[COMMITTEE PRINT]

DESCRIPTION OF H.R. 13619: INDIVIDUAL RETIREMENT PLAN TECHNICAL CHANGES ACT OF 1978

PREPARED FOR THE USE OF THE

COMMITTEE ON WAYS AND MEANS

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

This pamphlet describes a number of technical revisions to the tax laws relating to individual retirement plans contained in H.R. 13619.

The staff of the Joint Committee on Taxation has prepared brief summaries of each item under the bill. In addition, the staff has prepared detailed descriptions of each item under the bill, indicating the present law treatment, the issue involved, an explanation of the provision, its effective date, revenue effects, and the Treasury position.

I. SUMMARY OF THE BILL

A. Part I of the Bill Relating to IRA Contributions

1. Extension of period for making individual retirement plan contributions

Under present law, a deduction is allowed for a contribution to an IRA (an individual retirement account, an individual retirement annuity, or a retirement bond) for a year only if it is made within 45 days after the close of the year.

The bill would permit an individual to make a deductible contribution to an IRA (and establish IRA) for a year up to the time for filing the individual's tax return for the year (including extensions).

2. Deduction of contributions in subsequent year for which there is an unused limitation

Under present law, if an individual does not make the maximum deductible contribution to an IRA for a year, the additional amount which the individual could have contributed and deducted is applied to reduce any accumulated excess contributions to the IRA as of the close of the year. However, no deduction is allowed with respect to the reduction of excess contributions.

Under the bill, a deduction would be allowed to the extent that an unused IRA deduction limitation for a year is applied to reduce excess contributions to the IRA, but only to the extent that the excess contributions were not previously deducted. The bill also allows make-up deductions for corrections made in taxable years beginning after December 31, 1975.

3. Individual retirement plan deductions for certain months in which individual is not an active participant in employer plan

Under present law, an individual is not permitted to make a deductible contribution to an IRA for a year if the individual is an active participant in a qualified plan or a governmental plan for any part of that year.

Under the bill, an individual who is an active participant in a qualified plan or a governmental plan for only a portion of a year would be permitted to make a deductible contribution to an IRA based on the number of months in the year for which the individual is not an active participant.

4. Additional period to rectify certain excess contributions

Under present law, an excess contribution by an individual to an IRA for a year may be corrected without penalty only if the excess and any earnings thereon are withdrawn by the time for filing the individual's tax return for the year (including extensions) and only if the amount withdrawn does not exceed the excess of $1,500 ($1,750 for a spousal IRA) over the amount allowable as a deduction for an IRA contribution for the year.

The bill would allow an individual who (1) makes an excess contribution that does not exceed $1,750 to an IRA for a year, and (2) fails to correct the excess contribution by the date for filing the individual's tax return for the year (including extensions), later to withdraw the excess contribution without incurring a penalty for the year of withdrawal, but only to the extent that a deduction was not previously allowed with respect to the excess contribution. Also, the bill would allow an excess rollover contribution, regardless of the amount, to be corrected where it resulted from reasonable reliance on certain erroneous information. The bill allows corrections for taxable years beginning after December 31, 1975.

5. Addition of requirement that premiums on individual retirement annuity contracts must be flexible

Under present law, an individual retirement annuity contract may require the payment of fixed premiums, irrespective of whether the premiums are deductible under the IRA provisions.

Under the bill, individual retirement annuity contracts issued after the date of enactment of the bill would be required to provide for the flexible payment of premiums. In addition, the bill would permit tax-free exchange of previously issued fixed premium individual retirement annuity contracts for flexible premium individual retirement annuity contracts.

6. Clarification of dollar limitation in the case of individual retirement annuities and retirement bonds

Under present law, the maximum deductible contribution to a spousal individual retirement account is $1,750.

The bill would correct a technical oversight in connection with individual retirement annuities and retirement bonds to make it clear that contributions of up to $1,750 may be permitted in the case of all spousal IRAs.

B. Part II of the Bill Relating to Rollovers

1. Partial rollovers

Under present law, the recipient of a distribution from a qualified plan eligible for rollover treatment must contribute the entire amount distributed to an IRA or to another qualified plan to qualify for tax-free rollover treatment.

Under the bill, the recipient of a distribution from a qualified plan eligible for rollover treatment would be permitted to roll over a portion of the distribution or the full amount distributed. In the case of a partial rollover, amounts not rolled over generally would be taxed as ordinary earned income.

2. Rollover of proceeds from sale of property

Under present law, an individual who receives property as part of a distribution from a qualified plan eligible for rollover treatment is accorded tax-free rollover treatment only if the actual property distributed from the qualified plan is contributed to an IRA or to another qualified plan.

Under the bill, an individual who receives property as part of a distribution from a qualified plan eligible for rollover treatment would be permitted to engage in a tax-free rollover of the proceeds from the sale of the property distributed rather than of the property itself.

3. Rollover contribution to individual retirement plan of distribution to spouse from qualified plan or annuity

Under present law, a participant in a qualified plan is eligible to make a tax-free rollover contribution to an IRA of a lump sum distribution from the plan, but if the spouse of a deceased participant receives a lump sum distribution as a death benefit under the plan the spouse is not eligible to make a rollover contribution.

Under the bill, the spouse of a deceased participant who receives a lump sum distribution as a death benefit from a qualified plan would be eligible to make a rollover contribution to an IRA.

4. Removal of certain restrictions on rollovers

Under present law, an individual must have been a participant in a qualified plan for five years in order to receive a lump sum distribution from the plan which is eligible for tax-free rollover treatment.

Also, under present law, rollovers between IRAs are permitted only once every three years.

Under the bill, an individual who has participated in a qualified plan for less than five years would be eligible to receive a lump sum distribution from the plan which is eligible for tax-free rollover treatment.

Also under the bill, rollovers between IRAs would be permitted without any limitation as to frequency.

C. Part III of the Bill Relating to Changes in Penalty Provisions

1. Waiver of excise tax on certain accumulations in individual retirement accounts or annuities

Present law imposes a 50-percent excise tax on an individual who fails to make certain minimum distributions from an IRA beginning at age 70½.

Under the bill, the Secretary of the Treasury would have the authority to waive the 50-percent excise tax where the failure to make a required minimum distribution from an IRA is due to reasonable error and reasonable steps are being taken to correct the error.

2. Removal of certain limitations on provision allowing correction of excess contributions

Under the present law, an excess contribution to an IRA for a year may be corrected without penalty if the contribution and earnings thereon are withdrawn from the IRA by the date for filing the tax return for the year (including extensions) and if the amount withdrawn does not exceed the excess of $1,500 ($1,750 for a spousal IRA) over the amount allowable as a deduction for an IRA contribution for the year.

Under the bill, the dollar limitations would be withdrawn and an excess contribution to an IRA for a year could be corrected without penalty if the excess contribution and the earnings thereon are withdrawn on or before the date for filing the tax return for the year (including extensions).

D. Part IV of the Bill Relating to Simplification of Return Requirements With Respect to Individual Retirement Plans

Under present law, an individual maintaining an IRA is required to file a tax return with respect to the IRA each year.

Under the bill, IRA tax returns would not be required for a year in which no IRA penalty taxes are imposed and no activity occurs with respect to the IRA other than the making of deductible contributions and permissible distributions.

II. DESCRIPTION OF PROVISIONS OF PART I OF THE BILL RELATING TO IRA CONTRIBUTIONS

A. Extension of Period for Making Individual Retirement Plan Contributions (sec. 11 of the bill and secs. 219(c)(3) and 220(c)(4) of the Code)

Present law

Present law allows an individual a deduction from gross income for certain contributions to an IRA (an individual retirement account, an individual retirement annuity or a retirement bond) (secs. 219, 220). Under the Employee Retirement Income Security Act of 1974 (ERISA) the contributions for a particular year, in order to be deductible, had to be made by the close of the year. The Tax Reform Act of 1976 extended the time for making deductible contributions for a year to 45 days after the close of the year.

Issue

The issue is whether the time for making deductible contributions to an IRA for a taxable year should be extended to the time prescribed by law for filing the tax return for that year (including extensions).

Explanation of provision

The amendment would extend the date by which an individual could make deductible contributions to an IRA for a taxable year. Under the amendment, such contributions would be deductible for the year if made on or before the date prescribed by law for filing the individual's federal income tax return for the year (including extensions). As under present law, the individual would be permitted to establish an IRA on the same date on which he or she made the contribution, so the extension would apply to plan establishment as well as to contributions.

Effective date

The amendments made by this section would apply to taxable years beginning after December 31, 1977.

Revenue effect

It is estimated that this amendment would have a negligible effect on budget receipts.

Treasury position

The Treasury Department supports the amendment.

B. Deduction of Contributions in Subsequent Year for Which There is an Unused Limitation (sec. 12 of the bill and new secs. 219(c)(5) and 220(c)(6) of the Code and sec. 4973(b)(2) of the Code)

Present law

Present law allows an individual a deduction from gross income for certain contributions to an IRA (secs. 219, 220). The maximum deduction allowable for a taxable year generally is the lesser of 15 percent of compensation includible in gross income or $1,500. In the case of an individual who has a nonworking spouse, the maximum deduction allowable is the lesser of 15 percent of compensation includible in gross income or $1,750 provided the individual shares the contribution equally with his or her spouse. An amount contributed which does not qualify as a rollover contribution and which is in excess of the maximum deduction allowable is an "excess contribution".

An excess contribution is subject to an annual 6 percent penalty tax unless corrected. In order to correct an excess contribution, an individual must either (1) receive a distribution of the excess amount, or (2) contribute an amount in a future year which falls short of the maximum deduction allowable for that year, in which case the excess contribution is deemed to be corrected to the extent of the shortfall. However, the deduction for the year does not include the amount of the shortfall.

Issue

The issue is whether an individual should be allowed a deduction in the circumstance where an excess contribution is corrected in a year because the individual makes a contribution in an amount which is less than the maximum deduction allowable.

Explanation of provision

The amendment would allow an individual a deduction from gross income for a taxable year where he corrects a previous excess contribution to an IRA by contributing less than his maximum deduction allowable for the year. The maximum deduction allowed by the amendment would be the amount of the undercontribution. If the individual erroneously took a deduction in a previous year for any part of the excess contribution and the period for assessing a deficiency for the previous year has expired, the amount allowed as a deduction under the amendment would be correspondingly reduced.

The amendment provides a transitional rule with respect to amounts of excess contributions made up by undercontributions for years prior to 1978. The rule would allow a one-time catchup deduction from gross income for those amounts for 1978 rather than requiring amended returns to be filed for each year of undercontribution.

Effective date

The amendments made by this section would apply to taxable years beginning after December 31, 1975.

Revenue effect

It is estimated that this amendment would budget receipts by $20 million in fiscal year 1979, and by $8 million annually thereafter.

Treasury position

The Treasury Department supports the amendment.

C. Individual Retirement Plan Deductions for Certain Months in Which Individual is not Active Participant in Employer Plan (sec. 13 of the bill and secs. 219 and 220 of the Code)

Present law

Present law allows an individual a deduction from gross income for contributions to an IRA (secs. 219, 220). The maximum deduction with respect to contributions for a year generally is the lesser of 15 percent of compensation includible in gross income or $1,500. In the case of an individual with a nonworking spouse, the maximum deduction is the lesser of 15 percent of compensation includible in gross income or $1,750, provided the individual shares the contribution equally with his or her spouse (spousal IRA).

Under present law, no deduction is allowed for a contribution to an IRA if the individual (or his or her spouse in the case of a spousal IRA) is an active participant in a tax-qualified retirement plan, bond purchase plan, or annuity plan or in a governmental plan for any part of the year, or had amounts contributed by his or her employer to a tax-sheltered annuity (secs. 219(b)(2), 220(b)(3)).

Issues

The issues are (1) whether an individual who is an active participant in a qualified plan or in a governmental plan for only a part of a taxable year should be permitted to make a deductible contribution to an IRA for the portion of the year for which the individual is not an active participant, and (2) whether an individual should be permitted to make a deductible contribution to a spousal IRA for the portion of the year for which neither the individual nor his or her spouse is an active participant in a qualified plan or in a governmental plan.

In the case of a spousal IRA, the individual would be allowed to make a deductible contribution for that portion of the year for which neither the individual nor his or her spouse is an active participant in a qualified plan or in a governmental plan. The amount of the permissible deductible contribution would be the lesser of (1) 15 percent of compensation includible in gross income, or (2) $1,750 times the monthly proration.

Explanation of provision

Under the amendment, an individual who is an active participant in a qualified plan or in a governmental plan for only a portion of a year would no longer automatically be prevented from making a deductible contribution to an IRA. Instead, the individual would be allowed to make a deductible contribution to an IRA for that portion of the year for which the individual is not an active participant in a qualified plan or in a governmental plan. The amount of the permissible deductible contribution would be the lesser of (1) 15 percent of compensation includible in gross income, or (2) $1,500 multiplied by a fraction. The numerator of the fraction would be the number of full months in which the individual did not participate in a qualified plan and the denominator of the fraction would be 12. For example, if an individual is not an active participant in a qualified plan for nine months of a year, the amount of his deductible contribution to any IRA would be the lesser of 15 percent of compensation includible in gross income or \$1,125 (\$1,500 x $\frac{9}{12}$).

Effective date

The amendments made by this section would apply to taxable years beginning after December 31, 1978, but only in the case of contributions made after December 31, 1979.

Revenue effect

It is estimated that this amendment would decrease budget receipts by \$10 million in fiscal year 1980, by \$12 million in fiscal year 1981, by \$14 million in fiscal year 1982, and by \$16 million in fiscal year 1983.

Treasury position

The Treasury Department opposes the amendment because the solution to the problem should have further public discussion. The Treasury Department suggests that a simpler and more satisfactory approach is to allow IRA contributions only in the case of a change in employment and if the contributions are based, not on a monthly proration, but rather on compensation paid by the employer not (1) maintaining a qualified or governmental plan in which the individual is an active participant or (2) contributing to a tax-sheltered annuity for the individual.

D. Additional Period to Rectify Certain Excess Contributions (sec. 14 of the bill and sec. 408(d) of the Code)

Present law

Under present law, a 6-percent penalty tax is imposed annually on an excess contribution to an IRA. An excess contribution is a contribution which exceeds the maximum deductible contribution and which does not qualify as a rollover contribution. The 6-percent penalty tax is not imposed on the excess contributed in a year, however, if (1) such amount does not exceed the excess of $1,500 ($1,750 in the case of a spousal IRA) over the amount allowable as a deduction for the year, (2) such amount and the earnings thereon are withdrawn on or before the filing date for the individual's income tax return (including extensions) for the year, and (3) the individual did not take a deduction for such amount.

If the excess contributed for a year is withdrawn after the date for filing the individual's return, (1) it is subject to the 6-percent penalty tax for each year for which the excess remains, (2) it is subject to a 10-percent premature distribution penalty tax if the individual is not at least age 59½, and (3) it is includible in the individual's gross income for the year.

Issue

The issue is whether in the case of certain excess contributions to an IRA an individual should be permitted to withdraw the excess contributed for a year after the date prescribed by law for filing his or her tax return for the year without incurring any penalty for the year of the withdrawal.

Explanation of provision

The amendment would allow an individual who has made an excess contribution for a year which does not exceed $1,750 to an IRA and who does not correct the excess contribution prior to the due date for filing his or her tax return for the year, later to withdraw the excess contributed for the year without (1) incurring a 10-percent premature distribution penalty tax, and (2) being required to include the amount withdrawn in gross income.[1] The amendment would apply only to the extent that a deduction was not allowed for the amount of the excess contribution withdrawn.

The amendment provides a transitional rule for excess contributions to IRAs for taxable years beginning before January 1, 1978. For such excess contributions, the provisions of the amendment would apply without regard to the $1,750 limitation. Thus, an individual could withdraw all such excess contributions, regardless of amount, to the extent deductions were not previously allowed for the excess contributions.

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[1] As under present law, the 6 percent excess contribution tax would not apply to the year of withdrawal.

The amendment also allows an individual to withdraw an excess contribution (regardless of the amount) made with respect to a rollover contribution (including an attempted rollover contribution) in any case in which the excess contribution occurred because the individual making the contribution reasonably relied on erroneous information required to be supplied by the plan, trust, or institution making the distribution which was the subject of the rollover.

Effective date

The amendments made by this section would apply to distributions from IRAs in taxable years beginning after December 31, 1975.

Revenue effect

It is estimated that this amendment would decrease budget receipts by less than $5 million annually.

Treasury position

The Treasury Department supports the amendment.

E. Addition of Requirement that Premiums on Individual Retirement Annuity Contracts Must be Flexible (sec. 15 of the bill and sec. 408(b) of the Code)

Present law

Under present law, an individual is allowed a deduction from gross income for certain contributions to an individual retirement annuity. To qualify as an individual retirement annuity an annuity contract must meet certain statutory specifications (sec. 408(b)). A fixed premium contract (e.g., a contract which requires fixed payments over a fixed period of time) which meets these specifications qualifies as an individual retirement annuity. However, if the fixed premium exceeds the individual's maximum allowable IRA deduction for the year, the excess premium payment is not deductible and is subject to a 6-percent excess contribution penalty.

Issue

The issue is whether an annuity contract should be required to provide for flexible payment of premiums to qualify as an individual retirement annuity.

Explanation of provision

The amendment would require that an annuity contract provide for the flexible payment of premiums in order to qualify as an individual retirement annuity.

The amendment provides a transitional rule under which the exchange before January 1, 1981, of any fixed premium individual retirement annuity issued on or before the effective date of the amendment for a flexible premium annuity contract would, at the election of the individual, be treated as a nontaxable exchange.

Effective date

The amendment made by this section would apply to contracts issued or exchanged after the date of its enactment.

Revenue effect

It is estimated that this amendment would have a negligible effect on budget receipts.

Treasury position

The Treasury Department supports the amendment.

F. Clarification of Dollar Limit in the Case of Individual Retirement Annuities and Retirement Bonds (sec. 16 of the bill and secs. 408(b) and 409 of the Code)

Present law

The Employee Retirement Income Security Act of 1974 (ERISA) permitted individuals to make deductible contributions to IRAs in an amount equal to the lesser of 15 percent of compensation includible in gross income or $1,500. The Tax Reform Act of 1976 raised the dollar limitation for such contributions to $1,750 provided the individual has a nonworking spouse with whom he or she shares the contribution equally (spousal IRA). Certain provisions of the Code defining individual retirement annuity and retirement bond were not amended by the 1976 Act to reflect the change in the dollar limitation from $1,500 to $1,750 for spousal IRAs.

Issue

This amendment corrects a technical oversight.

Explanation of provision

The amendment would modify the definitions of individual retirement annuity and retirement bond to make it clear that the maximum dollar limitation for deductible contributions to a spousal IRA is $1,750.

Effective date

The amendments made by this section would apply to taxable years beginning after December 31, 1976,

Revenue effect

This amendment would have no effect on budget receipts.

Treasury position

The Treasury Department supports the amendment.

III. DESCRIPTION OF PROVISIONS OF PART II OF THE BILL RELATING TO ROLLOVERS

A. Partial Rollovers (sec. 21 of the bill and secs. 402(a)(5), 402(e)(4), and 403(a)(4) of the Code)

Present law

Under present law a participant in a qualified retirement plan who receives a lump sum distribution from the plan or a complete distribution upon termination of the plan may avoid current tax by making a rollover contribution to an IRA or to another qualified plan within 60 days of the date of the distribution. In order to qualify for tax-free rollover treatment, the individual must contribute to the IRA or to the other qualified plan, the amount of money plus all of the assets received from the qualified plan, except for an amount allocable to previous employee contributions to the qualified plan. An employee who fails to contribute the required amount is taxed currently on the entire distribution from the qualified plan. If the distribution qualifies as a lump sum distribution the individual may elect special 10-year income averaging.

Under present law, assests contributed to an IRA in a nonqualified rollover constitute an excess contribution to the extent not deductible as current year IRA contributions. Accordingly, (1) a 6 percent excise tax is imposed for each year for which the excess remains, (2) the excess contribution and the earnings thereon are included in gross income when distributed from the IRA, and (3) generally the excess contribution and earnings thereon are subject to a 10 percent penalty tax if distributed before age 59½.

Issue

The issue is whether a participant in a qualified plan who receives a lump sum distribution from the plan or a complete distribution upon termination of the plan should be permitted to engage in a rollover of only part of the assets distributed.

Explanation of provision

The amendment would permit the recipient of a lump sum distribution from a qualified plan or of a complete distribution upon termination of a qualified plan to make a rollover contribution of all or a portion of the distribution (less the amount allocable to employee contributions) to an IRA or to another qualified plan.[1] In any case

[1] An amendment which permits partial rollovers has been passed by both the House and the Senate (H.R. 1337). In addition to allowing partial rollovers prospectively, the amendment permits a special make-up provision for individuals who attempted in the past to roll over a distribution but failed to comply with the requirement that the entire amount of the distribution be rolled over. Such individuals would have until December 31, 1978, to roll over any portion of the distribution. Cash could be rolled over instead of distributed property.

Because of changes made to the Senate amendment by the House, H.R. 1337 must be passed by the Senate again. The House made certain technical changes to the Senate amendment and provided for partial rollovers from tax-qualified annuity plans. (The Senate provision dealt only with rollovers from other types of qualified retirement plans, i.e., pension, profit-sharing, etc.)

where the individual makes a rollover contribution of less than the full distribution (other than amounts allocable to employee contributions), the amount retained by the individual would be taxed currently as ordinary earned income and would not be eligible for special 10-year income averaging.

Effective date

The amendments made by this section would apply to lump sum distributions after December 31, 1978, in taxable years ending after December 31, 1978.

Revenue effect

It is estimated that this amendment would have a negligible effect on budget receipts.

Treasury position

The Treasury Department supports the amendment.

B. Rollover of Proceeds from Sale of Property (sec. 22 of the bill and secs. 402(a)(6) and 403(a)(5) of the Code)

Present law

Under present law, a participant in a qualified plan who receives a lump sum distribution from the plan or a complete distribution upon termination of the plan may avoid current tax by making a rollover contribution to an IRA or to another qualified plan within 60 days of the date of the distribution. If the individual receives property other than cash in the distribution, the actual assets received must be contributed to the IRA or to the other qualified plan in order to qualify for tax-free rollover treatment. If the individual sells any asset received in the distribution and contributes the proceeds from the sale to an IRA or to a qualified plan as part of an attempted rollover contribution the entire contribution will fail to qualify as a rollover. Also, if the unsuccessful rollover was made to an IRA, the amount contributed is treated as an excess contribution. Accordingly, (1) a 6-percent excise tax is imposed for each year for which the excess contribution remains, (2) the excess contribution and the earnings thereon are included in gross income when distributed from the IRA, and (3) generally the excess contributions and earnings thereon are subject to a 10-percent penalty tax if distributed before age 59½.

Issue

The issue is whether a participant in a qualified plan who receives a lump sum distribution from the plan or a complete distribution upon termination of the plan which consists in whole or in part of property other than cash should be accorded tax-free rollover treatment if the proceeds from the sale of the property rather than the property itself are contributed to an IRA or to another qualified plan.

Explanation of provision

The amendment would permit the recipient of a lump sum distribution from a qualified plan or a complete distribution upon termination of a qualified plan, which consists in whole or in part of property other than cash to receive tax-free rollover treatment by contributing the proceeds from the sale of the property rather than the property itself to an IRA or to another qualified plan within 60 days from the date of the distribution.

Effective date

The amendments made by this section would apply to lump sum distributions completed after December 31, 1978, in taxable years ending after December 31, 1978.

Revenue effect

It is estimated that this amendment would have a negligible effect on budget receipts.

Treasury provision

The Treasury Department supports the amendment.

C. Rollover Contribution to Individual Retirement Plan of Distribution to Spouse From Qualified Plan or Annuity (sec. 23 of the bill and new secs. 402(a)(7) and 403(a)(6) of the Code)

Present law

Under present law, a participant in a qualified plan who receives a lump sum distribution from the plan may avoid current tax by making a rollover contribution to an IRA or to another qualified plan within 60 days of the date of the distribution. However, the recipient of a lump sum distribution on account of the death of a plan participant is not eligible to engage in a tax-free rollover.

Issue

The issue is whether the spouse of a participant in a qualified plan who receives a lump sum distribution from the plan on account of the participant's death should be permitted to engage in a tax-free rollover of the distribution to an IRA.

Explanation of provision

Under the amendment, if an individual participating in a qualified plan dies and his or her spouse receives a distribution from the plan which qualifies as a lump sum distribution, the spouse could, within 60 days of the date of the distribution, make a rollover contribution to an IRA of the assets distributed from the qualified plan.

Effective date

The amendments made by this section would apply to lump sum distributions completed after December 31, 1978 in taxable years ending after such date.

Revenue effect

It is estimated that this amendment would decrease budget receipts by less than $5 million annually.

Treasury position

The Treasury Department supports the amendment.

D. Removal of Certain Restrictions on Rollovers (sec. 24 of the bill and secs. 402(a)(5)(A), 403 (a)(4)(A), and 408(d)(3) of the Code)

Present law

Under present law, if an individual receives a lump sum distribution from a qualified plan or a complete distribution upon termination of a qualified plan, the individual may avoid current tax by making a rollover contribution of the amount of cash plus the property distributed (less an amount allocable to employee contributions) to an IRA or to another qualified plan. For a distribution to qualify as a lump sum distribution, the individual must have been a participant in the qualified plan for five or more taxable years before the taxable year of the distribution.

Under present law, an individual is permitted to make a rollover contribution of a distribution from an IRA to another IRA without including the amount of the distribution in gross income, providing the rollover occurs within 60 days after the date of the distribution. An individual is allowed to engage in this type of rollover only one time during any three-year period.

Issues

The issues are: (1) whether an individual who receives a lump sum distribution from a qualified plan should be required to have been a participant in the plan for five years to be eligible to engage in a rollover of the distribution to an IRA or to another qualified plan, and (2) whether rollover contributions by an individual from one IRA to another IRA should be permitted more frequently than once every three years.

Explanation of provision

The amendment would remove the requirement that an individual must participate in the qualified plan from which he or she receives a lump sum distribution for five or more years in order to be eligible for a tax-free rollover of the distribution to an IRA or to another qualified plan. For individuals who received lump sum distributions in a taxable year beginning in 1978, but who could not engage in a tax-free rollover because of the five-year participation rule, the amendment extends the time period for making such rollovers until December 31, 1978.

The amendment also would remove the limitation on rollovers between IRAs which allows only one such rollover every three years. Thus, an individual would be allowed to make rollover contributions of amounts from one IRA to another at any time.

Effective date

The amendments made by this section would apply to taxable years beginning after December 31, 1977.

Revenue effect

It is estimated that this amendment would decrease budget receipts by less than $5 million annually.

Treasury position

The Treasury Department supports the provision of the amendment which would repeal the five-year rule. The Treasury Department opposes the provision of the amendment which would repeal the three-year rule because it believes that the provision would create certain abuse potential. The Treasury Department would support the provision, however, if it is amended to replace the three-year rule with a rule permitting one rollover a year.

IV. DESCRIPTION OF PROVISIONS OF PART III OF THE BILL RELATING TO CHANGES IN PENALTY PROVISIONS

A. Waiver of Excise Tax on Certain Accumulations in Individual Retirement Accounts or Annuities (sec. 31 of the bill and new sec. 4974(c) of the Code)

Present law

Under present law, an individual who has established an individual retirement account or an individual retirement annuity is required to begin receiving distributions of a certain minimum amount from the account or annuity not later than the end of taxable year in which the individual reaches age 70½. If an individual fails to make a required minimum distribution, the individual is subject to an accumulation penalty tax equal to 50 percent of the amount which was required to be distributed, but was not distributed.

Issue

The issue is whether the Secretary of the Treasury should be authorized to waive the 50-percent accumulation penalty tax.

Explanation of provision

The amendment would give the Secretary of the Treasury the power to waive the 50-percent accumulation penalty tax in circumstances where the individual subject to the tax establishes to the satisfaction of the Secretary that (1) the shortfall in the amount distributed was due to reasonable error, and (2) the individual is taking reasonable steps to remedy the shortfall.

Effective date

The amendments made by this section would apply to taxable years beginning after December 31, 1975.

Revenue effect

It is estimated that this amendment would have a negligible effect on budget receipts.

Treasury position

The Treasury Department supports the amendment.

B. Removal of Certain Limitations on Provision Allowing Correction of Excess Contributions (sec. 32 of the bill and sec. 4973(b) of the Code)

Present law

Under present law, a 6-percent excise tax is imposed on an excess contribution to an IRA. If for a taxable year an individual makes an excess contribution to an IRA but withdraws the amount of the contribution and any earnings thereon on or before the date prescribed by law for filing his or her tax return for the year, the 6-percent excise tax is not imposed if (1) the excess contribution resulted either from employer contributions to a qualified plan, governmental plan or tax-sheltered annuity, or from the failure of the individual to earn sufficient compensation for the year to make him eligible for the full amount of the contribution, and (2) the total amount withdrawn from the IRA does not exceed the excess of $1,500 ($1,750 in the case of a spousal IRA) over the amount allowable as a deduction for the year for a contribution to an IRA.

Issue

The issue is whether the dollar limitation on this method of correcting an excess contribution should be removed. Removal of the dollar limitation would facilitate the use of this method of correction in the case of excess rollover contributions.

Explanation of provision

Under the amendment, the dollar limitation would be removed. Thus, an individual makes an excess contribution to an IRA but withdraws the full amount of the excess contributed and any earnings thereon on or before the date prescribed by law for filing his or her tax return for the year (including extensions), the individual will be treated as not having made an excess contribution for the year. Accordingly, no 6-percent excise tax would be imposed for the year with respect to the excess contributed. The earnings on the excess contributed up to the date of withdrawal would be includible in the gross income of the individual for the year for which the excess contribution was made.

Effective date

The amendments made by this section would apply to contributions made for taxable years beginning after December 31, 1977.

Revenue effect

It is estimated that this amendment would have a negligible effect on budget receipts.

Treasury position

The Treasury Department supports the amendment.

V. DESCRIPTION OF PROVISIONS OF PART IV OF THE BILL RELATING TO SIMPLIFICATION OF RETURN REQUIREMENTS WITH RESPECT TO INDIVIDUAL RETIREMENT PLANS

(Sec. 41 of the Bill and Sec. 6058 of the Code)

Present law

Under present law, an individual who establishes an IRA is required to file a tax return with respect to the IRA for each year of its existence irrespective of whether, in any particular year, the individual makes contributions to the IRA, makes withdrawals or receives distributions from the IRA, engages in a prohibited transaction with respect to the IRA, or incurs a penalty tax with respect to the IRA.

Issue

The issue is whether the owner of an IRA should be required to file a tax return with respect to the IRA for any taxable year for which there is no penalty tax imposed with respect to the IRA and for which the owner of the IRA engages in no activity with respect to the IRA other than making deductible contributions to or receiving permissible distributions from the IRA.

Explanation of provision

Under the amendment, an individual would not have to file a tax return for an IRA for any taxable year (1) for which no penalty tax is imposed with respect to the IRA, and (2) for which no activity is engaged in with respect to the IRA other than making deductible contributions to and permissible distributions from the IRA.

Effective date

The amendments made by this section would apply to taxable years beginning after December 31, 1977.

Revenue effect

This amendment would have no effect on budget receipts.

Treasury position

The Treasury Department supports the amendment.