a great thing, it's good idea for taxpayers to carefully consider whether it is good for them in their situation.

G. Nix: Now we're going to take a look at some loans and hardship distributions. Sometimes like in a case of Roth IRA conversion, you can look at the situation from all angles and decide the best way to proceed. But there's other times that you really have little control over life events and things do get tough for everybody. Although the goal is not to tap into your retirement plan or those accounts until after you retire, the law does recognize that there are times when you may need immediate access to that money.

First there's a few different ways you can do that. One of those is a plan loan. Not every type of retirement plan allows a plan loan. If you have an IRA based plan, such as a SEP, a SIMPLE IRA, a SARSEP or even a traditional and Roth IRA, they are not allowed to have plan loans. Qualified plans such as 401(k) and profit sharing plans are permitted to make participant loans, but only if the plan document allows for it. The plan language or a document that's referenced in the plan must outline this loan program. It will describe the rules, the limits, and all the procedures for borrowing.

Unless the participant loan meets the code requirements, it's going to be subject to income tax to the borrower. Some of these requirements are that the amount of the loan is limited to the lesser of 50% of the employee's vested account balance or \$50,000. A borrower must make payments at least quarterly over no more than five years. There's an exception to this five year rule for loans that are used to purchase a principal residence by that employee.

There may be taxability issues with plan loans, of course. For example, loans that aren't limited to the 50% of an employee's vested account balance or loans that exceed \$50,000 are treated as a distribution to the extent they exceed those limits and they're taxed accordingly. Missed payments may send the entire loan into default. If left uncorrected, the entire loan will become fully taxable to that employee. The law treats a loan as a deemed distribution and it will be included in the borrower's income.

The most common reason we have that a loan becomes taxable is when an employee terminates employment with an outstanding loan balance. In this situation plans will give

that participant some time to pay that money back. But most often these loans are offset by a distribution of that account by that outstanding loan balance. The taxable amount of the distribution is reported on a 1099R and it would include the loan balance because this money was never taxed.

Another way employees may tap into their retirement funds is through a hardship distribution. Only certain types of retirement plans, such as a 401(k), a 403(b) and 457 plans might offer hardship distribution. Plans are not required to offer these hardship distributions. If they do, they must contain specific criteria to be used to determine that the hardship qualifies for the distribution.

Now the regulations for 401(k) plans require that there be an immediate and heavy financial need to meet this hardship. My neighbor's 1967 Camaro has for sale, no matter much I really want that car, it doesn't meet the IRS definition of a hardship. Distribution of elective deferrals is deemed to be for an immediate and heavy financial need if it's for medical expenses, the purchase of a principal resident, tuition and related education expenses, to prevent eviction, funeral expenses and repairing casualty damage to the participant's house.

A distribution may not be considered necessary to satisfy this immediate and heavy financial need if employees have other resources available to meet that need. That includes a spouse and minor children's assets.

Employees may also be able to obtain a hardship distribution for medical, tuition, and funeral related expenses for their grandchild or domestic partner if that individual has been designated as the employee's beneficiary in the plan.

So how much would be available for a hardship? In the case of a hardship distribution of elective contributions, the distribution must be limited to an employee's total elective contributions. The amount of the hardship cannot be greater than what's necessary to satisfy this financial hardship need. That includes any associated costs of taking the distribution. As usual, there's tax issues that are related to hardships. It's not going to be free money. It's going to hurt. Hardship distributions are subject to income tax in the year of distribution and if the employee is under age 59.5, they're also subject to the additional 10% early distribution tax.

However, these distributions are not subject to the mandatory 20% income tax withholding for distribution. Employees may add the amount of the income tax they have to pay because of the hardship distribution to the amount of the distribution request. For example, Joe has an account balance that includes \$50,000 in elected deferrals and has a hardship need of \$26,000. Assuming Joe is in a 25% tax bracket and is also subject to the additional 10% early distribution tax, it would take a distribution of around \$40,000 to satisfy this hardship. And it would be even more if you have to include state and local taxes. So taking a hardship distribution from retirement plans should be used as a true last resort because unlike a plan loan, a hardship distribution is a permanent reduction of an account balance and would never be paid back.

K. Herman: In addition to loans and hardship distributions, another way to access money in your retirement account is to take a distribution. However, there's tax consequences to taking a distribution as well. Let's first talk about IRAs. A taxpayer can withdraw all or some of the funds from their traditional or Roth IRA or any IRA plan like a SEP or SIMPLE at any time. The tax consequences of the withdrawal depend on a number of factors, such as what type of account the individual withdrew the money from and when and why the withdrawal was made.

Typically the amount withdrawn from a traditional IRA that is from deductible contributions and the associated earnings must be included in gross income in the year of the withdrawal. In addition unless the taxpayer is age 59.5 or one of the following exceptions apply, the taxpayer also will owe an additional 10% early distribution tax on the amount withdrawn.

The exceptions to the 10% early distribution tax include if the taxpayer has unreimbursed medical expenses in excess of 7.5% of AGI. The taxpayer is unemployed and the distributions are not more than the cost of medical insurance; the taxpayer is disabled. The taxpayer receives distributions in substantially equal periodic payments over his life or his life expectancy, sort of like an annuity. The distributions aren't more than qualified higher education expenses. The distributions are used to buy, build or rebuild a first home or the distribution is to a qualified reservist, which is a military person.

Keep in mind that the amount still goes into income. It's just that that early distribution tax doesn't apply to it. There's a complete list of the exceptions in Pub 590.

Now I want to make special mention of SIMPLE IRAs because they're a little bit different. Just like other IRAs, an individual can withdraw contributions and earnings from a SIMPLE IRA at any time. The individual will be taxed on the withdrawal in the year it is received. However with SIMPLE IRAs, the additional 10% early distribution tax is increased to 25% if the withdrawal occurs within two years of beginning participation in this SIMPLE. Also, if a person wants to make a rollover or a transfer from a SIMPLE IRA within this first two year period, it can only go to another SIMPLE IRA.

Distributions from Roth IRAs are a little different also. Because they're funded with after tax contributions, individuals don't have to pay income tax on any withdrawals as long as they're qualified distributions. The earnings associated with those withdrawals are not taxed either. If an individual takes a non-qualified distribution from a Roth IRA, they will have to include the earnings in the gross income. The actual distribution is not taxed because it was already an after tax contribution however unless an exception applies the early distribution 10% tax does apply.

A qualified distribution as was mentioned earlier is after five years. It's measured from January 1<sup>st</sup> of the year in which the individual made the contribution to the Roth IRA. And it ends on the last day of the fifth year. In addition to having to wait five years, there



has to be on other event, either be 59.5, be disabled, use it to buy or rebuild a home or on account of death.

Distributions from company retirement plans are also a little different. Plans generally don't give distributions to a participant unless there's a distributable event. That is retirement, death, disability or leaving your job. Most plans will allow participants to take a lump sum distribution. However, whether or not you can depends on the plan provisions regarding distribution.

If an individual takes a lump sum from a plan, any money withdrawn from the plan that the individual hasn't already paid taxes on will be includable in gross income in the year received. The individual may also have to pay the additional 10% early distribution tax unless an exception applies.

Some of these exceptions are the same as with the IRA. There are a few different ones. The list includes being 59.5, being disabled; a distribution in substantially equal periodic payments after you separate from service; a distribution after you separate from service in the year in which you reach age 55; for medical care up to the amount allowable as a medical expense deduction; because of an IRS levy; or the qualified reservist distributions. Publication 560 has a complete list of all of these exceptions.

Generally speaking you can leave your money in a plan if it's greater than \$5,000. If it's less than \$5,000 when you leave the plan can force it out. Usually an individual can roll their tax deferred account to another tax deferred account. And that would be discussed in the next couple of slides.

G. Nix: An alternative to cashing out from a qualified plan is rolling it over. If you leave your old job, you can move the money from your old employer's retirement plan directly into your new employer's retirement plan if that plan allows or into an IRA. There are two ways you can do a rollover from your employer's plan to an IRA. The first is a direct rollover, in which you inform the plan administrator that you want to transfer your retirement plan account into an IRA. Then you give them the name of the institution, where the IRA is located. And then they just roll the money over directly into that IRA.

As an alternative, you can do an indirect rollover commonly called a 60 day rollover. The administrator gives you your account balance minus the 20% income tax withholding. And then you have 60 days to deposit the asset into an IRA or they'll become taxable distributions to you. There are some very limited waivers to the 60 day rollover deadline and they're outlined in publication 590.

You have to apply for a waiver or show that the 60 day deadline wasn't met because of an error that was made by your financial institution and that's what caused this failure to meet the 60 day deadline. That's a lot of paperwork. It can be expensive to get this done. So you really need to be careful about that. I'd definitely recommend the direct rollover into the accounts.

Remember the amounts rolled over are not includable in your gross income and that they'll continue to enjoy tax deferred growth in the new plan or in that IRA.

K. Herman: Now we're going to talk a little bit about beneficiaries. If an individual is named as a beneficiary of someone's retirement plan account, the individual has some decisions to make. Generally plan rules will determine whether a beneficiary can keep the money in the plan or he or she must take a distribution.

Depending on what the terms of the plan provide, the beneficiary may be able to take periodic distributions or they may be required to take a lump sum distribution.

If the beneficiary takes a lump sum distribution, he might be able to roll it over. Rules regarding what the beneficiary can do depend on whether the beneficiary is a surviving spouse or a designated non-spouse beneficiary.

If the beneficiary is able to and decides to keep the money in the plan, future distributions from the inherited account depend on whether the deceased participant was already receiving payments or not. If the deceased participant was already receiving payments from the plan, payments to the beneficiary, either a spouse or a non-spouse, will continue. If the deceased participant had not begun receiving periodic payments from the plan, the beneficiary may be able to set up his own payment schedule if the plan allows this.

The payments from the plan must be made by end of the fifth year or over life expectancy. That means basically if the beneficiary decides to go with the five year option, all payments have to be out by the end of the fifth year. The beneficiary generally has until the December 31<sup>st</sup> of the year following the year the person dies to choose between the five year or the life expectancy option.

The surviving spouse if they choose the life expectancy option may elect to start receiving payments by the end of the year of the participant's death or the end of the year in which the participant would have turned 70.5. The non-spouse beneficiary doesn't have this option. They can only start payments at the end of the year following the participant's death.

If the beneficiary elects to receive a lump sum distribution in certain circumstances, they may be able to roll it over to an IRA. If the beneficiary decides to just keep the lump sum distribution, any previously untaxed money would be included in the beneficiary's gross income. However the 10% early distribution tax would not apply, because the exception that the distribution was on account of death would apply.

Beneficiary may also roll over the inherited amount. Starting in 2010, all plans must offer designated non-spouse beneficiaries the option of doing a direct rollover into an IRA set up to receive such funds. For either a spouse or a non-spouse beneficiary, unless the rollover is into a Roth IRA, the beneficiary would not include the amount in gross income. Instead the beneficiary would include the amount in gross income when the payments are received from the IRA at a later date.

Rules regarding rollover differ, depending on whether the beneficiary is the spouse or the non-spouse designated beneficiary. We'll look at the surviving spouse first. The surviving spouse can roll an inherited plan account to three different places, well, actually three different types of accounts. They can roll it over to an IRA that the spouse elects to treat as his or her own and name him or herself as the account owner.

If the spouse treats the account as his or her own, the spouse's required minimum distribution rules apply, which mean he or she can leave the amounts in the IRA until his or her required beginning date. Any withdrawals from that IRA would be subject to the early distribution tax if no other exception applies. The surviving spouse can also roll the amount into an inherited IRA, either traditional or Roth, and by designating himself or herself as the beneficiary of the IRA.

If the spouse treats the account as inherited, the spouse uses the required minimum distribution rules of the participant as discussed previously, where they have the five year or the life expectancy option and any distributions would not be subject to the early distribution tax because the distributions would be considered on account of death. A surviving spouse can also roll an inherited amount into another qualified plan if the other qualified plan will accept that rollover.

If the beneficiary is a designated non-spouse beneficiary, the options are more limited. That beneficiary can only roll over to an inherited IRA and the participant's required minimum distribution rules apply, as five year life expectancy. The significance of an inherited IRA is that the beneficiary can't make any other contributions or rollovers to or from that account.

The rules for inheriting an IRA from someone are similar to inheriting plan accounts. If a beneficiary inherits a traditional IRA from a person other than his or her spouse, the beneficiary could not treat the inherited IRA as his or her own. It has to be treated as an inherited IRA. Like the original owner, the beneficiary will only include amounts in gross income as he or she received distributions from that IRA. And if a beneficiary inherits an IRA that has after tax contributions in the IRA, the basis stays with the IRA, carries over to the beneficiary.

However, a non-spouse beneficiary cannot combine that basis with any basis of their own. If the spouse treats the IRA as their own, then they can combine the basis with their own basis because they're treating the IRA as their own. When the non-spouse beneficiary takes future distributions from an inherited IRA, they have to keep the basis in that IRA separate from their own basis and complete separate form 8606 for each IRA to determine the taxable and non-taxable portions of the distributions.

G. Nix: So far we've been trying to talk about how to keep money in retirement plans. But eventually the law requires people to start taking required minimum distributions from their retirement plans and from traditional IRAs. You must begin taking these required minimum distributions from your traditional IRAs when you

turn age 70.5. If you participate in an employer sponsored retirement plan, you must begin taking these required minimum distributions from that plan by the later of when you turn 70.5 or retire. If you own more than 5% of the business, however, you need to take the required minimum distributions when you turn 70.5. You don't have that later of date.

The Worker Retiree and Employer Recovery Act of 2008 waived the 2009 required minimum distributions. But this act did not waive any 2010 required minimum distributions that would be due by December 31<sup>st</sup> of 2010 or April 1<sup>st</sup> of 2011 for those people that turn 70.5 during 2010.

A participant who turned 70.5 in 2009 would not have been required to take their first required minimum distribution that's normally due by April 1, 2010. But they would be required to take the 2010 required minimum distribution by December 31, 2010.

Qualified plans will usually calculate the amount of your required minimum distribution. But for IRAs, you may have to calculate the amount of this required distribution yourself. For IRAs, to calculate the amount due by December 31, 2010, you need to take the account balance of the December 31, 2009 and divide that by the distribution period that's found in the life expectancy table that are in publication 590.

If you have a number of IRAs, you can take a required minimum distribution from one or more of these IRAs to meet the requirement. However, if you're in a retirement plan, a required minimum distribution is calculated separately for that plan. A person's account balance is going to be adjusted for any outstanding rollovers and recharacterizations of Roth IRA conversions that aren't in any account at the end of that preceding year. The tables that you're going to use depend on whether you're a beneficiary, single, married, or married with a spouse more than ten years younger than you and the sole beneficiary of your account. Publication 590 has all the details on how to calculate these required minimum distributions from your IRA.

You can always withdraw more, but you must withdraw at least the amount of your required minimum distribution. Otherwise you'll be subject to an excise tax of 50% of the amount that you should have withdrawn. These required minimum distributions are going to be taxed just like any other distribution. You must include any previously untaxed amount in your gross income in that year distributed.

K. Herman: It's no surprise that many people's IRAs and retirement clients have incurred losses in the past few years. In the case of IRA based and other defined contribution plans, employees bear the investment losses. The employer on the other hand makes up the defined benefit plan losses. The defined benefit plan sponsors may need to make substantial contributions to meeting funding requirements. There's an excise tax if minimum funding requirements for defined benefit plans aren't satisfied or if contributions aren't made in a timely manner.

When a traditional IRA has a loss, a taxpayer can deduct it on their income tax return, but only when all the taxpayer's traditional IRAs have been distributed and the total amount distributed is less than the taxpayer's unrecovered basis. Taxpayer's basis in an IRA is the nondeductible or after tax contributions that have been made the IRA.

For example, if the taxpayer's basis is \$10,000 and the loss is \$5,000, then the taxpayer can only deduct \$5,000. If the loss is \$20,000, then the taxpayer can deduct the \$10,000 in basis. For Roth IRAs, a taxpayer can recognize a loss on an income tax return also. But the same situation applies only when all the amounts in all of the taxpayer's Roth IRAs have been distributed and the total distributions are less than the total Roth IRA contributions that have been made. For this purpose taxpayers have to aggregate all of their like IRAs when they're figuring out whether they have losses.

With both traditional and Roth IRA losses, the taxpayer can claim the loss as a miscellaneous itemized deduction subject to the 2% of AGI on Form 1040 Schedule A. Any such losses are added back into taxable income for purposes of calculating the alternate minimum tax.

One area that's kind of been of interest lately are losses due to taxpayers who have invested in Ponzi schemes with their IRA. Many people have losses as a result of these Ponzi schemes and they like to try to deduct it as a theft loss. There's not a deduction as a theft loss for this type of investment loss. This is a theft loss for the plan or the IRA and cannot be treated as a theft loss by an individual account owner. The regular loss rules apply to this situation and the individual can only take a deduction when all of their accounts have been liquidated as discussed previously.

G. Nix: Last year as part of President Obama's Retirement and Savings Initiative, the IRS and Treasury clarified some additional ways that employees can save for retirement. Profit sharing and 401(k) plans can be amended to allow for employees to contribute the dollar equivalent of their unused paid time off, such as vacation and sick leave to the plan, either on an annual basis or when they terminate employment.

Of course, in either of those cases, there's going to be an overall contribution limit. These contributions can't exceed the elective salary deferral limits under 402(g) if the contributions are elected deferrals, or the overall annual additional limits that are under code Section 415(c). Check out our Web page for links to the guidance for employers that they can use for contributions in lieu of leave.

We've been receiving many questions on Notice 2009-68. That includes the 402(f) notice. This 402(f) notice provides participants with the timely written explanation that describes the rollover rules, tax consequences of distributions, etc. There seems to be a lot of confusion out there, so we're planning on releasing information very soon to make it a little bit clearer, so stay tuned on that.

K. Herman: Also, Greg, a new law was just passed and signed this week called the Small Job Business Act. This law provides an additional way to do a conversion. It allows conversion of 401(k) contributions within a plan to a Roth account also within the same plan. This would allow people to convert their money without having to move it into an IRA.

G. Nix: Oh, great. Well, we actually have an article in both of our newsletters that came out today that discusses that. That will segue right into our next little discussion here. We have two electronic newsletters that we'll talk a little bit in detail in the next slide. But right now I want to highlight a recurring article that we feature in the newsletter. It's called "We're Glad You Asked." It features current hot topics, questions that we're seeing. It provides answers and resources to those questions. It's a good resource to see what's new and to keep up with all the current information that's out there.

K. Herman: As Mark and Greg mentioned, we have developed many tools to assist you and your clients with retirement plans, whether your questions are how do I choose a retirement plan, how much money can I contribute to my retirement plan or this plan isn't working for me anymore, how do I terminate it.

Information is provided on the Web site. You can visit the Web site at [www.irs.gov/ep](http://www.irs.gov/ep) or you can find the retirement plan's community tab on the main [www.irs.gov](http://www.irs.gov) page. You'll find information for the benefits practitioner, plan participants and employees and plan sponsors and employees on that page. The pages contain all of the retirement plan information that you come to expect from the employee plans.

Be sure to check out our new plan participant Web page that contains a tremendous amount of information in plain language to answer plan participant questions about their retirement plans. The information is organized by major life events, so that they can get information on what they need to do when they start a new job, get married, have children or when they retire.

There are two different ways that you can discuss questions with retirement plan specialists. You can email your questions to [retirementplanquestions@irs.gov](mailto:retirementplanquestions@irs.gov) or you can call the customer account service toll free line at 877-829-5500. Our specialists respond to email questions by telephone, so remember to include your telephone number when you call.

We also have two free quarterly electronic newsletter you can subscribe to. The first is the *Employee Plan News* that's geared towards the practitioner community. It's more technical and involved than our newsletter that is geared toward plan sponsors. *Retirement News for Employers* being a Web based product, both of these newsletters make excellent reference guides as we fill them with embedded links to source materials.

You can easily subscribe to both of these newsletters. Just click on newsletters in the left navigation pane on our Web page and then *Employee Plans News* or *Retirement News of*

*Employers* and then click subscribe, which is down towards the bottom of the page and provide us with your email address. That's all it takes. Whenever we issue an edition, you'll receive a message in your email box with a link to it.

G. Nix: When we say that we'd like you to contact us with your questions and problems, etc., I just want to let you know we try to listen as much as we can to your concerns. Earlier in one of the earlier slides where we talked about the 402F notice, I think we've been listening to your concerns and trying to get out some more information on these, get some more guidance out. That communication is a big part of this because if there are areas you're having problems in, just let us know.

This last slide is where I tell to join us for our simple presentation, but that was a few days ago, so you can't join us on that phone forum. So I guess that concludes our presentation for today.

M. O'Donnell: Yes, this concludes our phone forum on the basics of Roth conversions retirement planning. Thanks, everyone, for listening in. Please look out for future phone forums on our Web site and in our newsletters. Good day, everyone.

Moderator: That does conclude our conference for today. Thank you for your participation and for using AT&T Teleconference Service. You may now disconnect.