

October 23, 2009

TCRS 2009-10: Rollovers from Eligible Employer Plans to Roth IRAs

In Notice 2009-75, the Internal Revenue Service (IRS) provides additional guidance regarding the federal income tax consequences of rolling over an eligible rollover distribution from a qualified plan described in Internal Revenue Code (IRC) section 401(a), an annuity plan described in IRC section 403(a), a plan described in IRC section 403(b), or an eligible governmental plan under IRC section 457(b) (collectively referred to as "eligible employer plan") to a Roth IRA.

Background

Prior to the enactment of the Pension Protection Act of 2006, an eligible rollover distribution from an eligible employer plan could not be made directly into a Roth IRA, except for the portion of the distribution representing amounts from a designated Roth account under the eligible employer plan. If a rollover to a Roth IRA of the non-Roth portion of the eligible rollover distribution was desired, the rollover had to first be made to a traditional IRA followed by a conversion to a Roth IRA.

The PPA amended the definition of a qualified rollover contribution for distributions made on and after January 1, 2008, to allow the rollover of the non-Roth portion of an eligible rollover distribution directly to a Roth IRA. However, for taxable years beginning before 2010, the ability to directly roll over the non-Roth portion of a distribution from an eligible employer plan is only available if the participant's modified adjusted gross income for the year of the distribution does not exceed \$100,000 (and who, if married, files jointly).

Notice 2009-75

Federal Tax Consequences of Rollovers from Eligible Employer Plans to Roth IRAs

- o Mandatory withholding does not apply.
- o Additional income tax on early distributions generally does not apply.
- o The special rule relating to additional income tax for early distributions from the Roth IRA during the first 5 years following a rollover applies.
- o An eligible rollover distribution that is not made from a designated Roth account is included in gross income in the year of the distribution. However, the amount of any after-tax contributions included in such rollover is not included in gross income.
- o The Notice provides that the special rules relating to net unrealized appreciation in IRC section 402(e)(4) and certain optional methods for calculating tax available to participants born on or before January 1, 1936, do not apply.
- o An eligible rollover distribution made from a designated Roth account to a Roth IRA is not included in gross income, whether or not the amount rolled over is a qualified distribution from the designated Roth account.

Application of Modified Adjusted Gross Income Limits

- o An eligible rollover distribution made prior to January 1, 2010, may not be rolled over to a Roth IRA unless a participant's modified adjusted gross income is \$100,000 or less and, in the case of a married participant, the participant files a joint tax return with his/her spouse. On and after January 1, 2010, the income restriction and the requirement that a married participant file a joint return no longer apply.
- o The Notice provides that if an eligible rollover distribution made before 2010 could not be rolled over to a Roth IRA because of the income restriction and the requirement to file a joint return, such distribution could first be rolled over to a traditional IRA and then converted, on and after January 1, 2010, into a Roth IRA.
- o The Notice further provides that there are no income restrictions and joint filing requirements that apply to a rollover of an eligible rollover distribution made from a designated Roth account to a Roth IRA.

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