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EMPLOYEE BENEFITS PRACTICE GROUP

ALERT

THE WORKER, RETIREE, AND EMPLOYER RECOVERY ACT OF 2008 WAIVES REQUIRED MINIMUM DISTRIBUTIONS FOR 2009

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Recent declines in the financial markets have had a major impact on those required to receive required minimum distributions (RMDs) from qualified retirement plans and IRAs. Because of the way in which RMDs are calculated (based on the previous year's closing value), current distributions may reflect a disproportionately large percentage of the remaining account balances. This affects not only retirees but also beneficiaries who must take minimum distributions from the accounts they inherited.

The Worker, Retiree, and Employer Recovery Act of 2008 (the Act), which was passed by Congress and is ready for the President's signature, is expected to provide some relief. Specifically, for calendar year 2009 only, plan participants and IRA owners, along with their beneficiaries, will be relieved of their obligation to take otherwise required minimum distributions. Unfortunately, the Act does not help taxpayers with 2008 RMDs. Additionally, it does not change the way in which an RMD is calculated, such as providing interim valuation dates.

BACKGROUND

Employer-sponsored defined contribution retirement plans, IRAs, and individual retirement annuities are subject to the RMD rules. Generally, RMDs must begin by April 1 following the later of the calendar year in which the individual reaches age 70-1/2 or retires. (The required beginning date for five-percent owners from qualified retirement plans is April 1 following the year in which the individual reaches 70-1/2.) Typically, the RMD for each year is determined by dividing the account balance as of the end of the prior year by a distribution period prescribed by uniform tables in IRS regulations.

PENALTIES

Failure to take an RMD triggers a 50 percent excise tax, payable by the plan participant or IRA owner or, if deceased, the beneficiary. In some cases, the tax may be waived by the IRS if the distribution was missed because of reasonable error and if reasonable steps are taken to remedy the violation.

THE WORKER, RETIREE, AND EMPLOYER RECOVERY ACT OF 2008

Under the Act, no RMD is required for calendar year 2009 from individual retirement accounts/annuities or defined contribution plans. Thus, any minimum distribution that otherwise would have been required for 2009 need not be made. The next RMD will be for calendar year 2010.

The Committee Report for the Act makes it clear that the new relief applies both to otherwise-required lifetime distributions to employees and IRA owners and to after-death distributions to beneficiaries. However, for purposes of applying the RMD rules after 2009, the required beginning date is determined without regard to the temporary waiver rule. The hope is that those taxpayers whose retirement fund investment values have deteriorated substantially during 2008 and who can afford to wait, can defer their withdrawals and allow their investments time to recover.

The Committee Report specifically says that the relief provision will not help a taxpayer who attained age 70-1/2 in 2008 but chose to delay his or her first RMD (for 2008) until April 1, 2009. That individual still must take that first (2008) RMD by April 1, 2009; however, he or she will not have to take the otherwise-required RMD for 2009.

EXAMPLE

IRA owner John Smith attains age 70-1/2 in 2009, which means his required beginning date is April 1, 2010. Under pre-Act law, the first year for which Mr. Smith would have to take an RMD from his IRA would be 2009; that first distribution could be taken in 2009 or delayed until April 1, 2010. Normally, if Mr. Smith had delayed until April 1, 2010, he would have been required to take two distributions that year (one for 2009 and one for 2010). Under the Act, no RMD is required for 2009. Therefore, Mr. Smith need only take one distribution in 2010, based on the December 31, 2009, value.

CONCLUSION

Although the suspension of RMDs for 2009 may mean little to taxpayers who must make regular withdrawals from their retirement plan accounts and IRAs in order to get by each month, the Act signifies some much welcomed relief for taxpayers in light of the downturn in the economy.

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