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SEP 07 2016

Honorable Ron Wyden
United States Senate
SD-221
Washington, D.C. 20510

Dear Senator Wyden:

This letter is in response to your request for a technical explanation of your discussion draft OTT16321, the "Retirement Improvements and Savings Enhancements Act of 2016," to amend the Internal Revenue Code to encourage retirement savings, to reform the treatment of Roth IRAs, and for other purposes, The enclosed document, prepared by the staff of the Joint Committee on Taxation, provides such technical explanation.

I hope this information is helpful to you. If we can be of further assistance in this matter, please let me know.

Sincerely,

Thomas A. Barthold

Thomas A. Barthold

Enclosure

cc: Tiffany Smith
Kara Getz

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THE RETIREMENT IMPROVEMENTS AND SAVINGS ENHANCEMENTS ACT OF 2016[1]

TITLE I – ENCOURAGEMENT OF RETIREMENT SAVINGS

A. Matching Payments for Elective Deferral and IRA Contributions by Certain Individuals

Present Law

Present law provides a nonrefundable tax credit for eligible taxpayers for qualified retirement savings contributions, referred to as the saver's credit.[2] The maximum annual contribution eligible for the credit is $2,000 per individual. The credit rate depends on the adjusted gross income ("AGI") of the taxpayer. For this purpose, AGI is determined without regard to certain excludable foreign-source earned income and certain U.S. possession income.

For taxable years beginning in 2016, married taxpayers filing joint returns with AGI of $61,500 or less, taxpayers filing head of household returns with AGI of $46,125 or less, and all other taxpayers filing returns with AGI of $30,750 or less are eligible for the credit. As the taxpayer's AGI increases, the credit rate available to the taxpayer is reduced, until, at certain AGI levels, the credit is unavailable. The credit rates based on AGI for taxable years beginning in 2016 are provided in the table below. The AGI levels used for the determination of the available credit rate are indexed for inflation.

Table 1.–Credit Rates for Saver's Credit

Joint Filers	Heads of Households	All Other Filers	Credit Rate
$0-$37,000	$0-$27,750	$0-$18,500	50 percent
$37,001-$40,000	$27,751-$30,000	$18,501-$20,000	20 percent

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[1] This document provides a description of the Retirement Improvements and Savings Enhancements Act of 2016, a discussion draft to amend the Internal Revenue Code to encourage retirement savings, to reform the treatment of Roth IRAs, and for other purposes, released September 8, 2016 (the "discussion draft").

[2] Sec. 25B. Unless otherwise states, all section references are to the Internal Revenue Code of 1986 ('the Code"), as amended.

Joint Filers	Heads of Households	All Other Filers	Credit Rate
$40,001-$61,500	$30,000-$46,125	$20,001-$30,750	10 percent
Over $61,500	Over $46,125	Over $30,750	0 percent

The saver's credit is in addition to any deduction or exclusion that would otherwise apply with respect to the contribution. The credit offsets alternative minimum tax liability as well as regular tax liability. The credit is available to individuals who are 18 years old or older, other than individuals who are full-time students or claimed as a dependent on another taxpayer's return.

Qualified retirement savings contributions consist of (1) elective deferrals to a section 401(k) plan, a section 403(b) plan, a governmental section 457(b) plan, a SIMPLE plan, or a SARSEP;[3] (2) contributions to a traditional or Roth individual retirement arrangement ("IRA");[4] and (3) voluntary after-tax employee contributions to a qualified retirement plan or section 403(b) plan. Under the rules governing these arrangements, an individual's contribution to the arrangement generally cannot exceed the lesser of an annual dollar amount (for example, in 2016, $5,500 in the case of an IRA of an individual under age 50) or the individual's compensation that is includible in income. In the case of IRA contributions of a married couple, the combined includible compensation of both spouses may be taken into account.

The amount of any contribution eligible for the credit is reduced by distributions received by the taxpayer (or by the taxpayer's spouse if the taxpayer files a joint return with the spouse) from any retirement plan to which eligible contributions can be made during the taxable year for which the credit is claimed, during the two taxable years prior to the year for which the credit is claimed, and during the period after the end of the taxable year for which the credit is claimed and prior to the due date (including extensions) for filing the taxpayer's return for the year. Certain distributions, such as those that are rolled over to another retirement plan, do not affect the credit.

[3] These plan are various types of employer-sponsored retirement plans, respectively, a qualified defined contribution plan under section 401(a) or 403(a) that includes a qualified cash-or-deferred arrangement under section 401(k), a tax-deferred annuity plan under section 403(b), a governmental eligible deferred compensation plan under section 457, a plan consisting of SIMPLE IRAs under section 408(p), or a salary reduction simplified employee pension plan under section 408(k)(6). In addition to pretax elective deferrals, a section 401(k) plan, 403(b) plan or governmental 457 plan may include a designated Roth program under section 402A, under which after-tax contributions are made to a separate account (a designated Roth account), which receives tax treatment similar to the treatment of a Roth IRA.

[4] Sections 219, 408 and 408A provide rules for IRAs.

<u>Description of Discussion Draft</u>

The proposal replaces the present-law saver's credit with a new, refundable credit to be deposited directly into a tax-favored retirement account. Under the proposal, eligible taxpayers who make qualified retirement savings contributions (defined as under present law) are allowed a credit equal to the applicable percentage of their contributions up to $1,000. The maximum annual allowable credit is $500 (50 percent of $1,000) per individual. The 50-percent credit rate may be phased out based on the modified AGI ("MAGI") of the taxpayer. For this purpose, MAGI is determined without regard to certain excludable foreign-source earned income and certain U.S. possession income and without regard to any deduction or exclusion allowed for qualified retirement savings contributions made during the year. Thus, MAGI includes the taxpayer's qualified retirement savings contributions, including those exceeding $1,000.

For taxable years beginning in 2017, married taxpayers filing joint returns with AGI of $65,000 or less are permitted a tax credit of 50 percent for contributions up to $1,000. For those married taxpayers with AGI greater than $65,000 but less than $85,000, the tax credit rate of 50 percent is proportionally phased out (with rounding down to the next whole percentage point). For married taxpayers with AGI greater than $85,000, the credit is unavailable. Similarly, taxpayers filing head of household returns with AGI of $48,750 or less, and all other taxpayers filing returns with AGI of $32,500 or less are eligible for a credit of 50 percent. The credit for taxpayers filing as head of household is phased out over $15,000 of AGI, and the credit for all other taxpayers filing returns is phased out over $10,000 of AGI. As a result, heads of household with AGI of $63,750 and above, and all other taxpayers with AGI of $42,500 and above are not eligible for the credit.

For years after 2017, the maximum contribution amount of $1,000 taken into account for purposes of the credit and the AGI threshold of $65,000 for married taxpayers are indexed for inflation. The AGI thresholds and phase-out ranges for head of household returns and all other returns are calculated to be 75 percent and 50 percent, respectively, of the threshold and range for the joint returns.

Table 2.–Credit Rates for Saver's Credit Under the Proposal

	Joint Filers	Heads of Households	All Other Filers
Threshold AGI	$65,000	$48,750	$32, 500
Phase-out Range	$20,000	$15,000	$10,000
Phase-out Interval	$65,001-$85,000	$48,751-$63,750	$32,501-42,500

The amount of the credit is not limited to the amount of the taxpayer's tax liability. In addition, rather than being applied against taxpayer's tax liability, the credit amount is to be deposited as a contribution to an applicable retirement savings vehicle of the taxpayer.[5] An applicable retirement savings vehicle is, if elected by the taxpayer, a Roth IRA or a designated Roth account under a section 401(k) plan, a section 403(b) plan, or a governmental section 457 plan of the taxpayer, if the plan accepts the contribution. If the taxpayer does not elect a particular applicable retirement savings vehicle, the credit amount is contributed to a Roth IRA established under the MyRA program established by the Secretary. These credits will be treated as a contribution made by the individual. However, under the proposal, the contributions are not taxable as income to the taxpayer and do not count toward the usual contribution limits. Any plan or account to which a credit is contributed will not violate any Code requirement solely by reason of accepting the contribution.

Finally, the Secretary is directed to promote and educate taxpayers about the benefits of the credit. In addition, the Secretary (or delegate) is directed to issue guidance on the implementation and administration of the proposal by December 31, 2017.

Effective Date

The proposal applies to taxable years beginning after December 31, 2016.

[5] Any erroneously made contribution is treated as an underpayment of tax.

B. Repeal of Maximum Age for Traditional IRA Contributions

Present Law

Under present law, an individual may make deductible contributions to a traditional IRA up to the IRA contribution limit if neither the individual nor the individual's spouse is an active participant in an employer-sponsored retirement plan.[6] If an individual (or the individual's spouse) is an active participant in an employer-sponsored retirement plan, the deduction is phased out for taxpayers with adjusted gross income ("AGI") for the taxable year over certain indexed levels.[7]

To the extent an individual cannot or does not make deductible contributions to a traditional IRA, the individual may make nondeductible contributions to a traditional IRA (that is, no AGI limits apply), subject to contribution limits.[8]

An individual who has attained age 70½ prior to the close of a year is not permitted to make contributions to a traditional IRA.[9] This restriction does not apply to contributions to a Roth IRA.[10]

Description of Discussion Draft

The proposal repeals the prohibition on contributions to a traditional IRA by an individual who has attained age 70½ prior to the close of a year.

Effective Date

The proposal applies to contributions made for taxable years beginning after December 31, 2016.

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[6] Sec. 219.

[7] Sec. 219(g).

[8] Sec. 408(o). The annual contribution limit for IRAs is coordinated so that the maximum amount that can be contributed to all of an individual's IRAs (both traditional and Roth) for a taxable year is the lesser of a certain dollar amount ($5,500 for 2016) or the individual's compensation.

[9] Sec. 219(d)(1).

[10] Sec. 408A(c)(4).

C. 60-Day Rollover to Inherited Individual Retirement Plan of Nonspouse Beneficiary

Present Law

Tax-free rollover of distributions from eligible employer plans

An eligible rollover distribution from an eligible employer plan[11] may be rolled over tax-free to another eligible employer plan or IRA. A tax-free rollover may be accomplished either through a direct rollover or a 60-day rollover. A direct rollover is accomplished by direct payment through a trustee-to-trustee transfer from an eligible employer plan to another or to an IRA. A 60-day rollover from an eligible employer plan is accomplished by contributing a distribution from the plan to another eligible employer plan or IRA within 60 days of the distribution.

An eligible rollover distribution is any distribution from an eligible employer plan with certain exceptions, including certain periodic payments, any distribution to the extent the distribution is a required minimum distribution and any distribution made on account of hardship of the employee.[12] Only an employee or a surviving spouse of an employee is allowed to roll over an eligible rollover distribution from an eligible employer plan to another eligible employer plan. In the case of an eligible rollover distribution from an eligible employer plan to a beneficiary who is not the surviving spouse of the employee whose benefit is being distributed ("nonspouse beneficiary"), a rollover is permitted only to an IRA and a 60-day rollover is not permitted.[13] That is, a nonspouse beneficiary is allowed to roll over the distribution tax-free only to an IRA and only using a direct rollover.

Direct rollover and 20-percent income tax withholding

An eligible employer plan is required to offer any distributee (employee, surviving spouse, or nonspouse beneficiary) of an eligible rollover distribution an opportunity to have the distribution paid as a direct rollover before making a direct payment of the eligible rollover distribution to the distributee. Further, before making the distribution, the plan administrator (or individual acting in that capacity for the plan) must provide the distributee with a notice explaining the distributee's choices between a direct rollover or 60-day rollover, and the tax consequences of not choosing to roll over the distribution. If, after receiving the notice, the distributee fails to elect a direct rollover of the distribution, the distribution is subject to mandatory 20-percent income tax withholding.

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[11] An eligible employer plan is a qualified retirement plan (including a section 401(k) plan), a section 403(b) plan, or a governmental section 457(b) plan.

[12] Sec. 402(c)(4).

[13] Sec. 402(c)(10).

After-death minimum distribution requirement

A central element of the after-death minimum distribution requirement is whether an employee or IRA owner dies before, or on or after, the individual's required beginning date. For employer-sponsored tax-favored plans (for an employee other than an employee who is a five-percent owner in the year the employee attains age 70½), the employee's required beginning date is April 1 after the later of the calendar year in which the employee attains age 70½, or retires.[14] Under employer-sponsored qualified retirement plans, for an employee who is a five-percent owner in the year the employee attains age 70½, and for traditional IRAs, the required beginning date is April 1 following the calendar year in which the employee or IRA owner attains age 70½.

If an employee or IRA owner dies before the individual's required beginning date, the required distributions after death depend on whether there is a designated beneficiary. If there is no individual designated as beneficiary (for example the individual's estate is named as the beneficiary), the entire remaining interest must generally be distributed by the end of the fifth year following the individual's death. If there is a designated beneficiary, generally, distributions are required to be made using a distribution period measured by the designated beneficiary's life expectancy, based on the life expectancy table in the regulations, calculated in the year after the year of the death and reduced by one for each year thereafter.[15] Special rules apply if the designated beneficiary is the surviving spouse.

If an employee or IRA owner dies on or after the individual's required beginning date, the remaining interest must be distributed at least as rapidly as under the minimum distribution method being used as of the date of death. If there is an individual who is a designated beneficiary of the employee or IRA owner, the regulations interpret this as allowing payments using a distribution period equal to the remaining years of the beneficiary's life expectancy, calculated in the same manner as applies if the individual died before the required beginning date. If there is no designated beneficiary, a distribution period equal to the remaining years of the employee or IRA owner's life, as of the year of death, applies, based on the life expectancy table in the regulations.[16]

Roth IRAs are not subject to the minimum distribution rules during the IRA owner's lifetime. However, Roth IRAs are subject to the after-death minimum distribution rules that apply to traditional IRAs.

Required minimum distribution rules for rollover IRA of nonspouse beneficiary

An IRA established to receive a direct rollover on behalf of a nonspouse designated beneficiary must be an inherited IRA.[17] Thus, when a nonspouse beneficiary rolls over a distribution from an eligible employer plan to an IRA, the IRA must be established in a manner

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[14] Sec. 401(a)(9)(C).

[15] Treas. Reg. sec. 1.401(a)(9)-5, A-5(b).

[16] Treas. Reg. sec. 1.401(a)(9)-5, A-5(a).

[17] Sec. 402(c)(11).

that identifies it as an IRA with respect to a deceased individual and also identifies the deceased individual and the beneficiary, for example, "Tom Smith as beneficiary of John Smith."

The after-death minimum distribution requirements apply to the inherited IRA. The rules for determining the required minimum distributions under the distributing plan with respect to the nonspouse beneficiary also apply under the IRA. Thus, if the employee dies before his or her required beginning date and the five-year rule applies to the nonspouse designated beneficiary under the plan making the direct rollover (for example because the beneficiary inherits the IRA through the individual's estate), the five-year rule applies for purposes of determining required minimum distributions under the recipient's inherited IRA. If the life expectancy rule applies to the nonspouse designated beneficiary under the plan, the required minimum distribution under the IRA must be determined using the same applicable distribution period as would have been used under the plan if the direct rollover had not occurred. Similarly, if the employee dies on or after his or her required beginning date, the required minimum distribution under the IRA for any year after the year of death must be determined using the same distribution period as would have been used under the plan if the direct rollover had not occurred.

Tax-free rollover of distributions from IRAs

A distribution from an IRA to an IRA owner or the surviving spouse of an IRA owner may be rolled over tax-free to an eligible employer plan or another IRA. This can be accomplished by a 60-day rollover or a direct rollover. Distributions to nonspouse beneficiaries of an IRA are not permitted to be rolled over tax-free. However, a trustee-to-trustee transfer between IRAs is not treated as a rollover and is a permitted method to move funds from one IRA trustee to another by a nonspouse beneficiary. In contrast to 60-day rollovers or direct rollovers, trustee-to-trustee transfers between IRAs generally are implemented by contacting the transferee trustee and requesting that the transferee trustee arrange the transfer.

Description of Discussion Draft

The proposal allows 60-day rollovers for nonspouse beneficiaries under eligible employer plans and IRAs. Funds eligible for these rollovers include any portion of a distribution that is eligible for rollover and is paid to an IRA that is established as an inherited IRA, and for which the trustee or provider of the account or annuity is notified that the IRA is an inherited IRA.

The recipient IRA is required to be established as an inherited IRA subject to the same after-death required minimum distribution rules as applied to the distributing eligible employer plan or IRA, as required under present-law rules for direct rollovers by nonspouse beneficiaries and for trustee-to-trustee transfers between IRAs.

Effective Date

The proposal is effective for distributions after December 31, 2016.

D. Treatment of Student Loan Payments as Elective Deferrals for Purposes of Matching Contributions

Present Law

Certain tax-favored employer-sponsored retirement plans include a feature under which, subject to limits, an employee may elect to have contributions (referred to as "elective deferrals") made to the plan, rather than receive the same amount in cash. Specifically, such a feature may be included in a qualified defined contribution plan (referred to in that case as a "section 401(k) plan") or a tax-deferred annuity plan (referred to as a "section 403(b)" plan).[18] Such a feature is also included in a SIMPLE IRA plan.[19] An employee's elective deferrals for a year under these plans are subject to a limit of the lesser of (1) a dollar amount, depending on the type of plan, and (2) the employee's compensation. In the case of a section 401(k) or section 403(b) plan, the dollar amount for 2016 is $18,000. In the case of a SIMPLE IRA plan, the dollar amount for 2016 is $12,500.[20]

These plans also commonly provide for employer matching contributions, that is, contributions made by the employer on behalf of an employee that are contingent on the employee's making elective deferrals and the amount of which depends on the amount of the employee's elective deferrals.[21] Thus, an employee who makes no elective deferrals receives no matching contributions. Alternatively, an employee may make some elective deferrals, but not in an amount to receive the maximum amount of matching contributions available under the plan.

Elective deferrals and matching contributions under a section 401(k) or section 403(b) plan must satisfy certain requirements that prohibit discrimination in favor of highly compensated employees (referred to as "nondiscrimination" requirements). Certain plan designs (referred to as "safe harbor" plans) automatically meet the nondiscrimination requirements. Some of the requirements applicable to SIMPLE IRA plans are also designed to prevent discrimination in favor of highly compensated employees.

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[18] Section 401(k) provides rules for including this feature in a qualified defined contribution plan, and section 403(b) provides rules for tax-deferred annuity plans. An eligible deferred compensation plan of a State or local government under section 457(b) also provides for elective deferrals, but not employer matching contributions. Elective deferrals may be made on a pretax basis, or, if the plan permits, on an after-tax "Roth" basis as discussed below in Part II.B.

[19] Sec. 408(p).

[20] Secs. 402(g) and 408(p). Under section 414(v), employees age 50 or older may also make additional contributions, referred to as "catch-up" additional contributions.

[21] Sec. 401(m). A qualified defined contribution plan or section 403(b) plan may also allow employees to make after-tax employee contributions that are not elective deferrals and may provide matching contributions with respect to the after-tax employee contributions.

Description of Discussion Draft

Under the proposal, employer matching contributions include any employer contribution made to a section 401(k), section 403(b) or SIMPLE IRA plan on behalf of an employee on account of a qualified student loan payment of the employee, including for purposes of the nondiscrimination requirements.

Qualified student loan payments are payments made by an employee in repayment of a qualified education loan incurred to pay higher education expenses of the employee or to refinance a qualified education loan of the employee.[22] The employee must provide evidence of the loan and loan payments. The total qualified student loan payments taken into account for matching purposes in a given year, together with elective deferrals made by the employee for the year, are subject to the present law limits on elective deferrals.

The employer plan must provide matching contributions on qualified student loan payments only on behalf of employees who are otherwise eligible to make elective deferrals; matching contributions on elective deferrals must be made at the same rate as matching contributions on qualified student loan payments; and all employees eligible to receive matching contributions on elective deferrals must be eligible to receive matching contributions on qualified student loan payments.

For purposes of the nondiscrimination requirements, a safe harbor plan or SIMPLE IRA plan may treat a qualified student loan payment as an elective deferral, and employer matching contributions on qualified student loan payments will not be considered to be unavailable to an employee solely because such employee does not have debt incurred under a qualified education loan.

Effective Date

The proposal is effective for contributions made for years beginning after December 31, 2016.

[22] The proposal refers to qualified education loan as defined in section 221(d)(1).

TITLE II – TREATMENT OF ROTH IRAS; MINIMUM REQUIRED DISTRIBUTIONS

A. Special Rules Relating to Large Roth IRA Account Balances

Present Law

In general

An IRA is a tax-favored savings arrangement under which retirement savings are held in a tax-exempt trust or custodial account (or annuity contract) until distributed. There are two basic types of IRAs under present law: traditional IRAs,[23] to which both deductible and nondeductible contributions may be made,[24] and Roth IRAs, to which only nondeductible contributions may be made.[25] The principal difference between these two types of IRAs is the timing of income tax inclusion. For a traditional IRA, an eligible contributor may deduct the contributions made for the year, and distributions are includible in gross income to the extent attributable to earnings on the account and the deductible contributions. For a Roth IRA, all contributions are after-tax (that is, no deduction is allowed) and, if certain requirements are satisfied, distributions are not includible in gross income.

Tax-favored treatment applies also to certain employer-sponsored retirement plans, including qualified retirement plans, tax-deferred annuity plans ("section 403(b) plan"), and governmental eligible deferred compensation plans ("governmental section 457(b) plan").[26] A qualified defined contribution plan may include a qualified cash-or-deferred arrangement ("section 401(k) plan"), under which a participant may make pretax elective deferrals. Section 403(b) plans and governmental section 457(b) plans also generally provide for pretax elective deferrals. These plans may also provide for pretax employer contributions that are not elective deferrals. The distinction between traditional accounts (also called pretax accounts) and Roth accounts also exists for amounts held in individual accounts under these tax-favored employer-sponsored retirement plans with a qualified Roth contribution program.[27]

Accumulations or aggregate account balances in IRAs (both traditional and Roth IRAs) include both regular IRA contributions and rollover contributions from tax-favored employer-sponsored retirement plans and other IRAs. As discussed in more detail below, the amount (and attributable earnings) held in Roth IRAs may consist of not only amounts originally contributed

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[23] Sec. 408. IRAs include individual retirement accounts under section 408(a) and individual retirement annuities under section 408(b).

[24] Sec. 219.

[25] Sec. 408A.

[26] Sections 401(a) and 403(a), 403(b), and 457 respectively provide rules governing these plans. Section 401(k) provides rules for a cash-or-deferred arrangement.

[27] Section 402A describes a qualified Roth contribution program. See Part II.B for a detailed description of these programs.

to Roth accounts (Roth IRAs or designated Roth accounts under employer-sponsored plans) as Roth contributions, but also amounts originally contributed to traditional or pretax accounts and then subsequently converted to Roth accounts.

An individual may receive an interest in a traditional or Roth IRA as a result of a transfer from a spouse or former spouse under a divorce or separation instrument.[28] Such a transfer is not taxable for the transferring spouse, and the resulting IRA is considered to be the IRA of the recipient spouse maintained for his or her benefit. An individual may also become the beneficiary of a traditional or Roth IRA after the death of the original IRA owner.[29] In some respects, an IRA inherited by a beneficiary other than the IRA's surviving spouse are subject to more restrictive rules than other IRAs. If the spouse of the original IRA owner inherits the IRA, the spouse may treat the IRA as his or her own IRA, rather than as an inherited IRA.

Limits on regular annual IRA contributions

Annual contribution limit

An annual limit applies to contributions to IRAs. The contribution limit is coordinated so that the aggregate maximum amount that can be contributed to all of an individual's IRAs (both traditional and Roth) for a taxable year is the lesser of (1) a certain dollar amount ($5,500 for 2016) plus $1,000 for an individual who has attained age 50 or (2) the individual's compensation. In the case of a married couple, contributions can be made up to the dollar limit for each spouse if the combined compensation of the spouses is at least equal to the contributed amount. In addition, deductible contributions to traditional IRAs and after-tax contributions to Roth IRAs generally are subject to AGI limits. IRA contributions generally must be made in cash.

Traditional IRAs

An individual may make deductible contributions to a traditional IRA up to the IRA contribution limit if neither the individual nor the individual's spouse is an active participant in an employer-sponsored retirement plan. If an individual (or the individual's spouse) is an active participant in an employer-sponsored retirement plan, the deduction is phased out for taxpayers with adjusted gross income ("AGI") for the taxable year over certain indexed levels. In the case of an individual who is an active participant in an employer-sponsored plan, the AGI phase-out ranges for 2016 are: (1) for single taxpayers, $61,000 to $71,000; (2) for married taxpayers filing joint returns, $98,000 to $118,000; and (3) for married taxpayers filing separate returns, $0 to $10,000. If an individual is not an active participant in an employer-sponsored retirement plan, but the individual's spouse is, the deduction is phased out for taxpayers with AGI for 2016 between $184,000 and $194,000.

To the extent an individual cannot or does not make deductible contributions to a traditional IRA or contributions to a Roth IRA for the taxable year, the individual may make

[28] Sec. 408(d)(6).

[29] Sec. 408(d)(3)(C).

nondeductible contributions to a traditional IRA (that is, no AGI limits apply), subject to the same contribution limits as the limits on deductible contributions, including catch-up contributions. An individual who has attained age 70½ prior to the close of a year is not permitted to make contributions to a traditional IRA.

Roth IRAs

Individuals with AGI below certain levels may make nondeductible contributions to a Roth IRA. The maximum annual contribution that can be made to a Roth IRA is phased out for taxpayers with AGI for the taxable year over certain indexed levels. The AGI phase-out ranges for 2016 are: (1) for single taxpayers, \$117,000 to \$132,000; (2) for married taxpayers filing joint returns, \$184,000 to \$194,000; and (3) for married taxpayers filing separate returns, \$0 to \$10,000. Contributions to a Roth IRA may be made even after the account owner has attained age 70½.

Excise tax on excess contributions

To the extent that contributions to an IRA exceed the contribution limits, the individual is subject to an excise tax equal to six percent of the excess amount.[30] This excise tax generally applies each year until the excess amount is distributed. Any amount contributed for a taxable year that is distributed with allocable income by the due date for the taxpayer's return for the year will be treated as though not contributed for the year.[31]

Taxation of Roth IRA distributions

Amounts held in a Roth IRA that are withdrawn as a qualified distribution are not includible in income. A qualified distribution is a distribution that (1) is made after the five-taxable-year period beginning with the first taxable year for which the individual first made a contribution to a Roth IRA, and (2) is made after attainment of age 59½, on account of death or disability, or is made for first-time homebuyer expenses of up to \$10,000.

Distributions from a Roth IRA that are not qualified distributions are includible in income to the extent attributable to earnings; amounts that are attributable to a return of contributions to the Roth IRA are not includible in income. All Roth IRAs are aggregated for purposes of determining the amount that is a return of contributions. To determine the amount includible in income, a distribution that is not a qualified distribution is treated as made in the following order: (1) regular Roth IRA contributions (including contributions rolled over from other Roth IRAs); (2) conversion contributions (on a first in, first out basis); and (3) earnings. To the extent a distribution is treated as made from a conversion contribution, it is treated as made first from the portion, if any, of the conversion contribution that was required to be included in income as a result of the conversion. Thus, nonqualified distributions from all Roth

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[30] Sec. 4973(a), (b) and (f).

[31] Sec. 408(d)(4). To receive this treatment for a contribution to a traditional IRA, the taxpayer must not have claimed a deduction for the amount of the distributed contribution.

IRAs are excludable from gross income until all amounts attributable to contributions have been distributed.

The Code imposes an early distribution tax on distributions made from Roth IRAs before the earlier of when the Roth IRA owner attains age 59½, becomes disabled, or dies unless an exception applies.[32] The tax is equal to 10 percent of the amount of the distribution that is includible in gross income. The 10-percent tax is in addition to the taxes that would otherwise be due on distribution.

Distributions from Roth IRAs are permitted to be rolled over tax-free to another Roth IRA. The rollover generally can be achieved by direct rollover (direct payment from the distributing plan to the recipient plan) or by contributing the distribution to the eligible retirement plan within 60 days of receiving the distribution ("60-day rollover"). Distributions from an inherited IRA (except in the case of an IRA acquired by the surviving spouse by reason of the IRA owner's death) and required minimum distributions are not permitted to be rolled over.[33]

Separation of traditional and Roth IRA accounts and Roth conversions

Contributions to traditional IRAs and to Roth IRAs must be segregated into separate IRAs, meaning arrangements with separate trusts, accounts, or contracts, and separate IRA documents. Except in the case of a conversion or recharacterization, amounts cannot be transferred or rolled over between the two types of IRAs.

Taxpayers generally may convert any amount in a traditional IRA into an amount in a Roth IRA through a distribution from the traditional IRA and rollover to a Roth IRA (either a direct payment or a 60-day rollover).[34] The amount converted is includible in the taxpayer's income as if a withdrawal had been made, except that the 10-percent early distribution tax does not apply. However, the early distribution tax is imposed if the taxpayer withdraws the amount within five years of the conversion.

If an individual makes a contribution to an IRA (traditional or Roth) for a taxable year, the individual is permitted to recharacterize (in a trustee-to-trustee transfer) the amount of that contribution as a contribution to the other type of IRA (traditional or Roth) before the due date

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[32] Sec. 72(t). The tax also applies to early distributions made from qualified retirement plans, section 403(b) plans and traditional IRAs. The early distribution tax does not apply to distributions from governmental section 457(b) plans.

[33] A trustee-to-trustee transfer between IRAs is not treated as a distribution and rollover. Thus, nonspouse beneficiaries of IRAs can move funds to another inherited IRA established as a beneficiary of the decedent IRA owner. (See proposal in Part I.C eliminating this rollover restriction between inherited IRAs.) In contrast, a surviving spouse is permitted to roll over a distribution to his or her own IRA.

[34] Sec. 408A(d)(3). A conversion can also be achieved by simply redesignating the traditional IRA as a Roth IRA if the entire balance in the account is converted and the amount is eligible for rollover. The same limitations on amounts that may be rolled over from one Roth IRA to another apply. For example, a rollover of a required minimum distribution is not allowed.

for the individual's income tax return for that year.[35] Both regular contributions and conversion contributions to a Roth IRA can be recharacterized as having been made to a traditional IRA.

Rollovers from employer-sponsored plans to Roth IRAs

A distribution from a qualified retirement plan, section 403(b) plan, or a governmental section 457(b) plan that is an eligible rollover distribution may be rolled over to another such plan or an IRA (including to a Roth IRA).[36] The rollover generally can be achieved by direct rollover or 60-day rollover. Amounts that are rolled over are usually not included in gross income.

Distributions from designated Roth accounts may be rolled over tax-free to a Roth IRA. Other distributions from qualified retirement plans, section 403(b) plans, and governmental section 457(b) plans also may be rolled into a Roth IRA. However, under the Roth IRA conversion rules, distributions from these plans that are rolled over into a Roth IRA and that are not distributions from a designated Roth account must be included in gross income to the extent required if not rolled over.[37]

Required minimum distributions

Distributions from traditional IRAs and employer-sponsored retirement plans are generally required to begin at attainment of age 70½ and to be made in certain minimum amounts ("required minimum distributions").[38] Under present law, the requirement to begin distributions at attainment of age 70½ does not apply to Roth IRAs.[39]

Reporting requirements

Certain annual reporting requirements apply to the trustee, custodian, or issuer of an IRA. By January 31 of each year, the trustee, custodian, or issuer must report to the individual for whom the IRA is maintained the fair market value of the account as of the end of the immediately preceding calendar year as well as the amount of distributions made during such

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[35] Sec. 408A(d)(6) and Treas. Reg. sec. 1.408A-6. In the case of a recharacterization, the contribution will be treated as having been made to the transferee plan (and not the transferor plan). The amount transferred must be accompanied by any net income allocable to the contribution and no deduction is allowed with respect to the contribution to the transferor plan. Treasury regulations limit the number of times a contribution for a taxable year may be recharacterized.

[36] Under section 402(c)(4), any distribution of all or any portion of the balance to the credit of a participant is an eligible rollover distribution with exceptions, for example, certain periodic payments, required minimum distributions, and hardship distributions. Treas. Reg. sec. 1.402(c)-1 identifies certain other payments that are not eligible for rollover, including, for example, certain corrective distributions, loans that are treated as deemed distributions under section 72(p), and dividends on employer securities as described in section 404(k).

[37] Sec. 408A(d)(3).

[38] Secs. 401(a)(9) and 408(a)(6) and (b)(3). See Part II.C for a detailed description of the present-law required minimum distribution rules and proposals to change the rules.

[39] Sec. 408A(c)(5). See Part II.C for a proposal to repeal this provision and apply this rule to Roth IRAs.

preceding year. [40] Also by January 31, of each year, the trustee must also furnish an IRA owner with certain information with respect to the amount of life-time required minimum distributions for the year (that includes such January 31), either the amount of the required minimum distributions that must be made for the year or an offer to provide the amount upon request. [41]

Description of Discussion Draft

Dollar limit on aggregate Roth IRA accumulations

Under the proposal, a dollar limit is provided with respect to an individual's aggregate Roth IRA accumulations ("Roth IRA accumulation limit"). The Roth IRA accumulation limit for an individual is the greater of (1) $5,000,000 or (2) the aggregate account balances as of December 31, 2016, in all Roth IRAs maintained for the benefit of the individual ("grandfathered Roth IRA accumulation"). The $5,000,000 is adjusted for increases in cost of living for years after 2017.

In applying the Roth IRA accumulation limit for a year, an individual's aggregate account balances in all Roth IRAs maintained on behalf of the individual determined as of the close of the preceding calendar year ("prior year aggregate Roth IRA balance") are compared to the individual's Roth IRA accumulation limit. In calculating an individual's prior year aggregate Roth IRA balance or grandfathered Roth IRA accumulation, amounts attributed to the acquisition of Roth IRAs (or transfer or contributions of amounts to Roth IRAs) by reason of the death of another individual (such, as the individual's parent or spouse), on account of divorce, or resulting from a rollover from a designated Roth account are included in the aggregate account balance. Further any amount distributed before December 31 of a year and contributed to a Roth in the immediately following year as a 60-day rollover is also included in an individual's aggregate account balance as of that December 31. Finally, in the case of a Roth IRA that is an individual retirement annuity, the account balance of the Roth IRA is equal to the fair market value of the annuity for purposes of calculating the individual's prior year aggregate Roth IRA balance or grandfathered Roth IRA accumulation.

Limit on Roth IRA contributions

If an individual's prior year aggregate Roth IRA balance is less than an individual's Roth IRA accumulation limit, the individual is allowed to make Roth IRA contributions for the year to the extent of the lesser of (1) the individual's otherwise applicable Roth IRA contribution limit or (2) the amount by which the individual's Roth IRA accumulation limit exceeds the individual's prior year aggregate Roth IRA balance. If an individual's prior year aggregate Roth IRA balance equals or exceeds the individual's Roth IRA accumulation limit, no contributions

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[40] Sec. 408(i). This information is also required to be reported to the IRS. The end of year balance is reported on Form 5498 and the amount of distributions made during the year are reported on Form 1099-R.

[41] Notice 2002-27, 2002-1 C.B. 814. This reporting does not apply to required minimum distributions after the death of the IRA owner. Reporting to the IRS on Form 5498, must indicate whether a minimum distribution is required for the year.

are allowed to be made to any Roth IRA for the calendar year. To the extent that contributions exceed this limit, the excise tax on excess Roth contributions applies.

For purposes of this aggregate Roth IRA contribution limit, amounts resulting from the acquisition of Roth IRAs (or transfer or contributions of amounts to Roth IRAs) by reason of the death of another individual, on account of divorce, or a qualified rollover contribution are not treated as contributions but as described above are included in the individual's prior year aggregate Roth IRA balance for the next year.

<u>Additional minimum distribution requirement for Roth IRAs</u>

If an individual's prior year aggregate Roth IRA balance exceeds the individual's Roth IRA accumulation limit for a year, a minimum distribution is required for the year with respect to the individual's Roth IRAs. The minimum distribution is the greater of (1) 50 percent of the amount by which the individual's prior year aggregate Roth IRA balance exceeds the individual's Roth IRA accumulation limit, or (2) the sum of the minimum required distributions (determined without regard to this proposal) with respect to the individual's Roth IRAs. This minimum distribution requirement applies without regard to whether minimum distributions are otherwise required with respect to the individual's Roth IRAs (*i.e.*, the amount under (2) above is zero). To the extent that this additional minimum distribution requirement is not satisfied, an excise equal to 50 percent of the required minimum amount not distributed for the year is imposed.

If the individual is under age 59½, the 10-percent additional tax on early distributions does not apply to this required distribution.

<u>Administration of new requirements</u>

Because an individual's prior year aggregate Roth IRA balance may include account balances from multiple IRAs, it is understood that it is the responsibility of the individual for whose benefit the IRAs are maintained, not the IRA trustees, custodians, or issuers, to determine the amount of the prior year aggregate Roth IRA balance and whether the balance exceeds the limit, and by how much. Similarly, it is the responsibility of the individual to determine if the limit on contributions and additional required minimum distribution rule applies. However, as described above, present law requires IRA trustees, custodians, issuers to annually report the end-of-year account balances which the individual can use for these calculations.

<u>Effective Date</u>

The proposal applies to taxable years beginning after December 31, 2016.

B. Elimination of Roth Conversions

Present Law

Roth IRA conversions

As described above, there are two basic types of IRAs under present law: traditional IRAs and Roth IRAs. For a traditional IRA, an eligible contributor may deduct the contributions made for the year, and distributions are includible in gross income to the extent attributable to earnings on the account and the deductible contributions. For a Roth IRA, all contributions are after-tax (that is, no deduction is allowed) and, if certain requirements are satisfied, distributions are not includible in gross income. The contribution limit is coordinated so that the aggregate maximum amount that can be contributed to all of an individual's IRAs (both traditional and Roth) for a taxable year is the lesser of (1) a certain dollar amount ($5,500 for 2016) plus $1,000 for an individual who has attained age 50 or (2) the individual's compensation.

Taxpayers generally may convert any amount in a traditional IRA into an amount in a Roth IRA through a distribution from the traditional IRA and rollover to a Roth IRA (either a direct payment or a 60-day rollover, as described above).[42] The amount converted is includible in the taxpayer's income as if a withdrawal had been made, except that the 10-percent early distribution tax does not apply.[43] Distributions from employer-sponsored retirement plans that are not from designated Roth accounts (described below) may also be contributed to a Roth IRA as a rollover and thereby converted to a Roth IRA amount. The amount rolled over must be included in gross income to the extent required if not rolled over. However, for both types of conversions, the early distribution tax is imposed if the taxpayer withdraws the amount within five years of the conversion.

In-plan Roth conversions

Section 401(k) plans, section 403(b) plans, and governmental section 457(b) plans

A qualified defined contribution plan may allow an employee to make elective deferrals (that, is contributions made pursuant to an election between cash and an employer contribution to the plan pursuant to a qualified cash or deferred arrangement).[44] A plan with this feature is generally referred to as a section 401(k) plan. A section 403(b) plan may also allow an employee to make elective deferrals. The elective deferrals generally are excludable from gross income (pretax elective deferrals) and only taxed along with attributable earnings upon distribution from the plan. Alternatively the plan may include a qualified Roth contribution program under which eligible employees are offered a choice of either making pretax elective deferrals or making

[42] A conversion can also be achieved by simply predesignating the traditional IRA as a Roth IRA if the entire balance in the account is converted. See a more detailed description of the rollover rules in Part II.A above.

[43] A detailed discussion of the early distribution tax is provided in Part II.A.

[44] Sec. 401(k).

elective deferrals that are not excluded from income and are designated as Roth contributions.[45] If certain requirements are satisfied, distributions of designated Roth contributions and attributable earnings are excluded from gross income. The employer may also make nonelective and matching contributions for employees under a section 401(k) or 403(b) plan. These are not permitted to be designated as Roth contributions and generally are pretax contributions. A plan may also allow participants to make elective after-tax contributions that are not elective deferrals and are not treated as designated Roth contributions.

A limit applies to the aggregate amount of elective deferrals (both pretax elective deferrals and designated Roth contributions) that an employee is permitted to contribute to section 401(k) and section 403(b) plans for a taxable year. The limit is $18,000 for 2016, plus an additional catch-up amount of $6,000 for 2016 if the employee is age 50 or older (or the employee's compensation if less than this sum). Total contributions, including pretax employer nonelective and matching contributions, elective deferrals (but not including catch-up contributions), and after-tax contributions, to a section 401(k) plan or 403(b) plan for a plan year for an employee generally cannot exceed $53,000 for 2016 (or the employee's compensation, if less).[46]

A governmental section 457(b) plan may also provide for elective deferrals. Contributions to a governmental section 457(b) plan are subject to a limit of $18,000 for 2016 plus an additional $6,000 catch-up contribution amount for 2016 for employees at least age 50 (or the employee's compensation, if less).[47] This limit is separate from the limit on elective deferrals to section 401(k) and section 403(b) plans.[48] As in the case of a section 401(k) plan or a section 403(b) plan, the plan may include a qualified Roth contribution program under which employees are given the choice between making pretax elective deferrals and designated Roth contributions.

Designated Roth accounts

All designated Roth contributions made under a qualified Roth contribution program must be maintained in a separate account (a designated Roth account) under the plan. A qualified distribution from a designated Roth account is excludable from gross income. A qualified distribution is a distribution that is made after (1) an employee's completion of a specified five-year period and (2) the employee's attainment of age 59½, death, or disability.

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[45] Sec. 402A. Under Treas. Reg. secs. 1.401(k)-1(f) and 1.403(b)-3(c), a plan is not permitted to only allow employees to make designated Roth contributions; pretax elective deferrals must also be permitted.

[46] Secs. 415(c) and 403(b)(1).

[47] Under a special rule, additional catch-up contributions may be made by a participant to a governmental section 457(b) for the last three years before attainment of normal retirement age.

[48] For example, if an employee participates in both a section 403(b) plan and a governmental section 457(b) plan of the same employer, the employee may contribute up to $18,000 (plus $6,000 catch-up contributions if at least age 50) to the section 403(b) plan and up to $18,000 (plus $6,000 catch-up contributions if at least age 50) to the section 457(b) plan.

A distribution from a designated Roth account (other than a qualified distribution) is included in the distributee's gross income to the extent allocable to pretax earnings on the account and excluded from gross income to the extent allocable to the after-tax designated Roth contributions (commonly referred to as "basis" in the account).

Roth conversions

A section 401(k) plan, section 403(b) plan, or governmental 457(b) plan that maintains a qualified Roth contribution program may allow amounts held in accounts that are not designated Roth accounts ("nonRoth accounts") to be transferred into a designated Roth account either by an in-plan transfer or a distribution and 60-day rollover. The transfer is allowed whether or not the amount is otherwise distributable. However, the amount transferred (or rolled over) must be included in gross income as though distributed, as in the case of Roth IRA conversions, and the early distribution tax is imposed if the taxpayer withdraws the amount within five years of the conversion.

Description of Discussion Draft

Under the proposal, amounts held in traditional IRAs may not be converted to amounts held in Roth IRAs. Further, amounts held in nonRoth accounts in section 401(k) plans, section 403(b) plans, and governmental section 457(b) plans may not be converted into either amounts held in a designated Roth account or in a Roth IRA.

The elimination of Roth conversions is achieved by repealing the provisions that allow rollovers of distributions from nonRoth accounts (both under traditional IRAs or employer-sponsored retirement plans) to Roth IRAs and that allow in-plan transfers (or rollovers) from nonRoth accounts under an employer-sponsored retirement plan to designated Roth accounts under the plan.

Effective Date

The proposal applies to distributions, transfers, and contributions made in years beginning after December 31, 2016.

C. Modifications to Required Minimum Distribution Rules

Present Law

Minimum distribution rules apply to tax-favored employer-sponsored retirement plans and IRAs.[49] Employer-sponsored retirement plans are of two general types: defined benefit plans, under which benefits are determined under a plan formula and paid from general plan assets, rather than individual accounts; and defined contribution plans, under which benefits are based on a separate account for each participant, to which are allocated contributions, earnings and losses.

In general, under the minimum distribution rules, distribution of minimum benefits must begin to an employee (or IRA owner) no later than a required beginning date and a minimum amount must be distributed each year (sometimes referred to as "lifetime" minimum distribution requirements).[50] These lifetime requirements do not apply to a Roth IRA.

Minimum distribution rules also apply to benefits payable with respect to an employee (or IRA owner) who has died (sometimes referred to as "after-death" minimum distribution requirements). The regulations provide a methodology for calculating the required minimum distribution from an individual account under a defined contribution plan or from an IRA.[51] In the case of annuity payments under a defined benefit plan or an annuity contract, the regulations provide requirements that the stream of annuity payments must satisfy.

Failure to comply with the minimum distribution requirement results in an excise tax imposed on the individual who was required to take the distributions equal to 50 percent of the required minimum amount not distributed for the year.[52] The excise tax may be waived in certain cases. For qualified retirement plans, satisfying the minimum distribution requirement under the plan terms and in operation is also a qualification requirement for the trust of the plan to remain tax-exempt.

Required beginning date

For traditional IRAs, the required beginning date is April 1 following the calendar year in which the IRA owner attains age 70½. For employer-sponsored retirement plans, for an

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[49] Sections 401(a)(9), 403(b)(1), 408(a)(6), 408(b)(3), and 457(d)(2). Tax-favored employer-sponsored retirement plans include qualified retirement plans and annuities under sections 401(a) and 403(a), tax-deferred annuity plans under section 403(b), and governmental eligible deferred compensation plans under section 457(b). Minimum distribution requirements also apply to eligible deferred compensation plans under section 457(b) of tax-exempt employers.

[50] Under sec. 408A(c)(5),.

[51] Reflecting the directive in section 823 of the Pension Protection Act of 2006 (Pub. L. No. 109-280), pursuant to Treas. Reg. sec. 1.401(a)(9)-1, A-2(d), a governmental plan within the meaning of section 414(d) or a governmental eligible deferred compensation plan is treated as having complied with the statutory minimum distribution rules if the plan complies with a reasonable and good faith interpretation of those rules.

[52] Section 4974.

employee other than an employee who is a five-percent owner in the year the employee attains age 70½, the required beginning date is April 1 after the later of the calendar year in which the employee attains age 70½ or retires. For an employee who is a five-percent owner under an employer-sponsored tax-favored retirement plan in the year the employee attains age 70½, the required beginning date is the same as for IRAs even if the employee continues to work past age 70½.

Lifetime rules

While an employee (or IRA owner) is alive, distributions of the individual's interest are required to be made (in accordance with regulations) over the life or life expectancy of the employee (or IRA owner), or over the joint lives or joint life expectancy of the employee (or IRA owner) and a designated beneficiary.[53] For defined contribution plans and IRAs, the required minimum distribution for each year is determined by dividing the account balance as of the end of the prior year by a distribution period which, while the employee (or IRA owner) is alive, is the factor for the employee (or IRA owner's) age from the uniform lifetime table included in the Treasury regulations.[54] The distribution period for annuity payments under a defined benefit plan or annuity contract (to the extent not limited to the life of the employee (or IRA owner) or the joint lives of the employee (or IRA owner) and a designated beneficiary) is generally subject to the same limitations as apply to individual accounts.

After-death rules

Payments over a distribution period

The after-death minimum distributions rules vary depending on (i) whether an employee (or IRA owner) dies on or after the required beginning date or before the required beginning date, and (ii) whether there is a designated beneficiary for the benefit.[55] Under the regulations, a designated beneficiary is an individual designated as a beneficiary under the plan or IRA.[56]

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[53] Section 401(a)(9)(A).

[54] Treas. Reg. sec. 1.401(a)(9)-5. This table is based on the joint life and last survivor expectancy of the individual and a hypothetical beneficiary 10 years younger. For an individual with a spouse as designated beneficiary who is more than 10 years younger (and thus the number of years in the couple's joint life and last survivor expectancy is greater than the uniform lifetime table), the joint life expectancy and last survivor expectancy of the couple (calculated using the table in the regulations) is used. For this purpose and other special rules that apply to the surviving spouse as beneficiary, a former spouse to whom all or a portion of an employee's benefit is payable pursuant to a qualified domestic relations order (within the meaning of section 414(p)) is treated as the spouse (including a surviving spouse) of the employee for purposes of section 401(a)(9).

[55] In the case of amounts for which the employee or IRA owner's surviving spouse is the beneficiary, the surviving spouse generally is permitted to do a tax-free rollover of such amounts into an IRA (or account of a tax-favored employer-sponsored plan of the spouse's employer) established in the surviving spouse's name as IRA owner or employee. The rules applicable to the rollover account, including the minimum distribution rules, are the same rules that apply to an IRA owner or employee. In the case of an IRA for which the spouse is sole beneficiary, this is can be accomplished by simply renaming the IRA as an IRA held by the spouse as IRA owner rather than as a beneficiary.

[56] Treas. Reg. sec. 1.401(a)(9)-4, A-1. The individual need not be named as long as the individual is identifiable under the terms of the plan (or IRA). There are special rules for multiple beneficiaries and for trusts

Similar to the lifetime rules, for defined contribution plans and IRAs ("individual accounts"), the required minimum distribution for each year after the death of the employee (or IRA owner) is generally determined by dividing the account balance as of the end of the prior year by a distribution period.

If an employee (or IRA owner) dies on or after the required beginning date, the basic statutory rule is that the remaining interest must be distributed at least as rapidly as under the method of distribution being used before death.[57] Under the regulations, for individual accounts, this rule is also interpreted as requiring the minimum required distribution to be calculated using a distribution period. If there is no designated beneficiary, the distribution period is equal to the remaining years of the employee's (or IRA owner's) life, as of the year of death.[58] If there is a designated beneficiary, the distribution period (if longer) is the beneficiary's life expectancy calculated using the life expectancy table in the regulations, determined in the year after the year of death.[59]

If an employee (or IRA owner) dies before the required beginning date and any portion of the benefit is payable to a designated beneficiary, the statutory rule is that distributions are generally required to begin within one year of the employee's (or IRA owner's) death (or such later date as prescribed in regulations) and are permitted to be paid (in accordance with regulations) over the life or life expectancy of the designated beneficiary. If the beneficiary of the employee (or IRA owner) is the individual's surviving spouse, distributions are not required to commence until the year in which the employee (or IRA owner) would have attained age 70½. If the surviving spouse dies before the employee (or IRA owner) would have attained age 70½, the after-death rules apply after the death of the spouse as though the spouse were the employee (or IRA owner). Under the regulations, for individual accounts, the required minimum distribution for each year is determined using a distribution period and the period is measured by the designated beneficiary's life expectancy, calculated in the same manner as if the individual died on or after the required beginning date.[60]

In cases where distribution after death is based on life expectancy (either the remaining life expectancy of the employee (or IRA owner) or a designated beneficiary), the distribution period generally is fixed at the employee's (or IRA owner's) death and then reduced by one for each year that elapses after the year in which it is calculated. If the designated beneficiary dies

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named as beneficiary (where the beneficiaries of the trust are individuals). However, the fact that an interest under a plan or IRA passes to a certain individual under a will or otherwise under State law does not make that individual a designated beneficiary unless the individual is designated as a beneficiary under the plan or IRA.

[57] Section 401(a)(9)(B)(i).

[58] Treas. Reg. sec. 1.401(a)(9)-5, A-5(a)(2).

[59] Treas. Reg. sec. 1.401(a)(9)-5, A-5(a)(1).

[60] Treas. Reg. sec. 1.401(a)(9)-5, A-5(b).

during the distribution period, distributions continue to the subsequent beneficiaries over the remaining years in the distribution period.[61]

The distribution period for annuity payments under a defined benefit plan or annuity contract (to the extent not limited to the life of a designated beneficiary) is generally subject to the same limitations as apply to individual accounts.

Five-year rule

If an employee (or IRA owner) dies before the required beginning date and there is no designated beneficiary, then the entire remaining interest of the employee (or IRA owner) must generally be distributed by the end of the fifth calendar year following the individual's death.[62]

Defined benefit plans and annuity distributions

The regulations provide rules for the amount of annuity distributions from a defined benefit plan, or from an annuity purchased by the plan from an insurance company, that are paid over life or life expectancy. Annuity distributions are generally required to be nonincreasing with certain exceptions, which include, for example, (i) increases to the extent of certain specified cost-of-living indices, (ii) a constant percentage increase (for a qualified defined benefit plan, the constant percentage cannot exceed five percent per year), (iii) certain accelerations of payments, and (iv) increases to reflect when an annuity is converted to a single life annuity after the death of the beneficiary under a joint and survivor annuity or after termination of the survivor annuity under a qualified domestic relations order.[63] If distributions are in the form of a joint and survivor annuity and the survivor annuitant both is not the surviving spouse and is younger than the employee (or IRA owner), the survivor annuity benefit is limited to a percentage of the life annuity benefit for the employee (or IRA owner). The survivor benefit as a percentage of the benefit of the primary annuitant is required to be smaller (but not required to be less than 52 percent) as the difference in the ages of the primary annuitant and the survivor annuitant become greater.

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[61] If the distribution period is based on the surviving spouse's life expectancy (whether the employee or IRA owner's death is before or after the required beginning date), the spouse's life expectancy generally is recalculated each year while the spouse is alive and then fixed the year after the spouse's death.

[62] Section 401(a)(9) (B)(ii) provides that the entire interest must be distributed within five years of the employee's death. Treas. Reg. sec. 1.401(a)(9)-3, A-2, provides that this requirement is satisfied if the entire interest is distributed by the end of the fifth calendar year following the employee's death. There are provisions in the regulations allowing a designated beneficiary to take advantage of the five-year rule. See Treas. Reg. secs. 1.401(a)(9)-4, A-4, and 1.4974-2, A-7(b).

[63] Treas. Reg. sec. 1.401(a)(9)-6, A-14.

Prohibited payments

A single-employer defined benefit pension plan is required to comply with certain funding-based limitations on benefits and benefit accruals.[64] Among the limitations is a requirement that, if the plan's adjusted funding target attainment percentage ("AFTAP")[65] is less than 60 percent for a plan year, the plan is not permitted to make any prohibited payments after the valuation date for the plan year. If the plan sponsor of a defined benefit plan is a debtor in a bankruptcy case under Title 11 of the United States Code, or similar Federal or State law, the plan is generally not permitted to make a prohibited payment unless or until the plan's AFTAP is not less than 100 percent. If a defined benefit plan's AFTAP for a plan year is more than 60 percent but less than 80 percent, generally a distribution of 50 percent of the otherwise prohibited payment is permitted to be made.

A prohibited payment is generally any amount in excess of the monthly amount paid under a single life annuity to a participant or beneficiary whose annuity starting date occurs during any period that the limitation is in effect. A prohibited payment also includes any payment to purchase an annuity contract from an insurance company or any other payment specified by the Secretary of the Treasury ("Secretary").

Plan amendment and anti-cut-back requirements

Present law provides a remedial amendment period during which, under certain circumstances, a qualified retirement plan may be amended retroactively in order to comply with the qualification requirements.[66] In general, plan amendments to reflect changes in the law generally must be made by the time prescribed by law for filing the income tax return of the employer for the employer's taxable year in which the change in law occurs. The Secretary may extend the time by which plan amendments need to be made.

The Code and ERISA generally prohibit plan amendment that reduce accrued benefits, including amendments that eliminate or reduce optional forms of benefit with respect to benefits already accrued except to the extent prescribed in regulations.[67] This prohibition on the reduction of accrued benefits is commonly referred to as the "anti-cut-back rule."

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[64] Secs. 401(a)(29) and 436. Parallel rules apply under section 206(g)(3) of the Employee Retirement Income Security Act of 1974 (Pub. L. No. 93-406) ("ERISA"). Most governmental plans and church plans are excepted from these requirements and the anti-cut-back rule described below.

[65] A plan's funding target attainment percentage is the ratio, expressed as a percentage, that the value of the plan's assets (generally reduced by certain amounts attributable to contributions exceeding required contributions) bears to the plan's funding target for the year (that is the present value of benefits already earned under the plan). A plan's AFTAP is determined in the same way, except that the value of the plan's assets and the plan's funding target are both increased by the aggregate amount of purchases of annuities for employees other than highly compensated employees made by the plan during the two preceding plan years.

[66] Section 401(b).

[67] Section 411(d)(6) and ERISA section 204(g).

Description of Discussion Draft

In general

The proposal includes five basic modifications to the minimum distribution requirements:

- Applies the lifetime required minimum distribution rules to Roth IRAs,
- Increases the age used for determining an individual's required beginning date,
- Provides an exception from the minimum distribution requirements for individuals with aggregate retirement savings of $150,000 or less on a measurement date,
- Expands the beneficiaries subject to the five-year rule for required distributions after the death of an employee (or IRA owner),
- Changes the definition of required beginning date for five-percent owners, and
- Coordinates the minimum distribution requirements and the prohibited payment rule.

Lifetime required minimum distributions for Roth IRAs

Under the proposal, Roth IRA are subject to the same lifetime minimum distribution requirements as apply to traditional IRAs. For example, required distributions must begin on attainment of age 70½ (or, if later, the attainment of the individual's applicable age as described below).

Increase in the age used for determining required beginning date

The proposal raises the age used in determining an employee's (or IRA owner's) required beginning date in phases from age 70½ to age 73, and then provides further increases in the age to reflect increases in life expectancy. This is achieved by providing a new term, "applicable age," attained in a calendar year and basing the required beginning date on the first calendar year in which the employee attains the applicable age for that calendar year. For calendar years 2018 through 2022, the age is 71; for calendar years 2023 through 2027, the age is 72, for calendar year 2028, the age is 73. Beginning with calendar year 2029, the Secretary is required to adjust the applicable age annually in a manner proportional to increases in life expectancy. Therefore, the bill would increase the RMD age from 70½ to 71 in 2018. The age would be increased further to 72 in 2023, 73 in 2028 and, thereafter, would be adjusted in a manner proportional to increases in life expectancy.

In making this adjustment, the life expectancy of an individual who attains age 73 in the year preceding the year of the adjustment, is compared to the life expectancy of an individual who attains age 73 in 2027, determined on a unisex basis.[68] The applicable adjusted age for any calendar year is rounded down to the next whole number and, thus, is only increased when the adjusted age is increased by a whole year. In making this adjustment, the life expectancy of an

[68] The proposal specifies that the life expectancies underlying the tables described in section 430(h)(3)(A) used for the AFTAP calculation described above are also used in making these adjustments.

individual who attains age 73 in the year preceding the year of the adjustment, is compared to the life expectancy of an individual who attains age 73 in 2027, determined on a unisex basis.

Exemption for aggregate retirement savings of $150,000 or less

The proposal exempts an individual from the minimum distribution requirements if the aggregate value of the individual's account balances and accrued benefits under all IRAs (including Roth IRAs) and employer-sponsored tax-favored retirement plans ("aggregate retirement savings") does not exceed $150,000 (indexed for inflation) on a measurement date. However, benefits under qualified defined benefit pension plans that have already begun to be paid in life annuity form (including all forms of life annuity, such as joint and survivor, single, life and term certain) before the measurement date are excluded in determining aggregate retirement savings. The minimum distribution requirement would phase in ratably for individuals with aggregate retirement savings between $150,000 and $160,000 (both also indexed).

The initial measurement date for aggregate retirement savings is the first day of the calendar year in which the individual reaches age 70½ or, if earlier, the first day of the calendar year in which the individual dies, with additional measurement dates only at the beginning of the calendar year immediately following any calendar year in which the individual's IRAs or plans receive contributions, rollovers, or transfers of amounts that were not previously taken into account.

In the case of an IRA or defined contribution plan, the value of an individual's interest is the individual's account balance under the plan. The value of an individual's benefit under a defined benefit plan is the amount of the single sum payment (often referred to as a "lump sum") of the individual's full accrued benefit under the plan, if provided as a benefit option. If the plan does not offer a single sum distribution, the value is the minimum single sum allowed.[69]

Expansion of five-year after-death rule

General rule

Under the proposal, the five-year rule is the general rule for all distributions after death (regardless of whether the employee (or IRA owner) dies before, on, or after the required beginning date) unless the designated beneficiary is an eligible beneficiary as defined in the proposal. Thus, in the case of an ineligible beneficiary, distribution of the employee (or IRA owner's) entire benefit is required to be distributed by the end of the fifth calendar year following the year of the employee or IRA owner's death.

Eligible beneficiaries

For eligible beneficiaries, an exception to the five-year rule (for death before the required beginning date under present law) applies whether or not the employee (or IRA owner) dies

[69] See section 417(e) for the applicable interest rate and applicable morality assumptions for the minimum permissible single sum distribution.

before, on, or after the required beginning date. The exception (similar to present law) generally allows distributions over life or life expectancy of an eligible beneficiary beginning in the year following the year of death. Eligible beneficiaries includes any beneficiary who, as of the date of death (or in the case of a joint and survivor annuity, the annuity starting date for the employee or IRA owner), is the surviving spouse of the employee (or IRA owner),[70] is disabled, is a chronically ill individual, is an individual who is not more than 10 years younger than the employee (or IRA owner), or is a child of the employee (or IRA owner) who has not reached the age of majority. In the case of a child who has not reached the age of majority, calculation of the minimum required distribution under this exception is only allowed through the year that the child reaches the age of majority.

Further, under the proposal, the five-year rule also applies after the death of an eligible beneficiary or after a child reaches the age of majority. Thus, for example, if a disabled child of an employee (or IRA owner) is an eligible beneficiary of a parent who dies when the child is age 20 and the child dies at age 30, even though 52.1 years remain in measurement period,[71] the disabled child's remaining beneficiary interest must be distributed by the end of the fifth year following the death of the disabled child. If a child is an eligible beneficiary based on having not reached the age of majority before the employee's (or IRA owner's) death, the five-year rule applies beginning with the earlier of the date of the child's death or the date that the child reaches the age of majority. The child's entire interest must be distributed by the end of the fifth year following that date.

As under present law, if the surviving spouse is the beneficiary, a special rule allows the commencement of distribution to be delayed until the end of the year that the employee (or IRA owner) would have attained age 70½. If the spouse dies before distributions were required to begin to the spouse, the surviving spouse is treated as the employee (or IRA owner) in determining the required distributions to beneficiaries of the surviving spouse.

Definition of disabled and chronically ill individual

Under the proposal, disabled means unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to end in death or to be for long-continued and indefinite duration.[72] Further, under the definition, an individual is not considered to be disabled unless proof of the disability is furnished in such form and manner as the Secretary may require. Substantial gainful activity for

[70] As in the case of the present law special rule in section 401(a)(9)(B)(iv) for surviving spouses, spouse is not defined in the proposal. Under Treas. Reg. sec. 1.401(a)(9)-8, A-5, a spouse is the employee's spouse under applicable State law. In the case of a special rule for a surviving spouse, that determination is generally made based on the employee's marital status on the date of death. An exception is provided in Treas. Reg. sec. 1.401(a)(9)-6, A-6, under which a former spouse to whom all or a portion of the employee's benefits is payable pursuant to a qualified domestics relations order as defined in section 414(p) is treated as the employee's spouse (including a surviving spouse).

[71] The measurement period is the life expectancy of the child calculated for the child's age in the year after the employee's (or IRA owner's) death (age 21 (20 plus 1)).

[72] The definition of disabled in section 72(m)(7) is incorporated by reference.

this purpose is the activity, or a comparable activity, in which the individual customarily engaged prior to the arising of the disability (or prior to retirement if the individual was retired at the time the disability arose).[73]

Under the proposal, the definition of a chronically ill individual for purposes of qualified long-term care insurance[74] is incorporated by reference with a modification. Under this definition, a chronically ill individual is any individual who (1) is unable to perform (without substantial assistance from another individual) at least two activities of daily living for an indefinite period (expected to be lengthy in nature)[75] due to a loss of functional capacity, (2) has a level of disability similar (as determined under regulations prescribed by the Secretary in consultation with the Secretary of Health and Human Services) to the level of disability described above requiring assistance with daily living based on loss of functional capacity, or (3) requires substantial supervision to protect the individual from threats to health and safety due to severe cognitive impairment. The activities of daily living for which assistance is needed for purposes of determining loss of functional capacity are eating, toileting, transferring, bathing, dressing, and continence.

Defined benefit plans and annuities

The expansion of the five-year rule under the proposal applies to all after-death distributions under all retirement plans subject to the required minimum distribution requirements, including annuity distributions under defined benefit plans, and under annuity contracts purchased from insurance companies under defined contribution plans or IRAs. Thus, for example, under the proposal, after the death of an employee (or IRA owner), distribution in the form of a survivor life annuity (including a distribution that began before death as a joint and survivor annuity) is only permitted to an eligible beneficiary. In the case of a joint and survivor annuity that commences while the employee or IRA owner is alive, the determination of whether a beneficiary is an eligible beneficiary is made as of the annuity starting date for the employee or IRA owner rather than as of the date of death of the employee or IRA owner. Thus, any change in status, such due to a divorce or a recovery from a disability or a divorce, after annuity commencement and before the employee's (or IRA owner's) death does not prevent a beneficiary of the survivor portion of a joint and survivor annuity from being treated as an eligible beneficiary.

Required beginning date for five-percent owners

Under the proposal, if an employee becomes a five-percent owner after age 70½ (or the employee's applicable age if later) but before retiring and thus before the employee's required beginning date with respect to tax-favored retirement plans of the employee's employer, the

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[73] Treas. Reg. sec. 1.72-17(f). Under the regulations, in determining whether an individual is disabled, primary consideration is given to the nature and severity of the individual's impairment. However, consideration is also given to other factors such as the individual's education, training, and work experience. Whether an impairment in a particular case constitutes a disability is determined with reference to all the facts in the case.

[74] Section 7702B(c)(2).

[75] Section 7702B(c) only requires this period to be at least 90 days.

required beginning date for that employee becomes April 1 of the year following the year that the employee becomes a five-percent owner.

Coordination with prohibited payment limitations

Under the proposal, any required minimum distribution for an employee or beneficiary under a single-employer defined benefit plan for a period during which the plan is subject to the limitation on prohibited payments must not exceed the maximum payment allowable without violating the limitation on prohibited payments. The Secretary is directed to prescribe regulations for the application of this rule, including how this rule applies to required minimum distributions after the plan is no longer subject to this limitation.

Effective Date

Lifetime required minimum distributions from Roth IRAs

Under the proposal, the lifetime required minimum distributions rules apply to Roth IRAs for years beginning after December 31, 2016, but do not apply to any taxpayer who attains age 70½ on or before December 31, 2016.

Increase in age for required beginning date

The proposal applies for calendar years beginning after December 31, 2016.

Exemption for aggregate retirement savings of $150,000 or less

The proposal applies to initial measurement dates occurring on or after December 31, 2016.

Expansion of five-year after-death rule

General effective date

In determining required minimum distributions after the death of an employee (or IRA owner), the proposal is generally effective for required minimum distributions with respect to employees (or IRA owners) who die after December 31, 2016.

Delayed effective date for governmental and collectively bargained plans

In the case of a governmental plan (as defined in section 414(d)), in determining required minimum distributions after the death of an employee, the proposal applies to distributions with respect to employees who die after December 31, 2018.

In the case of a collectively bargained plan,[76] in determining required minimum distributions after the death of an employee, the proposal applies to distributions with respect to

[76] A collectively bargained plan is a plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers.

employees who die in calendar years beginning after the earlier of two dates. The first date is the later of (1) the date on which the last collective bargaining agreement ratified before date of enactment of the proposal terminates,[77] or (2) December 31, 2016. The second date is December 31, 2018.

In the case of any distribution from a governmental or collectively bargained plan to an ineligible beneficiary with respect to any employee who dies after December 31, 2016 but before January 1, 2018 (or such earlier effective date as may apply under a collectively bargained plan), any amount distributed after the end of the fourth calendar year after the date of death of the employee is not eligible for rollover to an IRA.[78] Any amount distributed from an employer-sponsored retirement plan that is rolled over to an IRA is subject to the required minimum distribution rules for the IRA as amended by this proposal.

Five-year rule after the death of a beneficiary

In the case of an employee (or IRA owner) who dies before the effective date (as described below) for the plan (or IRA), if the designated beneficiary of the employee (or IRA owner) dies on or after the effective date, the proposal applies to any beneficiary of the designated beneficiary as though the designated beneficiary were an eligible beneficiary. Thus, the entire interest must be distributed by the end of the fifth calendar year after the death of the designated beneficiary. For this purpose, the effective date is the date of death of the employee (or IRA owner) used to determine when the proposal applies to the plan (or IRA), for example, before January 1, 2017 under the general effective date.

Certain annuities grandfathered

The modification to the after-death minimum distribution rules does not apply to a qualified annuity that is a binding annuity contract in effect on the date of enactment of the proposal and at all times thereafter. A qualified annuity with respect to an employee (or IRA owner) is a commercial annuity,[79] or an annuity payable by a defined benefit plan, under which the annuity payments are made over the lives of the employee (or IRA owner) and a designated beneficiary (or over a period not extending beyond the life expectancy of the employee (or IRA owner) or the life expectancy of the employee (or IRA owner) and a designated beneficiary) in accordance with the required minimum distribution regulations for annuity payments as in effect

[77] The date that the last agreement terminates is determined without regard to any extension thereof agreed to on or after the date of enactment of this proposal. Further, any plan amendment made pursuant to a collective bargaining agreement relating to the plan that amends the plan solely to conform to any requirement added by this proposal shall not be treated as a termination of the collective bargaining agreement.

[78] Sections 402(c)(11), 403(b)(8), and 457(e)(16) allow a designated beneficiary under an employer-sponsored eligible retirement plan to rollover in a direct trustee-to trustee transfer an eligible rollover distribution from the plan to an inherited IRA. Section 402(c)(4)(B) defines an eligible rollover distribution as not including any required minimum distribution. Notice 2007-7, 2007-1 C.B. 395, A-17 through A-19, provides guidance on determining the amount of any distribution to a designated beneficiary that is a required minimum distribution and thus not eligible for rollover.

[79] For this purpose, commercial annuity is defined in section 3405(e)(6).

TITLE III – ANTI-ABUSE RULES RELATING TO IRAS

A. Valuation of IRA Investment Assets

Present Law

Limit on IRA investments and prohibited transactions

Present law prohibits the assets of an IRA[80] from being invested in collectibles.[81] For this purpose, collectible generally means a work of art, a rug or antique, a metal or gem, a stamp or coin, an alcoholic beverage, or certain other tangible personal property.[82] The acquisition of a collectible by an IRA is treated as a distribution from the IRA in an amount equal to the cost of the collectible.

The Code prohibits various transactions ("prohibited transaction") between certain tax-favored savings arrangements (referred to as plans) and disqualified persons.[83] Prohibited transactions include some transactions between an IRA and an IRA owner.[84] Although a prohibited transaction generally results in an excise tax, in the case of an IRA owner, a prohibited transaction generally results in the loss of tax-favored treatment as an IRA and income inclusion as if all the assets in the IRA were distributed.[85]

Qualified appraisal requirements for charitable deductions

Present law generally allows an income tax deduction for charitable contributions, including contributions of property, subject to verification, record-keeping and documentation requirements in some cases.[86] In the case of a contribution of property for which a deduction of more than $5,000 is claimed, a taxpayer must obtain a qualified appraisal of the property and include with the income tax return information about the property and the appraisal summary as

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[80] The prohibition on investments in collectibles under present law, and the proposal, apply to individual retirement accounts under section 408(a) (including an interest in a trust treated as an individual retirement account under section 408(c)), not to individual retirement annuities under section 408(b). When used in the description of the proposal below, "IRA" refers only to an individual retirement account and does not include an individual retirement annuity.

[81] Sec. 408(m). The prohibition on the acquisition of collectibles and deemed distribution in the amount of the cost of the collectible apply also to an individually-directed account under a qualified retirement plan under section 401(a).

[82] Under section 408(m)(3), certain coins and bullion are excepted from the definition of collectible.

[83] Sec. 4975. See Part III.D for further discussion of the prohibited transaction rules.

[84] As used herein, IRA owner refers to the individual for whose benefit the IRA is maintained, including a spouse or former spouse to whom an interest in an IRA is transferred under section 408(d)(6) or the beneficiary of an inherited IRA as described in section 408(d)(3)(C).

[85] Sec. 408(e)(2).

[86] Sec. 170(a).

required by the Secretary.[87] In the case of a contribution of property for which a deduction of more than $500,000 is claimed, a taxpayer must include the qualified appraisal with the income tax return.

For this purpose, a qualified appraisal means an appraisal document that, among other features, (1) relates to an appraisal made not earlier than 60 days before the date of contribution of the appraised property and not later than the due date (including extensions) of the return on which a deduction is first claimed; (2) is prepared, signed, and dated by a qualified appraiser; and (3) includes a detailed description of the property appraised, the appraised fair market value of the property, the valuation method used to appraise the property and the specific basis for the valuation, a statement that the appraisal was prepared for income tax purposes, the qualifications of the qualified appraiser (that is, background, experience, education and any membership in professional appraisal associations), and the signature and taxpayer identification number of the appraiser.[88] A qualified appraiser is an individual who has earned an appraisal designation from a recognized professional appraiser organization or has otherwise met minimum education and experience requirements under Treasury regulations, regularly performs appraisals for which the individual receives compensation, and meets such other requirements as may be prescribed in regulations or other guidance.[89] In addition, an individual is not treated as a qualified appraiser with respect to a specific appraisal unless the individual demonstrates verifiable education and experience in valuing the type of property subject to the appraisal and the individual has not been prohibited from practicing before the Internal Revenue Service ("IRS") at any time during the three-year period ending on the date of the appraisal.[90]

Description of Discussion Draft

The proposal prohibits any IRA funds from being invested in an asset acquired for less than fair market value and prescribes how fair market value is determined. If, during any taxable year of an IRA owner, the assets of the IRA are invested in a manner that does not comply with the proposal, the IRA ceases to be an IRA as of the first day of the taxable year. In that case, an amount is included in income, determined as if there were a distribution on the first day of the

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[87] Sec. 170(f)(11). Contributions of certain readily valued property, such as publicly traded securities, are not subject to these requirements.

[88] Treas. Reg. sec. 1.170A-13(c)(3). The regulations provide that an appraiser who falsely or fraudulently overstates the value of the contributed property in a qualified appraisal that the appraiser has signed may be subject to a civil penalty under section 6701 for aiding and abetting an understatement of tax liability. Section 6695A also provides for a penalty if (1) a person prepares an appraisal and the person knows, or reasonably should have known, that the appraisal would be used in connection with a return or a claim for refund, and (2) the claimed value of the property on a return or refund claim based on the appraisal results in a substantial valuation misstatement under within the meaning of section 6662(e), a substantial estate or gift tax valuation understatement within the meaning of section 6662(g), or a gross valuation misstatement within the meaning of section 6662(h), with respect to the property.

[89] Sec. 170(f)(11)(E).

[90] Practice before the IRS is subject to regulation under 31 U.S.C. sec. 330.

taxable year in an amount equal to the fair market value (as of that day) of all the assets in the IRA as of that day.

For purposes of the proposal, fair market value means--

- in the case of a security, including a foreign security, for which there is a generally recognized market, (1) the price of the security prevailing (as of the date of the acquisition of the security by the IRA) on a recognized foreign, national, or regional exchange or over-the-counter market in which quotations are published on a daily basis, or (2) a price not more favorable to the IRA than the offering price for the security established by the bid and ask prices quoted, as of the date of the acquisition by the IRA, by persons independent of the IRA owner,
- in the case of a security issued by an investment company registered under the Investment Company Act of 1940 that is not traded on a securities exchange, the price reported by the investment company,
- in the case of a security or other instrument issued by a bank or insurance company subject to supervision or periodic examination by a Federal or State authority, the price at which the security or other instrument is offered publicly for sale in the ordinary course of the business of the bank or insurance company, and
- in the case of any other asset the value determined by means of a qualified appraisal (as defined under the charitable deduction rules), except as otherwise provided in regulations prescribed by the Secretary.

In the case of an asset, the value of which is required to be determined by means of a qualified appraisal, the IRA owner must include on his or her tax return for a taxable year in which the asset is acquired any information that the Secretary may require. The required information may include a description of the property and the name, title, business address, and taxpayer identifying number of the qualified appraiser who conducted the appraisal.

The proposal grants the Secretary authority to issue regulations or guidance as the Secretary determines appropriate to provide rules for the valuation of assets for purposes of the proposal and for simplified methods of compliance with the proposal.

Effective Date

The proposal applies to taxable years beginning after December 31, 2017.

B. Statute of Limitations with Respect to IRA Noncompliance

Present Law

In general, in order for the IRS to assess a tax, the tax must be assessed within three years after the return to which the tax relates was filed (referred to as the statute of limitations on assessment), regardless of whether the return is filed by the due date for the return.[91] For this purpose, a return filed before the due date for the return is treated as filed on the due date.[92]

In some cases, a longer statute of limitations applies. For example, the statute of limitations is six years after an income tax return is filed if the taxpayer omits an amount of includible income exceeding 25 percent of the income shown on the return.[93] If certain information required to be included with a return is not so included, the statute of limitations may be determined by reference to the date when the information is provided to the IRS, rather than when the return was filed.[94] In addition, in some cases in which a tax results from a particular transaction, the statute of limitations may be determined by reference to the date when the IRS is notified of the transaction, rather than when the return was filed.[95]

Description of Discussion Draft

The proposal extends the statute of limitations in certain cases relating to IRAs and prohibited transactions.[96] In the case of a substantial error (willful or otherwise) in the reporting of any information relating to the valuation of investment assets of an IRA, the time for assessment of any tax or increase in tax with respect to the plan will not expire before the date that is six years after the return is filed (whether or not the return is filed on or after the due date for the return). In addition, the time for assessment of any tax imposed by reason of a prohibited transaction will not expire before the date that is six years after the return is filed (whether or not the return is filed on or after the due date).

Effective Date

The proposal applies to taxes with respect to which the three-year statute of limitations otherwise applicable under present law ends after December 31, 2016.

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[91] Sec. 6501(a). Under section 6501(c)(3), in the case of a failure to file a return, tax may be assessed at any time.

[92] Sec. 6501(b)(1).

[93] Sec. 6501(e)(1).

[94] See, for example, sec. 6501(c)(10), relating to listed transactions.

[95] See, for example, sec. 4979A(e)(2)(D), relating to certain prohibited allocations of employer securities under an employee stock ownership plan.

[96] See Part III.D for a discussion of the prohibited transaction rules.

C. Prohibition of Investment of IRA Assets in Entities in Which the IRA Owner Has a Substantial Interest

Present Law

Limit on IRA investments and prohibited transactions

As discussed above, present law prohibits the assets of an IRA[97] from being invested in collectibles. For this purpose, collectible generally means a work of art, a rug or antique, a metal or gem, a stamp or coin, an alcoholic beverage, or certain other tangible personal property. The acquisition of a collectible by an IRA is treated as a distribution from the IRA in an amount equal to the cost of the collectible.

The Code prohibits various transactions ("prohibited transaction") between certain tax-favored savings arrangements (referred to as plans) and disqualified persons, including some transactions between an IRA and an IRA owner. Although a prohibited transaction generally results in an excise tax, in the case of an IRA owner, a prohibited transaction generally results in the loss of tax-favored treatment as an IRA and income inclusion as if all the assets in the IRA were distributed.

Description of Discussion Draft

The proposal prohibits any IRA funds from being invested in an entity in which the IRA owner has an interest of 10 percent or more. Specifically, no IRA funds may be invested in a corporation, partnership or other unincorporated enterprise, or trust or estate, 10 percent or more of which is owned (directly or indirectly) or held by the IRA owner. For this purpose, an interest is measured by reference to (1) in the case of a corporation, the combined voting power of all classes of stock entitled to vote or the total value of shares of all classes of stock of the corporation, (2) in the case of a partnership or other enterprise, the capital interest or profits interest in the partnership or enterprise, and (3) in the case of a trust or estate, the beneficial interest in the trust or estate.

In determining ownership for purposes of the proposal, constructive ownership rules apply.[98] For example, an individual is treated as owning interests held by certain family members, defined for this purpose as the individual's spouse, ancestors, lineal descendants, and spouses of lineal descendants. In addition, any interest held by the IRA is treated as held by the IRA owner. Thus, an interest held by the IRA and an interest held by the IRA owner, as well as any constructively owned interest, are combined for purposes of the proposal.

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[97] The prohibition on investments in collectibles under present law, and the proposal, apply to individual retirement accounts under section 408(a) (including an interest in a trust treated as an individual retirement account under section 408(c)), not to individual retirement annuities under section 408(b). When used in the description of the proposal below, "IRA" refers only to an individual retirement account and does not include an individual retirement annuity.

[98] The proposal incorporates the constructive ownership rules under section 4975(e)(4) and (5), which refer to the rules of section 267(c), but using the definition of family members under section 4975(e)(6).

If, during any taxable year of an IRA owner, the assets of the IRA are invested in an entity in which the IRA owner has an interest of 10 percent or more, the IRA ceases to be an IRA as of the first day of the taxable year. In that case, an amount is included in income, determined as if there were a distribution on the first day of the taxable year in an amount equal to the fair market value (as of that day) of all the assets in the account as of that day.

Effective Date

The proposal applies to apply to investments made in taxable years beginning after December 31, 2016.

D. IRA Owners Treated as Disqualified Persons for Purposes of Prohibited Transactions Rules

Present Law

Prohibited transaction rules - in general

The Code prohibits various transactions ("prohibited transaction") between certain tax-favored savings arrangements (referred to as plans) and disqualified persons.[99] Among the arrangements to which the prohibited transaction rules apply are employer-sponsored qualified retirement plans[100] and traditional and Roth IRAs.[101]

Prohibited transactions include the following transactions, whether direct or indirect, between a plan and a disqualified person: (1) the sale or exchange or leasing of property, (2) the lending of money or other extension of credit, (3) the furnishing of goods, services or facilities, (4) the transfer to, or use by or for the benefit of, the income or assets of the plan, (5) in the case of a fiduciary, an act dealing with the plan's income or assets in the fiduciary's own interest or for the fiduciary's own account, and (6) the receipt by a fiduciary of any consideration for the fiduciary's own personal account from any party dealing with the plan in connection with a transaction involving the income or assets of the plan.[102]

Consequences of prohibited transactions

If a prohibited transaction occurs, in general, the disqualified person who participated in the transaction is subject to a two-tiered excise tax. The first-tier tax is 15 percent of the amount involved in the transaction. The second-tier tax, imposed if the prohibited transaction is not corrected within a certain period, is 100 percent of the amount involved.

For purposes of the excise tax, the amount involved with respect to a prohibited transaction is generally the greater of (1) the amount of money and the fair market value of the other property given, or (2) the amount of money and the fair market value of the other property received. For purposes of the excise tax, "correction" and "correct" mean, with respect to a prohibited transaction, undoing the transaction to the extent possible, but in any case placing the

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[99] Sec. 4975.

[100] Sections 401(a) and 403(a) provide the requirements for qualified retirement plans. Governmental plans and church plans are exempt from the prohibited transaction rules under section 4975. However, under section 503, the trust holding assets of a governmental or church plan may lose its tax exempt status in the case of a prohibited transaction listed in section 503(b).

[101] These are included in the definition of "plan" under section 4975(e)(1). Also included are Archer MSAs under section 220, health savings accounts under section 223, and Coverdell education savings accounts under section 530.

[102] Sec. 4975(c)(1). Under section 4975(d), certain transactions are statutorily exempt from prohibited transaction treatment. In addition, under section 4975(c)(2), an administrative exemption may be granted, on either an individual or class basis, subject to a finding that the exemption is administratively feasible, in the interests of the plan and of its participants and beneficiaries, and protective of the rights of participants and beneficiaries of the plan.

plan in a financial position not worse than that in which it would be if the disqualified person were acting under the highest fiduciary standards.

In the case of a prohibited transaction engaged in with respect to an IRA by the IRA owner during a taxable year, rather than application of the excise tax, the IRA ceases to be an IRA as of the first day of the taxable year.[103] In that case, an amount is included in income, determined as if there were a distribution on the first day of the taxable year in an amount equal to the fair market value (as of that day) of all the assets in the account as of that day.

Disqualified persons

A disqualified person is (1) a fiduciary; (2) a person providing services to the plan; (3) an employer any of whose employees are covered by the plan; (4) an employee organization any of whose members are covered by the plan; (5) a direct or indirect owner of an interest of 50 percent or more in the employer or employee organization; or (6) a corporation, partnership, or trust or estate of which (or in which) an interest of 50 percent or more is held directly or indirectly by a person described in (1), (2), (3), (4) or (5).[104] The following are also disqualified persons based on a relationship to a person described in (1) through (5) as follows:

- a member of the family of an individual described in (1), (2), (3) or (5);
- officers and directors (or individuals having powers or responsibilities similar to those of officers or directors), 10-percent or more shareholders, or highly compensated employees of a person described in (3), (4), (5) or (6); and
- a 10-percent or more (in capital or profits) partner or joint venturer of a person described in (3), (4), (5) or (6).

In determining ownership of a corporation or partnership for purposes of these rules, constructive ownership rules apply.[105] For example, an individual is treated as owning interests held by certain family members. In addition, for purposes of the prohibited transaction rules, members of an individual's family are the individual's spouse, ancestors, lineal descendants, and spouses of lineal descendants.[106]

A fiduciary is any person who: (1) exercises any authority or control respecting management or disposition of the plan's assets; (2) renders investment advice for a fee or other

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[103] Secs. 408(e)(2) and 4975(c)(3). This treatment applies also to an interest in a trust treated as an individual retirement account under section 408(c).

[104] Sec. 4975(e)(2). The 50-percent standard described in (5) above applies to (1) in the case of a corporation, the combined voting power of all classes of stock entitled to vote or the total value of shares of all classes of stock of a corporation, (2) in the case of a partnership, the capital interest or profits interest of the partnership, or (3) in the case of a trust or estate, the beneficial interest of the trust or estate.

[105] Under section 4975(e)(4) and (5), the constructive ownership rules of section 267(c) generally apply.

[106] Sec. 4975(e)(6).

compensation with respect to any plan moneys or property, or has the authority or responsibility to do so; or (3) has any discretionary authority or responsibility in the administration of the plan.

An IRA owner may be a fiduciary, and therefore a disqualified person, with respect to an IRA as a result of authority to control the investment of the assets in the IRA (a "self-directed IRA").[107] However, an IRA owner is not statutorily defined as a disqualified person with respect to the IRA. As a result, transactions between an IRA and the IRA owner of the type described in the prohibited transaction rules might not always be treated as prohibited transactions.

Description of Discussion Draft

The proposal modifies the statutory definition of disqualified person to specifically provide that an IRA owner is a disqualified person with respect to the IRA (regardless of whether the IRA owner would be a disqualified person on another basis). In addition, the following are treated as disqualified persons: (1) a family member of the IRA owner; (2) a corporation, partnership, or trust or estate in which an interest of 50 percent or more is held directly or indirectly by the IRA owner; and (3) a 10-percent or more (in capital or profits) partner or joint venturer of the IRA owner. The constructive ownership rules applicable under present law apply for purposes of the proposal. Moreover, for purposes of (2) and (3), any interest held by the IRA is treated as held by the IRA owner. Thus, an interest held by the IRA and an interest held by the IRA owner, as well as any constructively owned interest, are combined for those purposes.[108]

Effective Date

The proposal applies to transactions occurring after December 31, 2016.

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[107] See Department of Labor Advisory Opinion 89-12A (July 14, 1989).

[108] The proposal also revises section 408(e)(2) to clarify that it applies to the individual for whose benefit an IRA is maintained, that is, the IRA owner as used herein.