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## Summary of Recent Legislative Changes Affecting Individual Retirement Arrangements

Recent developments have spawned a variety of targeted legislative changes to the rules that govern individual retirement arrangements (“IRAs”). Specifically, the Heroes Earnings Assistance and Relief Tax Act of 2008 (“HEART Act”) enacted a number of changes designed to benefit those in military service, and the Tax Extenders and Alternative Minimum Tax Relief Act of 2008 (“TEAMTRA”) (which was enacted as part of the Fall 2008 economic stimulus package) and the Worker, Retiree, and Employer Recovery Act of 2008 (“WRERA”) contained several provisions designed to assist those affected by the economic downturn. The following is a brief summary of these legislative changes.<sup>1</sup>

### Heroes Earnings Assistance and Relief Tax Act of 2008

- **Military Service Differential Wage Payments.** Military service differential wage payments are treated as compensation for purposes of (i) determining the maximum amount of contributions that an individual can make to his or her IRA and (ii) any employer contributions to an individual’s Simplified Employer Pension (“SEP”) IRA or SIMPLE IRA. A differential wage payment is any payment made by an employer to an individual who is in uniformed military service during a period of active duty of more than 30 days that represents all or part of the compensation that the individual would have received from the employer had the individual continued to work for the employer during the period of uniformed service. This provision is effective January 1, 2009.
- **Permanent Extension of Qualified Reservist Distribution Provision.** The Pension Protection Act of 2006 (“PPA”) permitted individuals in the military reserve who are called to active duty for a period in excess of 179 days (or for an indefinite period) to take penalty-free withdrawals from IRAs and 401(k) plans. The PPA further permitted an individual who received such a distribution to return the distribution to his or her IRA during the two-year period beginning on the date after the period of active duty ends. The provision was originally enacted to expire with respect to any period of active duty that begins on or after December 31, 2007. The HEART Act eliminated the expiration date. This provision will, therefore, continue to apply to reservists who are prospectively called to active duty.

<sup>1</sup> The TEAMTRA also includes a provision permitting contributions of Exxon Valdez litigation settlement proceeds to IRAs, and the WRERA includes a provision permitting contributions of amounts received by employees of bankrupt airline carriers to Roth IRAs. These provisions are narrowly targeted and are not summarized in this Alert.

- Contributions of Military Death Gratuities to Roth IRAs. An individual who receives a death gratuity as a result of the death of an individual in military service may, within one year following receipt of the gratuity, contribute the gratuity to a Roth IRA. The contribution is not counted against the contribution limits otherwise applicable to Roth IRAs. The provision applies to deaths from injuries occurring on or after October 7, 2001. In the case of deaths or injuries occurring between October 7, 2001 and June 17, 2008, the contribution deadline is extended to June 17, 2009.
- SEP IRA and SIMPLE IRA Benefit Accruals for Military Service Members Who Die or Become Disabled During Military Service. An employer that contributes to an employee's SEP IRA or SIMPLE IRA may treat an employee who dies or becomes disabled during uniformed military service as having been reemployed on the date before the employee's death or disability. An employer that does so would then be obligated to provide the benefits that would have accrued to the employee during the period of military service. An employer that takes advantage of this provision must do so on a reasonably equivalent basis for all employees who die or become disabled during uniformed military service. This provision is effective for deaths and disabilities occurring on or after January 1, 2007.

### **Tax Extenders and Alternative Minimum Tax Relief Act of 2008**

- Extension of PPA Charitable IRA Distribution Provision. The PPA excluded from an individual's gross income up to \$100,000 of any IRA distribution made directly to a charitable organization after the IRA owner attains age 70-1/2, provided that the distribution would otherwise be deductible as a charitable contribution, determined without regard to the generally applicable percentage limitations on such deductions. This provision originally expired on December 31, 2007. The

TEAMTRA retroactively extends this provision through December 31, 2009.

### **Worker, Retiree, and Employer Recovery Act of 2008**

- 2009 Required Minimum Distribution Waiver. The WRERA waives the requirement that an IRA owner or beneficiary receive required minimum distributions for 2009. The WRERA also provides that calendar year 2009 is not included in the measurement of the five-year period during which nonspouse IRA beneficiaries must receive non-annuitized distributions following the death of the IRA owner.
- Clarification of Roth-to-Roth Rollover Rules. Prior to January 1, 2010, an individual is eligible to make a rollover contribution to a Roth IRA only if the individual's adjusted gross income is \$100,000 or less and, if married, only if the individual and his or her spouse file a joint return. The WRERA clarifies that these limitations do not apply to rollovers of distributions from other Roth IRAs or from Roth 401(k) plans. (Note: The Tax Increase Prevention and Reconciliation Act (enacted on May 17, 2006) eliminates the adjusted gross income and joint filing requirements for rollovers to Roth IRAs from non-Roth arrangements effective January 1, 2010.)
- Nonspouse Beneficiary Inherited IRA Rollovers Are Mandatory. The PPA included a provision that permits nonspouse beneficiaries in tax-qualified retirement plans to roll over certain distributions to inherited IRAs. The Internal Revenue Service interpreted this provision to be optional—i.e., an employer that sponsors a tax-qualified retirement plan could choose whether to make this rollover opportunity available to nonspouse beneficiaries. The WRERA requires that this opportunity be made available for plan years beginning after December 31, 2009.

- Withdrawals of Automatic Contributions to SEP IRAs and SIMPLE IRAs. The PPA enacted a variety of provisions that promote automatic contributions to retirement plans. Among those provisions was a provision that permits an employee to elect, within 90 days after the first such automatic contribution, to withdraw such contributions. Among other things, such a withdrawal is not subject to the 10% excise tax that generally applies to distributions made prior to age 59-1/2. The original PPA provision did not apply to salary reduction SEP IRA and SIMPLE IRA automatic contribution arrangements. The WRERA extends the provision to salary reduction SEP IRAs and SIMPLE IRAs. In addition, the original PPA

provision conditioned the excise tax waiver on the investment of automatic contributions in a qualified default investment alternative. The WRERA eliminates this requirement. These changes are retroactively effective to plan years beginning after December 31, 2007 (the original effective date of the automatic contribution arrangement provisions of the PPA).

Although none of these changes are reflected in the model IRA trust and custodial agreements published by the Internal Revenue Service, IRA trustees, custodians and issuers may wish to update their IRA disclosure statements and marketing materials to inform current and prospective IRA owners of these changes.

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