

200503036



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

U.I.L.72-20-04

OCT 25 2004

LEGEND:

- Taxpayer A = *****
- IRA X = *****
- Company M = *****
- Individual B = *****
- Amount D = *****
- Amount E = *****
- Amount F = *****
- Amount G = *****

Dear *****:

This is in response to your letter dated May 20, 2004, and supplemented by correspondence dated September 10, 2004, submitted on your behalf by your authorized representative in which you request a ruling as to whether a "make-up" distribution from your individual retirement arrangement (IRA) will not result in a modification to a series of substantially equal periodic payments you are currently receiving and, therefore, will not be subject to the additional 10 percent tax imposed on premature distributions under section 72(t) of the Internal Revenue Code (Code).

The following facts and representations were made in support of your ruling request.

Page 2

Taxpayer A retired in [REDACTED] at the age of [REDACTED]. Taxpayer A maintains IRA X, a rollover IRA he established in [REDACTED] with Company M with a distribution he received from a qualified retirement plan. Company M is the custodian of IRA X.

Taxpayer A's financial representative at Company M, Individual B, established an arrangement under which Taxpayer A would receive annual IRA distributions in the form of a series of substantially equal periodic payments calculated under the fixed annuitization method. Taxpayer A is required to annually withdraw an aggregate amount, Amount D, from IRA X. Company M, as custodian, makes the distributions to Taxpayer A. The distributions from IRA X began in calendar year [REDACTED] and were intended to comply with the requirements of section 72(t)(2)(A)(iv) of the Code.

Prior to [REDACTED], Taxpayer A received an aggregate distribution of Amount E from IRA X for the [REDACTED] calendar year as part of his required distribution. On [REDACTED], Taxpayer A met with Individual B and completed an IRA distribution form requesting a withdrawal of Amount F from IRA X. Amount F constituted the remaining portion of his [REDACTED] required annual distribution. The distribution form completed and signed by Taxpayer A on [REDACTED] provided the IRA X account number from which the withdrawal should be made; the withdrawal amount (Amount F), the account number of the Company M account to which Amount F should be transferred; and the percentage of federal income taxes to be withheld from Amount F; Taxpayer A asserts that he gave the distribution form to Individual B who forwarded it to Company M.

On [REDACTED], Individual B noticed that Taxpayer A's request to withdraw Amount F from IRA X had not been processed and that only Amount E had been distributed to Taxpayer A from IRA X for the [REDACTED] calendar year. A make-up distribution in the amount of Amount F was made from IRA X on [REDACTED] in accordance with Taxpayer A's prior withdrawal request of [REDACTED]. As a result of Company M's error, Taxpayer A's [REDACTED] Form 1099-R reflects a total distribution of Amount E. Taxpayer A's [REDACTED] Form 1099-R will total Amount G, which is the sum that Taxpayer A would have received for the [REDACTED] calendar year (Amount D) plus the make-up distribution of Amount F. The method for calculating Taxpayer A's annual distribution from IRA X and the annual payment amount will not change.

Based on the foregoing, you request a ruling that the failure to distribute the entire required distribution amount for the [REDACTED] calendar year and the subsequent make up distribution in the [REDACTED] calendar year will not be considered a modification to a series of substantially equal periodic payments under Code section 72(t)(4) that will result in the imposition of the 10 percent additional tax under Code section 72(t)(1).

Section 408(d)(1) of the Code provides that, except as otherwise provided in section 408(d), any amount paid or distributed out of an IRA shall be included in gross income by the payee or distributee, as the case may be, in the manner provided under section 72 of the Code.

Page 3

Section 72 of the Code provides rules for determining how amounts received as annuities, endowments, or life insurance contracts and distributions from qualified plans are to be taxed.

Section 72(t)(1) provides for the imposition of an additional 10 percent tax on early distributions from qualified plans, including IRAs. The additional tax is imposed on that portion of the distribution that is includible in gross income.

Section 72(t)(2)(A)(iv) of the Code provides that section 72(t)(1) shall not apply to distributions that are part of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the employee or joint lives (or joint life expectancies) of such employee and his designated beneficiary.

Section 72(t)(4) of the Code imposes the additional limitation on distributions excepted from the 10 percent tax by section 72(t)(2)(A)(iv) that, if the series of payments is subsequently modified (other than by reason of death or disability) before the later of the employee's attainment of age 59 ½, then the taxpayer's tax for the first taxable year in which such modification occurs shall be increased by an amount determined under regulations, equal to the tax that would have been imposed except for the section 72(t)(2)(A)(iv) exception, plus interest for the deferral period.

Notice 89-25 was published on March 20, 1989, and provided guidance, in the form of questions and answers, on certain provisions of the Tax Reform Act of 1986 (TRA '86). In the absence of regulations on section 72(t) of the Code, this notice provides guidance with respect to the exception to the tax on premature distributions provided under section 72(t)(2)(A)(iv). Q&A-12 of Notice 89-25 provides three methods of determining substantially equal periodic payments for purposes of section 72(t)(2)(A)(iv) of the Code.

Revenue Ruling 2002-62, 2002-42 I.R.B. 710, which was published on October 21, 2002, modifies Q&A-12 of Notice 89-25. Rev. Rul. 2002-62 provides, among other things, that payments are considered to be substantially equal periodic payments within the meaning of section 72(t)(2)(A)(iv) if they are made in accordance with the required minimum distribution method, the fixed amortization method or the fixed annuitization method (the three methods described in Q&A-12 of Notice 89-25).

The fixed annuitization method provides that the annual payment for each year is determined by dividing the account balance by an annuity factor that is the present value of an annuity of one dollar (\$1) per year beginning at the taxpayer's age and continuing for the life of the taxpayer (or the joint lives of the individual and beneficiary). The annuity factor is derived using the mortality table in Appendix B of Revenue Ruling 2002-62 and using the chosen interest rate. Under this method, the account balance, the annuity factor, the chosen interest rate and the resulting annual payment are determined once for the first distribution year and the annual payment is the same amount in each succeeding year.

In this case, Taxpayer A states that he began to receive payments from IRA X in calendar year [REDACTED] in a series of substantially equal periodic payments as described in Code section 72(t)(2)(A)(iv) using the fixed annuitization method as described in Revenue Ruling 2002-62. Taxpayer A further states that the annual payment from IRA X as determined under the above methodology is Amount D. For calendar year [REDACTED], Taxpayer A received distributions from IRA X prior to [REDACTED] that in the aggregate totaled Amount E. Taxpayer A has submitted documentation that shows that on [REDACTED], he requested Company M to distribute the balance of his [REDACTED] annual payment (Amount F) from IRA X. If Amount F had been distributed as requested by Taxpayer A on [REDACTED], he would have received for calendar year [REDACTED] the annual payment calculated using the method he chose to calculate the series of substantially equal periodic payments from IRA X. Amount F was not distributed by Company M by the end of the [REDACTED] calendar year. When the error was discovered by Company M on [REDACTED], Amount F was immediately distributed to Taxpayer A.

Documentation submitted by Taxpayer A shows that he completed the necessary Company M distribution form to have the remaining amount (Amount F) distributed from IRA X for the [REDACTED] calendar year and gave the form to Individual B, a Company M employee. Taxpayer A did all that he could in order to ensure that he received the balance of the annual payment from IRA X and had no reason to believe that Company M would not make the distribution as he requested. Taxpayer A did not intend to modify the series of substantially equal periodic payments he began receiving from IRA X in calendar year [REDACTED]. Rather, the modification is due to the failure of Company M to make the remaining distribution of Amount F from IRA X in calendar year [REDACTED] which resulted in Taxpayer A receiving an annual payment for the [REDACTED] calendar year that is less than the amount determined under the fixed annuitization method. Further, when Company M distributed Amount F to Taxpayer A in [REDACTED], this distribution, when added to Taxpayer A's previously calculated annual payment (Amount D), will result in Taxpayer A receiving an amount for calendar year [REDACTED] that will be more than the annual payment determined under the fixed annuitization method. Other than the amount of the annual payment for the [REDACTED] and [REDACTED] calendar years, Taxpayer A will continue to use the fixed annuitization method for calculating the annual payments from IRA X.

Accordingly, we conclude that the failure to distribute the entire required annual payment from IRA X for the [REDACTED] calendar year and the subsequent "make-up" distribution for the [REDACTED] calendar year made in calendar year [REDACTED] will not be considered a modification of a series of substantially equal periodic payments under Code section 72(t)(2)(A)(iv) and, therefore will not be subject to the 10 percent additional tax imposed on premature distributions under section 72(t)(1) of Code.

This ruling does not express an opinion as to whether (but assumes that) the series of substantially equal payments Taxpayer A is currently receiving from IRA X satisfies Code section 72(t)(2)(A)(iv) and Revenue Ruling 2002-62. This ruling assumes that

200503036

Page 5

IRA X meets the requirements of Code section 408(a) at all times relevant to this transaction.

This letter ruling is directed only to the taxpayer that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

A copy of this letter has been sent to your authorized representative in accordance with a power of attorney on file in this office.

If you have any questions, please contact *****SE:T:EP:RA:T2.

Sincerely yours,

~~(SIGNED) JOYCE E. FLOYD~~

Joyce E. Floyd, Manager
Employee Plans Technical Group 2

Enclosures:

Deleted copy of ruling letter
Notice of Intention to Disclose