MEMO# 9327

October 10, 1997

# CHAIRMAN'S MARK OF THE TAX TECHNICAL CORRECTIONS ACT OF 1997

[9327] VIA FAX October 10, 1997 TO: PENSION COMMITTEE No. 40-97 PENSION OPERATIONS ADVISORY COMMITTEE No. 39-97 RE: CHAIRMAN’S MARK OF THE TAX TECHNICAL CORRECTIONS ACT OF 1997

______________________________________________________________________ The House Ways and Means Committee yesterday approved by voice vote the Tax Technical Corrections Act of 1997. The purpose of this bill is to make various technical corrections to previously enacted tax legislation, primarily the Taxpayer Relief Act of 1997 (TRA ‘97). This memorandum summarizes the pension-related provisions in the Committee’s bill. The attachment to this memorandum contains pension-related excerpts from the Chairman’s mark, including the description report and the statutory language. The Committee also approved by a 19-17 roll call vote a separate bill that would (1) increase the maximum annual contribution to an Education IRA from $500 to $2,500 and (2) permit withdrawals from Education IRAs for educational expenses relating to kindergarten through grade 12 education. This separate bill is expected to be strongly opposed by the Clinton Administration. I. Roth IRA (See Section 5(b) of the bill.) A. The bill would modify current rules for distributions from conversion Roth IRAs within the 5-year period following the conversion by subjecting the amounts includible in income due to the conversion to (1) the 10 percent early withdrawal penalty under section 72(t) and, (2) for 1998 conversions, an additional 10 percent penalty. Further, amounts withdrawn from conversion Roth IRAs during the 5-year period following the conversion would be deemed to come first from amounts includible in income, i.e., the "contributions first" rule is suspended for withdrawals made from conversion Roth IRAs under these circumstances. The description report states that it is anticipated that appropriate forms will be developed to clearly differentiate Roth Conversion IRAs from other Roth IRAs and for taxpayers that make conversions in more than one year, to differentiate Roth Conversion IRAs for different years. Special rules would apply in circumstances where separate Roth IRAs are not maintained. In the case where a Roth IRA account commingles conversion and contribution amounts from more than one year, the 5-year aging period would - 2 - begin with the most recent taxable year for which a conversion contribution was made. For distribution purposes, all Roth IRAs with the same 5-year holding period would be aggregated. B. The bill provides an error correction mechanism for Roth IRA conversions and contributions. Contributions to an IRA (and earnings thereon) may be transferred from any IRA to another IRA by the due date of the taxpayer’s return for the year of contribution, including extensions. The transferred contributions will be treated as if contributed to the transferee IRA and not the transferor IRA. C. The bill addresses the effect of the death of the taxpayer during the 4-year spread period for 1998 conversions to a Roth IRA. Under the bill, any amounts remaining may be included in income on the final return of the taxpayer. If the surviving spouse is the beneficiary, the spouse could continue the deferral by including the remaining amounts in his or her income over the remainder of the 4-year period. II. IRA Expansion A. The bill provides that hardship distributions from cash or deferred arrangements are not eligible rollover distributions, may not be rolled over to any IRA and are not subject to the 20 percent withholding rule. (See Section 5(c) of the bill.) B. The bill clarifies that the AGI phase-out range for the maximum Roth IRA contribution for a married taxpayer filing separate return is $0 - $10,000. (See Section 5(b) of the bill.) C. The bill clarifies the intent of the TRA ‘97 to allow an individual to contribute up to $2,000 a year to all the individual’s IRAs. (See Section 5(b) of the bill.) D. The bill clarifies that the AGI phase-out range for maximum deductible IRA contributions for married individuals who are active participants in employer- sponsored plans will be increased to $80,000 - $100,000 in 2007, but that the AGI phase-out limits applicable to individuals who are not active participants and whose spouses are active participants, are $150,000 - $160,000. (See Section 5(a) of the bill.) III. Education IRA and Other Education Tax Incentives A. The bill clarifies that (1) consistent with the legislative history of TRA '97, balances remaining in an Education IRA when the beneficiary attains the age of 30 will be deemed to be distributed within 30 days after that date; (2) the 10% penalty that applies to nonqualified distributions from an Education IRA does not apply to the distribution of any contribution made during a taxable year if it is distributed on or before the date a return is required to be filed (including extensions of time) by the beneficiary for the taxable year in which the - 3 - contribution was made, and in cases where the beneficiary is not required to file a return, by April 15th of the year following the taxable year; (3) Education IRA distributions are treated as representing a pro-rata share of principal and earnings in the account; and (4) taxpayers may redeem U.S. Savings Bonds, contribute the proceed to an Education IRA and retain eligibility for the present- law Code section 135 exclusion. (See Sections 4(b) and (c) of the bill.) B. The bill clarifies the following aspects of the HOPE and Lifetime Learning Credit programs: (1) the manner in which the HOPE tax credit amount is indexed for inflation and (2) the information reporting obligations of educational institutions and taxpayers regarding payments of qualified tuition and related expenses under these programs. (See Section 4(a) of the bill.) IV. SIMPLE Plan Provisions The bill clarifies that uniform coverage rules similar to those of Code section 410(b)(6)(C)(i)(II) must be satisfied for a SIMPLE plan maintained in the case of mergers and acquisitions to remain "qualified" for the year of the transaction and the two following years. (See Section 15 of the bill.) V. Miscellaneous Pension Items The following miscellaneous items also are addressed in the bill: (1) The TRA ’97 provision relating to the treatment of partnership items of individual retirement accounts is clarified to provide that it applies to partnerships taxable beginning after December 31, 1997; and (2) the TRA ’97 provision permitting employees participating in certain 403(b) annuity contracts purchased by an Indian tribal government to rollover contract amounts into a 401(k) plan is clarified to permit similar rollover treatment for 403(b)(7) custodial accounts. Russell G. Galer Assistant Counsel - Pension Kathryn A. Ricard Assistant Counsel - Pension Attachment (in .pdf format)

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