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NRS
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NEWSLETTER

NEW ELECTRONIC FILING GLITCH: TIMELY FILED, PROCESSED LATE

As some readers are aware, the electronic filing due date for the 2009 calendar year Form 5500 Series was August 2, 2010 (July 31 fell on a Saturday). More precisely, the due date was midnight at the conclusion of August 2, 2010 in the Plan Administrator's time zone. Unfortunately for some Plan Administrators, the United States Department of Labor (DOL) takes the position that the Form 5500 must have been *processed* by that midnight due date in order to avoid financial penalties. This creates issues for last minute filers.

For example, suppose the Form is complete and the Plan Administrator (or his delegate) attempts to file it before midnight, but the transmission fails. Although a retransmission is completed successfully a few minutes later, the transmission is processed past the midnight deadline. As a second example, suppose the filing cannot be processed due to a flaw in the data. By the time the flaw is corrected, the filing is accepted by DOL after the due date. Of course, it is also possible for the DOL computer to encounter processing delays and simply accept the filing later than the time it was filed.

Anyone who files the 5500 Series Form is well advised to save a copy of the transmission report documenting that the Form was timely filed. This can come in handy in the event the DOL or IRS contend that the Form was filed late and so wish to assess penalties. Individuals reporting for plans with more than one participant who suspect they may run afoul of the deadline have an option. If they either do not have a good excuse or do not want to go through the hassle, the Form can be filed under the Delinquent Filer Voluntary Compliance ("DFVC") program. This strategy reduces the $25 per day penalty to $10 per day, with a much smaller maximum penalty, and it can be filed electronically.

DEATH BENEFITS TO NON-SPOUSE BENEFICIARIES: IT'S COMPLICATED

Paying death benefits from tax qualified defined contribution retirement plans has never been simple, but recent developments have added a new layer of complexity, particularly when the beneficiary is someone other than the deceased participant's spouse. This article focuses on issues that arise when the deceased participant named a beneficiary such as a parent, child, sibling, or a domestic partner. Benefits to surviving spouses represent a different set of rules designed to offer the surviving spouse more flexibility than other individuals named as beneficiaries and these rules are not covered here.

TWO DISTRIBUTION CHOICES FOR BENEFICIARIES:

Minimum distribution rules that normally come into play only after a participant reaches age 70½, have a definite impact on non-spousal beneficiaries (referred to simply as "beneficiaries" in this article). Two basic alternatives are offered to the beneficiary under the minimum distribution rules: (a) take out the entire benefit in the five calendar years immediately following the participant's death, or (b) arrange to receive roughly level installments over your life expectancy (the "life expectancy" method). The rules are very exact: if payments under the life expectancy method do not begin in the calendar year immediately following the year of the participant's death, the beneficiary must receive his or her entire interest by the last day of the fifth calendar year immediately following the participant's death. Failure to take the benefit within these time frames exposes the beneficiary to an excise tax equal to 50% of the missed payment. This can result in loss of half the entire inheritance if benefits are not paid out timely. Since failure to make timely payments can result in penalties to both the beneficiary and the plan, careful plan administration is a must.

The 2009 "Holiday" for required minimum distributions applies to beneficiaries as well as to living participants. For example, the beneficiary of a participant who died in 2008 has until the end of 2010 to initiate life expectancy payments and until the end of 2014 to receive all of his or her benefits if no life expectancy payments are initiated.

LIFE EXPECTANCY DISTRIBUTION CALCULATION METHODOLOGY:

Beneficiaries that choose the life expectancy distribution method must determine their single life expectancy per

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government published tables based on their age in the calendar year following the year of the participant's death. This number is divided into the participant's account balance at the end of the calendar year of death, thus determining the amount of the beneficiary's distribution for the first year. Subsequent annual payments are determined by reducing the previous year's life expectancy by one year and dividing that number into the account balance at the end of the immediately prior year. Payments continue in this manner until the account is exhausted. If the beneficiary dies before receiving the entire benefit, annual payments continue to the beneficiary's designated beneficiary; but the original life expectancy numbers continue to be used.

The above illustrates that a retirement plan need not have the same method of distribution for the benefits of all employees/participants.

TAX DEFERRED ROLLOVER: THE INHERITED IRA:

Non-spouse beneficiaries are allowed to roll over plan benefits to either a Roth IRA or a Traditional IRA. All plans are required to permit this option starting in 2010. Between 2007 and 2009, plans were permitted to offer this provision on a voluntary basis. The inherited IRA must be funded by direct payments from the Plan; the "60 day" rollover rule does not apply. Furthermore, an inherited IRA rollover must occur no later than the end of the *fourth* calendar year after the participant's death.

Many plans (including the majority of plans where NRS influenced the plan design) limit non-spousal death benefit distributions to five years. This provision avoids the administrative burden of payments to non-employees continuing for a period of many years. However, it raises issues for a beneficiary who wants to receive benefits under the life expectancy option because Plan payments cannot continue beyond five years. This dilemma is solved by a special tax provision: if a beneficiary rolls over the account to an inherited IRA by the close of the calendar year immediately following the participant's year of death, the beneficiary is permitted to use the life expectancy method for distributions from the IRA and thus delay taxable distributions beyond five years.

While defined contribution plan administration does not often involve handling benefit distributions for non-spouse beneficiaries, these situations do arise periodically and present unique administrative issues with substantial financial consequences.

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