

Application of Section 401(a)(9) to Employees who Attain Age 70½ in 1996.

Notice 96-67

PURPOSE

This Notice addresses certain issues related to amendments, made by section 1404 of the Small Business Job Protection Act of 1996, Pub.L. 104-188 (SBJPA), to the minimum distribution requirements of section 401(a)(9) of the Internal Revenue Code. Specifically, the notice provides guidance on the application of section 401(a)(9), as amended by the SBJPA, to employees (other than 5-percent owners) who attain age 70½ in 1996 but who have not retired by the end of 1996.

BACKGROUND

Section 401(a)(9) provides that, in order for a plan to be qualified under section 401(a), distributions from the plan must commence no later than the "required beginning date". Similar rules apply to an individual retirement account or annuity (IRA) and a section 403(b) contract (*i.e.*, an annuity contract described in section 403(b), a custodial account described in section 403(b)(7) or a retirement income account described in section 403(b)(9)).

Prior to the amendments made by the SBJPA, section 401(a)(9)(C) generally defined required beginning date as April 1 of the calendar year following the calendar year in which an employee attained age 70½. This meant that an employee who attained age 70½ was required to commence distributions from

the plan, even if the employee had not retired from employment with the employer maintaining the plan.

Section 1404 of the SBJPA amended the definition of required beginning date that applies to an employee who is not a 5-percent owner. The amendment provides that, in the case of such an employee, the required beginning date is April 1 of the calendar year following the later of the calendar year in which the employee attains age 70½ or the calendar year in which the employee retires. In the case of an employee who is a 5-percent owner, the required beginning date remains April 1 of the calendar year following the calendar year in which the 5-percent owner attains age 70½. The amendments made by section 1404 of the SBJPA apply to years beginning after December 31, 1996.

The amendments do not apply to the required beginning date for distributions from an IRA, including an IRA established in conjunction with a Simplified Employee Pension (SEP) or a SIMPLE Plan. In addition, the amendments do not affect the determination of the required beginning date for church plans and government plans, since, under the pre-SBJPA version of section 401(a)(9), the required beginning date for these plans already was April 1 of the calendar year following the later of the calendar year in which the employee attains age 70½ or the calendar year in which the employee retires.

Taxpayers have requested guidance on the application of the amendments to section 401(a)(9)(C) made by the SBJPA to employees who attain age 70½ in 1996, but have not retired by the end of

1996. This Notice is issued in response to those requests.

QUESTIONS AND ANSWERS

Q-1: What is the effective date of the amendments to section 401(a)(9) made by section 1404 of the SBJPA?

A-1: Section 401(a)(9), as amended by section 1404 of the SBJPA, applies in determining the amount of any minimum distribution required to be made during any calendar year beginning on or after January 1, 1997 (that was not required to be made during an earlier calendar year).

Q-2: Is a minimum distribution required to be made by April 1, 1997 for an employee (other than a 5-percent owner) who attains age 70½ in 1996, but has not retired from employment with the employer maintaining the plan by the end of 1996?

A-2: No. Such an employee's required beginning date is determined under section 401(a)(9), as amended by the SBJPA. Thus, the employee's required beginning date is not April 1, 1997. Instead, the employee's required beginning date is April 1 of the calendar year following the year in which the employee retires from employment with the employer maintaining the plan.

Q-3: If a plan distribution is made in 1996 to an employee (other than a 5-percent owner) who attains age 70½ in that year, but has not retired by the end of 1996 from employment with the employer maintaining the plan, is any portion of the distribution a required distribution for purposes of section 402(c)(4)(B)?

A-3: Yes. Section 402(c)(4)(B) provides that a distribution is not an eli-

gible rollover distribution to the extent that it is required under section 401(a)(9). If a distribution is made during 1996 (*i.e.*, prior to the January 1, 1997 effective date of the SBJPA amendments to section 401(a)(9)), then, whether that distribution is a required distribution under section 401(a)(9) is determined by applying section 401(a)(9) as in effect prior to amendment by the SBJPA.

Under Q&A-7 of § 1.402(c)-2 of the Income Tax Regulations, a distribution in the year an employee attains age 70½ is treated as a required distribution under section 401(a)(9) to the extent that the total required minimum distribution under section 401(a)(9) for that year has not been satisfied. Therefore, although under Q&A-2 of this Notice, no distribution is required to be made by April 1, 1997 with respect to an employee (other than a 5-percent owner) who attains age 70½ during 1996, but has not retired by the end of that year, if a distribution actually is made to such an employee in 1996, the distribution is treated as a required distribution to the extent that the total required minimum distribution under section 401(a)(9), as in effect prior to amendment by the SBJPA, has not been satisfied. Thus, to that extent, the distribution is not an eligible rollover distribution and is not subject to mandatory 20% withholding under section 3405(c). However, a distribution to such an employee in 1997 (*i.e.*, after the effective date of the SBJPA amendments) is not a required distribution under section 401(a)(9).

Q-4: How does the guidance provided in Q&A-2 and Q&A-3 of this Notice apply to the determination of the required minimum distribution from a section 403(b) contract?

A-4: In applying section 401(a)(9) to a section 403(b) contract to which contributions are made by an employer, an employee's required beginning date is determined under section 401(a)(9) in the same manner as it would be determined for a qualified plan maintained by that employer. Accordingly, the required beginning date with respect to a section 403(b) contract of an employee who attains age 70½ in 1996 and who has not retired from employment by the end of 1996 is determined under Q&A-2 of this Notice. Similarly, whether a distribution in 1996 from a section 403(b) contract is a required minimum distribution (and thus not an

eligible rollover distribution) is determined in accordance with the guidance in Q&A-3 of this notice.

REQUEST FOR COMMENTS CONCERNING RELAXATION OF SECTION 411(d)(6)

Except to the extent provided by regulations, section 411(d)(6)(B) precludes a plan amendment that eliminates an optional form of benefit as it applies to benefits accrued as of the later of the adoption date or the effective date of the amendment. The right to commence benefit distributions in any form at a particular time is an optional form of benefit within the meaning of section 411(d)(6)(B) and Q&A-1(b) of § 1.411(d)-4 of the Income Tax Regulations. When it enacted section 1404 of the SBJPA, Congress did not alter the application of section 411(d)(6). Accordingly, an amendment that eliminates the right to receive a distribution prior to retirement (an in-service distribution) after age 70½ is precluded by section 411(d)(6) if the amendment applies to benefits accrued as of the later of the adoption date or the effective date of the amendment.

A plan that retains in-service distributions after age 70½ (either as a mandatory or an optional form of distribution) will satisfy the requirements of section 401(a)(9) as amended, and will not be prohibited by section 411(d)(6). However, the Service and the Treasury recognize the potential complexity of administering these distribution options. Therefore, the Service and the Treasury are considering the extent to which it is appropriate to exercise the authority in section 411(d)(6)(B) to permit plan amendments to eliminate the option to receive in-service distributions after age 70½. In making this determination, factors that the Service and the Treasury will take into account include the importance to plan participants of protecting the option to receive in-service distributions as well as the potential complexity to employers, plan administrators and participants of retaining the option.

The Service and the Treasury request comments concerning the extent to which a relaxation of section 411(d)(6) protection is appropriate for amendments that eliminate in-service distributions after age 70½ (*e.g.*, by limiting section 411(d)(6) protection to employees above a certain age). Because the Service and the Treasury have received requests that this guidance be provided

on an expedited basis, comments are requested to be submitted by January 31, 1997.

Comments can be addressed to CC:DOM:CORP:R (Notice 96-XX), room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, comments may be hand delivered between the hours of 8 a.m. and 5 p.m. to CC:DOM:CORP:R (Notice 96-XX), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC. Alternatively, taxpayers may transmit comments electronically via the IRS Internet site at http://www.irs.ustreas.gov/prod/tax_regs/comments.html

DRAFTING INFORMATION

The principal author of this Notice is Cheryl Press of the Office of the Associate Chief Counsel (Employee Benefits and Exempt Organizations). For further information regarding this Notice, contact Thomas R. Foley at (202) 622-6050 (not a toll-free number).