DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

200214034

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

JAN 8 2002

Uniform Issue List: 72.22-01; 72.22-02

T:EP:RA:T4

Legend:

Dear :

This letter is in response to a request dated October 23, 2001, made by an authorized representative of both you and your spouse, for a ruling under 72(t)(1) and 72(t)(2) of the Internal Revenue Code.

The following facts and representations have been submitted on your behalf:

Taxpayer A, whose date of birth was Date 1, is married to Taxpayer B, whose date of birth was Date 2. Neither Taxpayer A nor Taxpayer B has attained age 59 ½. Taxpayers A and B are currently residents of State C. State C is a community property law jurisdiction.

By December 31, 2001, Taxpayers A and B will file a petition for divorce in Court D. A judgment of divorce will be entered by December 31, 2002, and will include a division of property. The judgment entered by Court D will be a "divorce or separation instrument" as described in subparagraph (A) of section 71(b)(2) of the Code. Among the marital

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assets is an Individual Retirement Arrangement, IRA X, owned by Taxpayer A.

In 1998, Taxpayer A began to receive a stream of payments from IRA X which your authorized representative asserts was intended to comply with the requirements of Code section 72(t)(2)(A)(iv). Taxpayer A has received approximately $85,200.00 annually from IRA X since 1998, by way of $7100.00 in monthly payments. Taxpayer A's IRA X distributions were based on the single life expectancy of Taxpayer A using an interest rate which your authorized representative asserts was reasonable as of the date on which IRA X distributions commenced. Taxpayer A will continue to receive such payments in 2002.

As part of the judgment of divorce, IRA X will be divided. It has been represented by your authorized representative that approximately ½ of IRA X will be transferred directly to a new IRA (IRA 2) to be set up and maintained in the name of Taxpayer B. After, and as a result of the above-referenced transfer, Taxpayer A's distribution will be reduced by a percentage equal to a percentage of the IRA awarded to Taxpayer B beginning with calendar year 2003, the year following the year of divorce.

Based on the above facts and representations, you, through your authorized representative, request the following rulings:

1. The division of IRA X and subsequent transfer of ½ of IRA X to an IRA in the name of Taxpayer B pursuant to a decree of divorce will be considered a nontaxable transfer pursuant to 408(d)(6) of the Code.

2. The reduction in the annual distribution from IRA X to Taxpayer A beginning in calendar year 2003, prior to Taxpayer A attaining age 59 ½, will not constitute a subsequent modification in his series of periodic payments, as the term "subsequent modification" is used in section 72(t)(4) of the Code, and will not result in the imposition upon Taxpayer A of the 10 percent additional income tax imposed by section 72(t)(1) of the Code pursuant to section 72(t)(4)(A) of the Code.

3. Taxpayer A may change the method of distribution, and the amount thereof, from his IRA X at any time after Date 3 without imposition on him of the 10 percent additional income tax imposed by 72(t)(1) of the Code which is imposed on subsequent modifications on periodic payments series by section 72(t)(4)(A) of the Code.

Section 408(a) of the Code provides, in pertinent part, that for purposes of section 408, the term "individual retirement account" means a trust created or organized in the United States for the exclusive benefit of an individual or his beneficiaries, but only if the written governing instrument creating the trust meets certain requirements specified under section 408.

Section 408(d) of the Code establishes the general requirements for the tax treatment of

distributions from IRAs while section 72(t) of the Code sets forth the rules regarding the 10 percent additional tax on early distributions from IRAs.

Section 408(d)(1) of the Code states that, except as otherwise provided in this subsection, any amount paid or distributed out of an IRA shall be included in gross income by the payee or distributee, as the case may be, in the manner provided under section 72 of the Code.

Section 408(d)(6) of the Code states that the transfer of an individual's interest in an IRA to his or her spouse or former spouse under a divorce or separation instrument described in subparagraph (A) of section 71(b)(2) is not to be considered a taxable transfer made by such individual notwithstanding any other provision of this subtitle, and such interest at the time of the transfer is to be treated as an IRA of such spouse, and not of such individual. Thereafter such IRA for purposes of this subtitle is to be treated as maintained for the benefit of such spouse.

Section 71(b)(2) of the Code defines the term "divorce or separation instrument" as: (A) a decree of divorce or separate maintenance or a written instrument incident to such a decree, (B) a written separation agreement, or (C) a decree (not described in subparagraph (A)) requiring a spouse to make payments for the support or maintenance of the other spouse.

Section 1.408-4(g)(1) of the Income Tax Regulations states that the transfer of an individual's interest, in whole or in part, in an IRA to his or her former spouse under a valid divorce decree or a written instrument incident to such divorce shall not be considered to be a distribution from an IRA to such individual or the former spouse; nor shall it be considered a taxable transfer by such individual to his former spouse notwithstanding any other provision of Subtitle A of the Code.

Section 1.408-4(g)(2) of the Regulations provides that the interest described in this paragraph (g) which is transferred to the former spouse shall be treated as an IRA of such former spouse.

With respect to your first ruling request, section 408(d)(6) of the Code specifies that IRA transfers incident to a divorce are not taxable at the time of transfer. The judgment entered by Court D is a decree of divorce under section 71(b)(2) of the Code. Therefore, we conclude that the division of IRA X and subsequent transfer of ½ of IRA X to an IRA in the name of Taxpayer B pursuant to a decree of divorce will be considered a nontaxable transfer pursuant to 408(d)(6) of the Code.

Section 72(t)(1) of the Code provides that if any taxpayer receives any amount from a qualified retirement plan (including an IRA) as defined in section 4974(c) of the Code, the taxpayer's tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 10 percent of the portion of such

amount which is includible in gross income.

Section 72(t)(2) of the Code lists certain distributions from qualified retirement plans which are not subject to the section 72(t)(1) tax, including a distribution described in section 72(t)(2)(A)(iv) as: part of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the employee or joint lives (or joint life expectancies) of such employee and his designated beneficiary.

Section 72(t)(4)(A) provides that if paragraph (1) of section 72(t) does not apply to a distribution by reason of paragraph (2)(A)(iv) of section 72(t), and the series of payments under such paragraph are substantially modified (other than by reason of death or disability) – (i) before the close of the 5-year period beginning with the date of the first payment and after the employee attains age 59 ½, or (ii) before the employee attains age 59 ½, the taxpayer's tax for the first taxable year in which such modification occurs shall be increased by an amount, determined under regulations, equal to the tax which (but for paragraph (2)(A)(iv)) would have been imposed, plus interest for the deferral period.

Code section 72(t)(4)(B) defines the term "deferral period" as the period beginning with the taxable year in which (without regard to paragraph (2)(A)(iv) of section 72(t)) the distribution would have been includible in gross income and ending with the taxable year in which the modification described in subparagraph (A) of section 72(t)(4) occurs.

With respect to your second ruling request, Taxpayer A currently owns IRA X from which he has been receiving distributions since calendar year 1998 that have been calculated to comply with the requirements of section 72(t)(2)(A)(iv) of the Code. Pursuant to a property settlement that will constitute part of a divorce decree, Taxpayer A will have approximately ½ of his IRA X transferred to IRA 2, an IRA set up and maintained in the name of Taxpayer B. Taxpayer A will have no interest in Taxpayer B's IRA 2.

Taxpayer A's calendar year 1998 through calendar year 2001 IRA X distributions have been based on said IRA X's pre-divorce division balance. In calendar year 2002, Taxpayer A's IRA X distributions will be based on said IRA X's pre-divorce division balance. This balance will decline by approximately ½ because of the divorce of Taxpayers A and B. Upon careful consideration of these facts, the Service believes that compliance with section 72(t)(2)(A)(iv) for calendar years beginning with 2003, the calendar year following the calendar year of the divorce, will continue if Taxpayer A reduces his annual IRA X distributions in proportion to his new balance. Thus, with respect to your second ruling request, we conclude that the reduction in the annual distribution from IRA X to Taxpayer A beginning in calendar year 2003, prior to Taxpayer A attaining age 59 ½, will not constitute a subsequent modification in his series of periodic payments, as the term "subsequent modification" is used in section 72(t)(4) of the Code, and will not result in the imposition upon Taxpayer A of the 10

percent additional income tax imposed by section 72(t)(1) of the Code pursuant to section 72(t)(4)(A) of the Code.

Taxpayer A will attain age 59 ½ on Date 3. In calendar year 1998, Taxpayer A began receiving distributions from IRA X, pursuant to section 72(t)(2)(A)(iv) of the Code. Thus, by calendar year 2003, five years will have elapsed since Taxpayer A received his first distribution. Date 3 is subsequent to calendar year 2003.

With respect to your third ruling request, it is assumed that the series of payments from IRA X, pursuant to section 72(t)(2)(A)(iv) of the Code, will not be subsequently modified, within the meaning of section 72(t)(4)(A) of the Code, prior to Date 3. As set forth above, the reduction in the amount of such payments from IRA X to Taxpayer A as a result of the reduction in the balance of IRA X pursuant to the divorce decree does not constitute a subsequent modification within the meaning of section 72(t)(4)(A) of the Code. Thus, we conclude that Taxpayer A may change the method of distribution, and the amount thereof, from his IRA X at any time after Date 3 without imposition on him of the 10 percent additional income tax imposed by 72(t)(1) of the Code which is imposed on subsequent modifications on periodic payments series by section 72(t)(4)(A) of the Code.

This ruling assumes that IRA X and IRA 2 either have met or will meet the requirements of section 408 of the Code at all times relevant thereto and that there will be no substantive changes in the transactions as herein described.

This ruling letter is directed only to the taxpayer who requested it. Code section 6110(k) provides that it may not be used or cited by others as precedent.

A copy of this ruling letter is being sent to your authorized representative pursuant to a power of attorney on file in this office.

If you wish to inquire about this ruling, please contact , at . Please address all correspondence to T:EP:RA:T4.

Sincerely yours,

Alan C. Pipkin
Manager, Technical Group 4
Employee Plans, TE/GE Division

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