

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

Significant Index Number: 401-06-00

199903051

Person to Contact:

Telephone Number:

Refer Reply to:

OP:E:EP:T:1, Room 6214

Date:

OCT 28 1998

Legend:

Taxpayer A =
Taxpayer B =
Taxpayer C =
Taxpayer D =
Taxpayer
Trust D =
SEP IRA X =

State Y =

Dear

This letter is in response to a ruling request dated June 26, 1998, submitted by your authorized representative, concerning the division and distribution of an Individual Retirement Arrangement ("IRA").

The facts on which the ruling requests are based are as follows:

On April 12, 1985, Taxpayer A established SEP IRA X and designated his two sons and a trust for his daughter (Taxpayers B, C, and Taxpayer Trust D) as his designated beneficiaries. The Taxpayer attained age 70 on April 20, 1996, and, thus, had not reached his required beginning date when he died on February 3, 1997. In years 1993 through 1996, Taxpayer A received distributions from SEP IRA X totalling \$12,829, 14,030, \$16,000, and \$25,000 respectively. At the time of his death, SEP IRA X had a balance of approximately \$414,138.

Taxpayer A decided that SEP IRA X be divided equally, one-third to Taxpayer B (born April 30, 1954), one-third to Taxpayer C (born July 10, 1955) and one-third to Taxpayer Trust D, a trust for Taxpayer A's daughter (born July 3, 1956) as the designated beneficiaries of SEP IRA X. In addition, Taxpayer A appointed Taxpayers B and C as co-trustees of Taxpayer Trust D, continuing for the life of the daughter and then for the daughter's descendants with distributions to such descendants at age 30 only after the death of Taxpayer D. No one has the power to change the designated beneficiaries after Taxpayer A's death.

Taxpayer Trust D is valid in State Y. Taxpayer A's will provides the purpose of the trust is to provide for the health, support, and maintenance of his daughter during her lifetime. The entire principal may be distributed to the daughter if required for trust purposes. The daughter has several children. There is no beneficiary of Taxpayer Trust D older than Taxpayer A's daughter. Taxpayer Trust D became irrevocable on the date of Taxpayer A's death. The taxpayer represents that a copy of the trust instrument was provided to the sponsor of SEP IRA X before Taxpayer A's death and again on or about September 28, 1998.

In order to accommodate the long-term financial goals of Taxpayers B, C, and D, it is proposed that SEP IRA X be equally divided into three separate IRA accounts. Required minimum distributions to Taxpayers B, C, and Taxpayer Trust D will be made from the subaccount for him or it, but with distributions to be made from all three subaccounts based upon the life expectancy of Taxpayer B, the oldest, and with each distribution from each subaccount to be based upon only the value of that subaccount. It is possible that a beneficiary may withdraw more than the minimum amount at any time.

The business reason for the transaction is to permit the orderly administration of the Taxpayer Trust D, and to allow Taxpayers B and C to properly file their tax returns, and to allow a SEP IRA X payout as provided by the Internal Revenue Code and regulations.

An initial distribution of SEP IRA X based upon the life expectancy of the oldest designated beneficiary, Taxpayer B, will be made prior to December 31, 1998, will be paid equally to the three taxpayers, and will be reported on Form 1040 for each of the two individual beneficiaries and on Form 1041 for the trust for 1998.

Based on the foregoing facts and representations, you request the following rulings:

1) That the creation of three equal subaccounts at the direction of Taxpayers B, C, and Taxpayer Trust D, effective as of Taxpayer A's date of death, will not effect the tax-deferred status of SEP IRA X and will not be treated as a taxable distribution to Taxpayers B, C, and Taxpayer Trust D.

2) That minimum distributions from each and every of the three separate subaccounts based upon the life expectancy of the designated beneficiary of the IRA having the shortest life expectancy, Taxpayer B who is the oldest, and based upon only the value of the separate subaccount for each particular beneficiary as to distributions to that beneficiary will satisfy the minimum distribution requirements of section 408(a)(6) of the Internal Revenue Code ("Code") with such distributions beginning no later than December 31, 1998.

3) That the beneficiary of the Taxpayer Trust D is identifiable from the trust instrument within the meaning of sections 1.401(a)(9)-1D-5.Q.&A.(a)(3) and 1.401(a)(9)-1D-2.Q.&A.(a)(1) of the proposed Income Tax Regulations.

4) That Taxpayers B and C and the daughter of the deceased who is the beneficiary of Taxpayer Trust D are beneficiaries of SEP IRA X for purposes of determining the distribution period under Code section 401(a)(9)(B)(iii) and such distribution period is based upon the life expectancy of the oldest, i.e. the designated beneficiary as herein ruled.

5) That the initial beneficiary of the Taxpayer Trust D and upon her death her descendants are treated as beneficiaries of the decedent and the distribution period shall be determined under Code section 401(a)(9)(B)(iii), based upon the life expectancy of the designated beneficiary of SEP IRA X having the shortest life expectancy, Taxpayer B, who is the oldest, thus, the designated beneficiary.

6) That sporadic distributions to the deceased participant while living before the required beginning date are irrelevant to the required distributions.

Code section 402(h)(3) provides that distributions from a plan such as SEP IRA X are subject to the rules for IRA distributions contained in Code section 408(d). Code section 408(d)(1) provides, in general, that any amount paid or distributed from an IRA shall be includible in gross income by the payee or distributee, as the case may be, in the manner provided under Code section 72.

Code section 408(d)(3)(A)(i) provides, in part, that section 408(d)(1) does not apply to any amount paid or distributed out of an IRA to the individual for whose benefit the account is maintained if the entire amount is paid into an IRA for the benefit of such individual not later than 60 days after the date on which that individual received the distribution.

Code section 408(d)(3)(B) provides that section 408(d)(3)(A) does not apply to any transfer described in section 408(d)(3)(A)(i) if at any time during the one-year period ending on the day of such receipt such individual received any other amount described in such subparagraph from an IRA which was not includible in his/her gross income because of the application of section 408(d)(3)(A).

Code section 408(d)(3)(E) provides, generally, that section 408(d)(3) shall not apply to any amount to the extent such amount is required to be distributed under either subsection (a)(6) or (b)(3).

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Section 408(d)(3)(C)(i) of the Code provides, in part, that in the case of an inherited IRA, section 408(d)(3) shall not apply to any amount received by an individual from such account (and no amount transferred from such account shall be excluded from income by reason of such transfer), and such inherited account shall not be treated as an IRA for purposes of determining whether any other amount is a rollover contribution.

Code section 408(d)(3)(C)(ii) states that an IRA shall be treated as an inherited IRA if the individual for whose benefit the IRA is maintained acquired the IRA by reason of the death of another individual and such individual was not the surviving spouse of such other individual.

Revenue Ruling 78-406, 1978-2 C.B. 157, provides that the direct transfer of funds from one IRA trustee to another IRA trustee does not result in such funds being paid or distributed to the participant, and it is not a rollover contribution. The Revenue Ruling states that this conclusion would apply whether the bank trustee initiates or the IRA participant directs the transfer of funds.

Therefore with respect to ruling requests #'s 1 and 2, we conclude the mere segregation into subaccounts of the interest of multiple beneficiaries to SEP IRA X by the trustee/custodian of such IRA, at the request of the beneficiaries, does not affect the character or qualifications of the trustee or of SEP IRA X. In addition, the act of segregation of multiple interests in SEP IRA X does not affect its tax-deferred status and will not be treated as a taxable distribution to Taxpayer's B, C, or Taxpayer Trust D. In the present case, a direct trustee to trustee transfer of SEP IRA X or a continuation of SEP IRA X in subaccounts at the same financial institution as opposed to a rollover, is proposed and, thus, although SEP IRA X meets the description of an inherited IRA, there is no prohibition against a non-spousal beneficiary having the IRA moved from one IRA in which Taxpayer's B, C, and Taxpayer Trust D participate to three subaccounts with the same trustee (or custodian) with each subaccount to adopt a

different investment plan and with distributions to be made from each subaccount based upon the life expectancy of Taxpayer B, but with the amount paid to each beneficiary based upon the value of only his/her account.

Code section 408(a)(6) states that under regulations prescribed by the Secretary, rules similar to the rules of section 401(a)(9) and the incidental death benefit requirements of section 401(a) shall apply to the distribution of the entire interest of an individual for whose benefit the IRA is maintained. Code section 401(a)(9)(A)(ii) provides that a trust shall not constitute a qualified trust under that subsection unless the plan provides that the entire interest of each employee will be distributed, beginning not later than the required beginning date, in accordance with regulations, over the life of such employee or over the lives of such employee and a designated beneficiary (or over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and a designated beneficiary).

Code section 401(a)(9)(B)(iii) provides an exception to the five-year rule for certain amounts payable over the life of a beneficiary if: 1) any portion of the employee's interest is payable to (or for the benefit of) a designated beneficiary; 2) such portion will be distributed (in accordance with regulations) over the life of such designated beneficiary (or over a period not extending beyond the life expectancy of such beneficiary); and 3) such distributions begin not later than one year after the date of the employee's death.

Proposed regulation 1.401(a)(9)-1C-3.Q.&A.(a) provides as to a non-spouse beneficiary that in order to satisfy the rule in Code section 401(a)(B)(iii) (the exception to the five year rule for non-spouse beneficiaries), if the designated beneficiary is not the employee's surviving spouse, distributions must commence on or before December 31, of the calendar year immediately following the calendar year in which the employee died.

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Proposed regulations 1.401(a)(9)-1E-5.Q.&A.(a) and 1.401(a)(9)-1F-1.Q.&A.(d) provide that if more than one individual is designated as a beneficiary with respect to an employee as of the employee's date of death, the designated beneficiary with the shortest life expectancy will be the designated beneficiary for purposes of determining the distribution period.

With regard to ruling requests three, four, and five, Code Section 401(a)(9)(E) provides for the purposes of section 401(a)(9), the term designated beneficiary means any individual designated as a beneficiary by the employee. Proposed regulations 1.401(a)(9)-1D-5.Q.&A.(a) and 1.401(a)(9)-1D-6.Q.&A.(a) provide that in the case in which a trust is named as a beneficiary of an employee, all beneficiaries of the trust with respect to the trust's interest in the employee's benefits are treated as having been designated as beneficiaries of the employee under the plan for purposes of determining the distribution period under section 401(a)(9)(B)(iii) if, as of the employee's date of death on which the trust is named as a beneficiary of the employee, or the employee's required beginning date, and as of all subsequent periods during which the trust is named as a beneficiary, the following requirements are met: (1) the trust is a valid trust under state law, or would be but for the fact that there is no corpus; (2) the trust is irrevocable; (3) the beneficiaries of the trust are beneficiaries with respect to the trust interest in the employee's benefit are identifiable from the trust instrument within the meaning of proposed regulation 1.401(a)(9)-1D-2.Q.&A.(a)(1); and, (4) a copy of the trust instrument is provided by the plan. The members of a class of beneficiaries capable of expansion or contraction will be treated as being identifiable if it is possible at the applicable time to identify the class member with the shortest life expectancy.

Taxpayer Trust D has been ruled to be a valid trust by a Superior Court in State Y. The trust became irrevocable on the date of Taxpayer A's death which was before his required beginning date. All the beneficiaries of Taxpayer Trust D are identifiable from the trust instrument within

the meaning of proposed regulation 1.401(a)(9)-1D-2.Q.&A.(a)(1) because during the life of Taxpayer D, she is the only beneficiary of Taxpayer Trust D. After her death, the beneficiaries of Taxpayer Trust D are her then surviving descendants until they attain the age specified in the Trust at which time final distribution will be made. The taxpayer represents that a copy of the trust instrument was provided to the sponsor of SEP IRA X before Taxpayer A's death and again on or about September 28, 1998, within nine months of the date of death.

Therefore, with respect to ruling requests #'s 3, 4, and 5, we conclude that the beneficiaries of the Taxpayer Trust D and her descendants are identifiable from the trust instrument within the meaning of sections 1.401(a)(9)-1D-5.Q.&A.(a)(3) and 1.401(a)(9)-1D-2.Q.&A.(a)(1) of the proposed Income Tax Regulations. Taxpayers B and C and the daughter (Taxpayer D) of the deceased who is the beneficiary of Taxpayer Trust D are designated beneficiaries of SEP IRA X within the meaning of proposed regulation 1.401(a)(9)-1D-2.Q.&A.(a)(1) for purposes of determining the distribution period under section 401(a)(9) and such distribution period is based upon the life expectancy of the oldest designated beneficiary as herein ruled. Finally, we conclude that Taxpayer Trust D's descendants are treated as designated beneficiaries and the distribution period shall be determined under Code section 401(a)(9)(B)(iii), based upon the life expectancy of the designated beneficiary of SEP IRA X having the shortest life expectancy, Taxpayer B who is the oldest designated beneficiary.

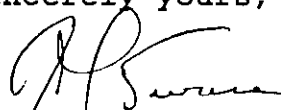
Proposed regulation 1.401(a)(9)-1B-5.Q.&A.(a) provides that except as provided for annuities, distributions are treated as having begun to the employee in accordance with Code section 401(a)(9)(A)(ii) on the employee's required beginning date, even though payments may actually have been made before that date. Therefore, with respect to ruling requests # 6, we conclude that sporadic distributions to the deceased participant while living before the required beginning date are irrelevant to the required distributions.

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These rulings are contingent on the valid status of SEP IRA X at the time the subaccounts were created, and that the minimum distribution requirements of Code section 401(a)(9)(B)(iii) with respect to SEP IRA X and its subaccounts are satisfied at all times.

A copy of this letter has been sent to your authorized representative in accordance with the power of attorney on file in this office.

Sincerely yours,



John Swieca,
Chief, Employee Plans
Technical Branch 1

Enclosures:

Deleted copy of letter
Notice of Intention to Disclose

cc: