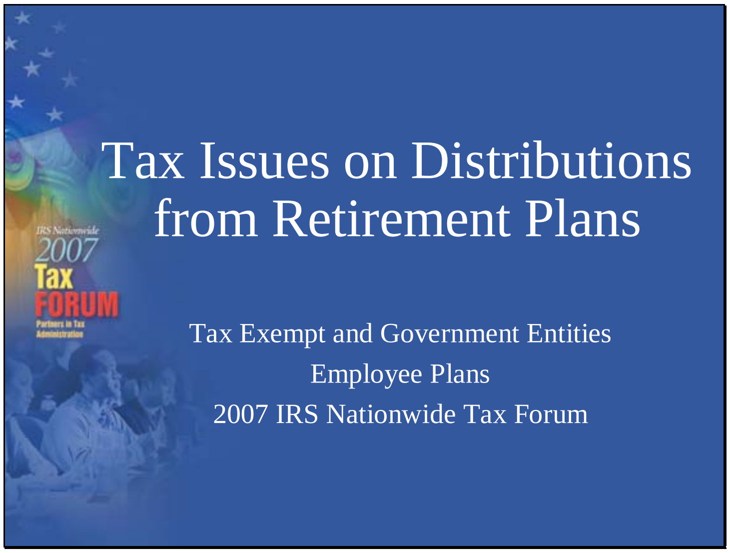
Slide 1




Hello everybody. Introduce yourself and give them a quick review of your bio and what you do at the IRS.

This presentation is going to focus on the tax issues on distributions on retirement plans before retirement, at retirement and after retirement. Mainly, we will be focusing on 401(k) plans and IRA-based plans: SEPs, SIMPLEs and SARSEPs.

Slide 2


We all need a little financial help from time to time. If employees have been making regular salary deferral contributions into their 401(k) plans, they may have accumulated a nice retirement nest egg. Many people look to that nest egg to help them out of a tight financial situation, for emergencies or to help pay for a home or college.

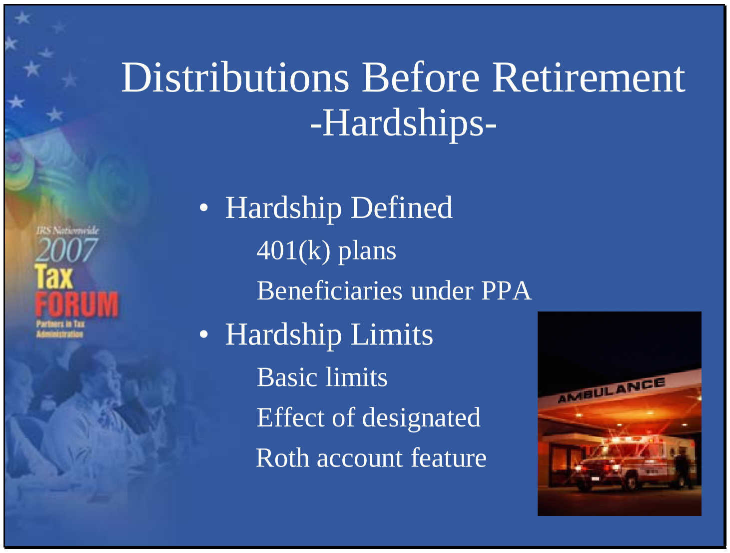
Not every type of plan can allow for participant loans. Any of the IRA-based plans, such as SEPs, SIMPLE IRAs and SARSEPs and traditional and Roth IRAs, cannot allow loans. However, qualified plans, such as profit-sharing, 401(k) and money purchase plans, may allow for loans. The plan document must include specific language that outlines the loan program before participants are allowed to borrow from their accounts.

Unless the loan meets the requirements spelled out in the Internal Revenue Code, it is taxable income to the participant. The amount a participant may take for a loan is limited to the lesser of 50% of their vested account balance or \$50,000. Payments are required to be made at least quarterly, over a period not exceeding 5 years (except for the purchase of a primary home) and must have a reasonable interest rate.  A plan may limit the number of loans, the length of the repayment period and may require payments be made more frequently, but at least quarterly.

When are there taxability issues with plan loans?  Loans that don't meet the requirements of the Code - that aren't limited to 50% of the vested account balance or exceed $50,000 become ordinary income to the participant.  Missing payments can throw the loan into default, again causing it to be taxed as ordinary income.  Sometimes, this is just a payroll mix-up.  Suddenly, the loan payments are no longer coming out of the participant's payroll check.  If it goes uncorrected there will be taxes to pay.  Some plans may provide for a "cure period" in which to make up missed payments.

The number one taxability issue with a loan occurs when a participant terminates employment with an outstanding loan balance.  In this case, plans usually offset the distribution of the participant's account by the amount of the outstanding loan balance.  If the participant doesn't roll over the offset amount with money from his or her own pocket, it will be includible in gross income.  The 10% early withdrawal additional tax may apply if the person is under age 59 ½.

Slide 3




First, the law and IRS guidance spell out the criteria used to determine if a hardship exists. You'll only find hardship distributions in defined contribution plans, such as 401(k), 403(b) and 457 plans. We'll confine our discussion today to 401(k) plans. A plan is not required to provide hardship distributions to participants. But if it does provide hardships, the plan must provide the *specific* criteria used to make the determination of hardship.

General legal requirements for a hardship distribution are:

There must be an "immediate and heavy financial need." I'm sure that many of you think, prior to Super Bowl Sunday that not having a big screen plasma TV is a hardship. The Regulations would disagree.

IRS has deemed an "immediate and heavy financial need" of the employee if the distribution is for:

- Medical expenses;
- Purchase of principal residence;
- Tuition and related education expenses;

- To prevent eviction;
- Funeral expenses; and
- Repairing casualty damage to the employee's house.

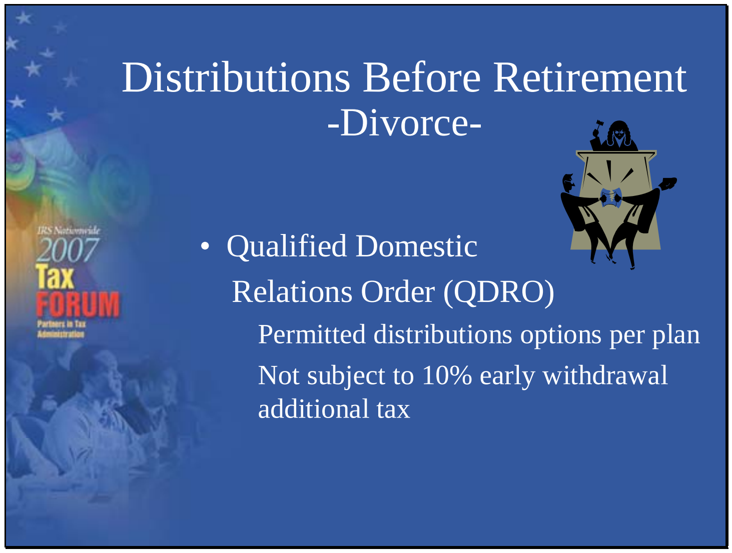
The Pension Protection Act (I'll refer to it as the PPA) modified the hardship rules to treat a participant's beneficiary the same as a participant's spouse and dependents for purposes of qualifying for a hardship distribution. In other words, a hardship distribution can now be made to a participant based upon the need of a grandchild or domestic partner as long as that individual has been designated as a beneficiary under the plan. This modification is only available for hardships related to medical, tuition, and funeral expenses.

Employers are not required to modify their plans to include this change; however, if an employer wants to make this option available, the plan document must be amended.

So how much is available for the hardship? A distribution on account of hardship must be limited to the distributable amount. The distributable amount is the total of all elective contributions as of the date of distribution, reduced by the amount of any previous distributions of elective contributions. With a Roth feature, any distribution from a designated Roth account is deemed to be a pro-rata portion of the Roth elective deferrals and earnings. The portion of a distribution from a Roth account attributable to earnings is subject to income tax and the 10% early withdrawal additional tax.

Hardship distributions should be used only as a last resort. The amount necessary to satisfy a financial need may include amounts necessary to pay any taxes or penalties reasonably anticipated to result from the distribution. For example, a participant has a vested account balance of $200,000, including $100,000 in elective deferrals and has a hardship requirement of $50,000. Assuming the participant is in a 25% tax bracket and is subject to the 10% early distribution additional tax, a distribution of approximately $77,000 would be required to in order to meet the hardship.

Slide 4




What about divorce?  In most states, the retirement plan account is up for grabs. Distributions to a spouse or another alternate payee, based on a qualified domestic relations order, or QDRO, may be based on a distributable event like a distribution based on termination or reaching retirement age, but a QDRO has its own set of rules.

First, the distribution option called for in the Domestic Relations Order (DRO) must be one offered by the plan.  If the plan offers a lump sum option only and the DRO calls for a ten-year payout, it won't be a qualified DRO.

Second, for QDROs, Federal law provides a very specific definition of earliest retirement age, which is the earliest date as of which a QDRO can order payment to an alternate payee (unless the plan permits payments at an earlier date). The earliest retirement age is the earlier of two dates:

- The date on which the participant is entitled to receive a distribution under the plan, or
- The later of either:
  - The date the participant reaches age 50, or

- The earliest date on which the participant could begin receiving benefits under the plan if the participant separated from service with the employer.

Third, a QDRO is not subject to the 10% additional tax on early distributions.

A plan must make the determination that a DRO is qualified within a reasonable period after receipt of the order.

A plan may charge the participant to make the determination a DRO is qualified.

Slide 5


**What happens if an employee separates from service before retirement age? Should the retirement account be left in the plan? Distributed? Rolled over to a new employer's plan or IRA? Here are some things to consider:** Does the plan offer an investment not available elsewhere, such as employer stock? Would the participant have easy access to the account, if needed? Is the participant allowed the same investment opportunities as participants in the old plan? Does the participant's new employer's plan offer better investment choices? Will the participant have access to those funds via plan loans or hardship distributions in the new employer's plan? Is the participant age 55 at separation?

**A 10% Additional Tax** under IRC section 72(t) applies to most distributions to participants under age 59 ½. This is in addition to the ordinary income tax paid on the distribution. When the 10% additional tax is tacked onto the Federal income tax and maybe even a state tax, many find these early distributions being reduced by a 40% plus tax bite. And mandatory withholding is only 20%. Needless to say, taxpayers find themselves coming up a little short on April 15.

The participant will not owe the 10% early withdrawal additional tax on distributions from a 401(k) plan if:

- The distribution was received after the participant left the company; and
- The participant left the company during or after the calendar year in which he or she reached age 55; and
- Their departure from the company qualifies as a separation from service.
- Note – the distributions do not have to begin immediately upon separation from service.

The participant will not owe the 10% early withdrawal additional tax on distributions made at any age if:

- The distribution was received after the participant left the company and they begin a series of substantially equal payments, at least yearly, based on the participant's life expectancy, or the joint life expectancy of the participant and their designated beneficiary, and
- The payments must be continued for at least five years or to age 59 ½, if later.
- Or due to the death or disability of the employee.

The separation from service at age 55 option is not available in an IRA. Once a participant rolls money out of their 401(k) into an IRA, any early distribution from that IRA is subject to the early withdrawal additional tax. With the recently changed rollover rules, IRA monies can now be rolled into a 401(k) plan. Upon separation from service, the full balance in the 401(k) account, including the money rolled in from the IRA, is eligible for the age 55 option to avoid the 10% additional tax. As you can see, it's important to make some decisions prior to taking a distribution or rollover of a 401(k) account.

Slide 6


A participant terminating employment with a vested account balance greater than $5,000 is not required to take a distribution from any plan prior to reaching Normal Retirement Age.  However, if they consent to take a distribution, the plan is required to offer a direct rollover distribution option.  A participant can set up an IRA account with a financial institution, give this information to the plan administrator, and then select the rollover option for the distribution from the plan. In a direct trustee-to-trustee rollover, there are no tax consequences.

A participant with an account balance between $1,000 and $5,000 may be subject to an automatic rollover.  Prior to March 2005, plan administrators typically distributed, or cashed-out, account balances of less than $5,000 straight to the participant, less the required 20% withholding.  Not only did participants spend the distributed funds instead of saving them, they also didn't save for the additional taxes the 20% withholding didn't cover.

Effective March 28, 2005, for account balances between $1,000 and $5,000, a plan is required to set up an IRA in the name of the participant and then make a direct rollover of the funds to the account but only if the participant does not elect to receive the funds directly or have them rolled over to a plan or IRA specified by the participant.  In reality, most plans do their best to contact participants prior to setting up an IRA in their name.  They would prefer to make a direct rollover of the funds to the participant's own IRA if at all possible.

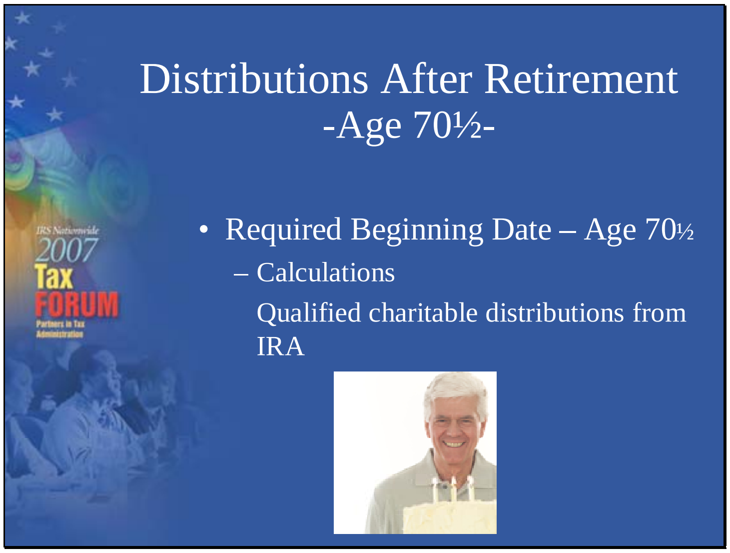
Rollovers from a Roth 401(k) to a Roth IRA have a special rule:  The age of the designated Roth contributions is not taken into account in determining the 5-year period for qualified distributions from a Roth IRA.  Thus, if a participant, under age 59 ½ takes a distribution from his 10-year-old designated Roth account in his former employer's 401(k) plan and uses the money to open his first Roth IRA, he must wait at least 5 years before he can get a qualified distribution from the Roth IRA.  A qualified distribution is not taxable.

All eligible rollover distributions to participants are subject to a required 20% withholding.  If the participant subsequently decides to rollover the distribution within 60 days, they can use their own funds to make up the 20% withheld from the original distribution.

An individual that didn't meet the 60-day deadline for rolling funds over to their IRA or to another qualified plan may apply for a private letter ruling, asking the IRS to waive that requirement.  The fee for those rulings has increased significantly, from $95 to upwards of $3,000.  If the reason for missing the 60-day deadline is legitimate and out of the control of the taxpayer, the IRS will likely approve the request.

Or an individual can always take the money and run.  Live for today.  Don't worry about money at retirement; we'll always have social security to fall back on.

Slide 7




Distributions from a 401(k) or other qualified plan must begin by April 1 of the year following the year the participant reached age 70 ½. The second distribution is due by December 31 of that same year, with distributions to follow by each subsequent December 31. If the participant is not a 5% owner of the employer and is still employed, a required minimum distribution, or RMD, is not required until employment is terminated. Chapter 1 of Pub 590 contains detailed instructions on how to determine the RMD. There is some confusion among participants between the April 1 and April 15 dates, but the first payment is due by April 1 of the year following the year the participant reached age 70 ½ or terminated employment in the case of non-5% owners. There is also some confusion if there is more than one retirement account. If the participant has more than one qualified plan retirement account, a separate required minimum distribution must be determined for each account and taken from each account.

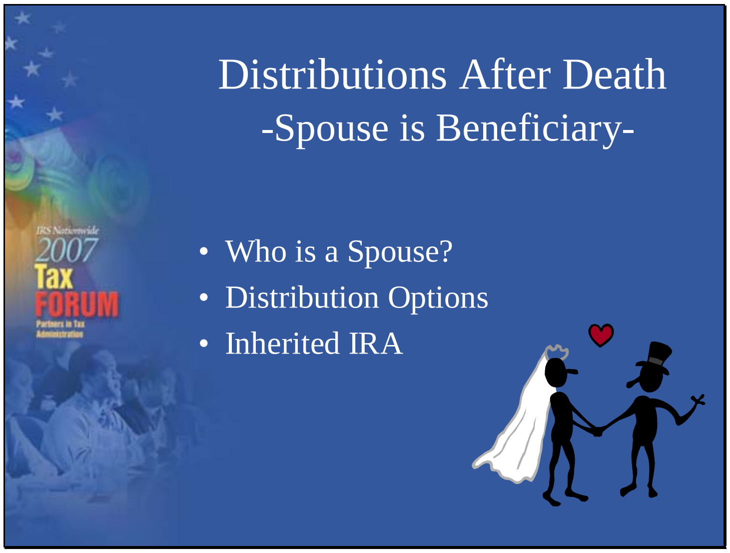
The only difference in the RMD calculation for a traditional IRA, SEP or SIMPLE is that distributions must begin at age 70 ½. An IRA owner must begin distributions by April 1 following the year he or she turned 70 ½; however, if a participant in a 401(k) plan is still employed at age 70 ½, the RMDs can wait until the participant is no longer employed, assuming a non-5% owner.  Additionally, financial institutions should provide a calculation of the RMD for each IRA. Unlike qualified plans, as long as the total amount of the RMDs for all IRAs owned by one individual is timely distributed, a RMD for one IRA owned by the individual can be taken from another IRA owned by the same individual.  There are no RMD requirements for a Roth IRA while the owner is alive.  However, designated Roth contributions in a Roth 401(k) account are subject to the regular RMD rules.

Under the PPA, for the 2006 and 2007 taxable years only, an IRA owner may exclude from income up to $100,000, including a RMD that is contributed directly to a qualified charitable organization.

- The maximum amount that can be excluded is $100,000 per individual per year.
- It must be made to a qualified charitable organization as described in the Code.
- This is also available for distributions from an IRA maintained for the benefit of a beneficiary after the death of the IRA owner.
- The contribution must be made by a direct rollover from the IRA to the qualified charitable organization.

If it’s determined the contribution was not a qualified charitable contribution, it is includible in income and whether or not it’s deductible depends on the normal rules for charitable contributions.

Slide 8




Most retirement plans and IRAs are not intended to permit the permanent deferral of the payment of income taxes. As a result, rules have been established to ensure distributions are made from the accounts and taxes paid, when applicable. Congress didn't want the money taken out too early, thus the 10% additional tax on early withdrawals, but Congress does not want money to remain indefinitely in retirement accounts.

We're going to talk about distributions from retirement accounts and IRAs after the death of the account holder.

First up – Post death options for the surviving spouse who is the designated beneficiary. This is the *easy one* and generally works for both IRAs and Retirement Accounts.

Who is a spouse?

- Some states recognize domestic partnerships or civil unions or same sex marriages, so some have asked how this affects spousal rollover rules.

- The Federal Defense of Marriage Act states that a marriage for Federal Law purposes is a legal union between one man and one woman and the word “spouse” refers to the person of opposite sex who is a husband or wife.
- This precludes domestic partners, individuals who enter into civil unions or into same sex marriages from being treated as surviving spouses under the rollover rules.
- Certain states have “common law marriage” statutes that deem certain couples as being married even without a legal ceremony. If the participant is in such a state and meets these common law marriage requirements, he/she may meet the Defense of Marriage Act legal union requirement to be called a spouse and be eligible to be treated as a surviving spouse under the rollover rules.

The surviving spouse is the only beneficiary entitled to full rollover rights. We’ll talk about the non-spouse beneficiaries on the next slide.

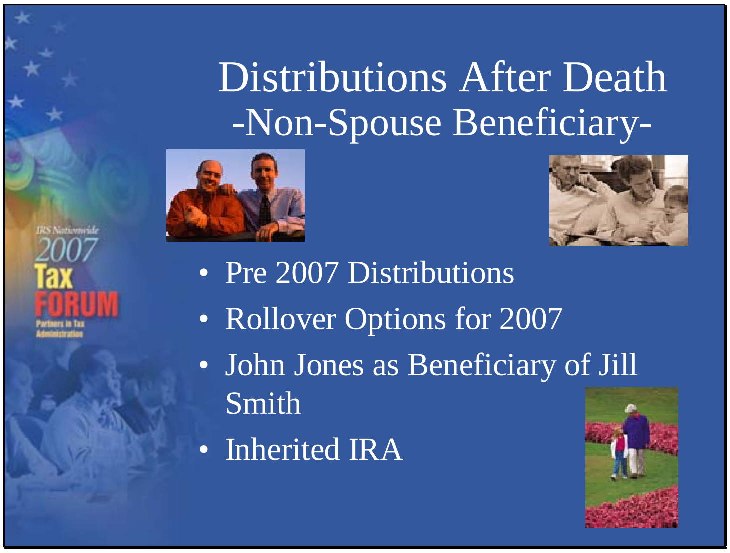
Payments to the surviving spouse are controlled by the plan document. Certain payments are not eligible for rollover treatment. For example, if the participant elects payout in the form of a joint and survivor annuity or a 10-year certain, payments made pursuant to such an election are not eligible for rollover treatment. However, lump sum payouts are eligible and we’ll limit our discussion to those distributions.

Several options exist with respect to distributions from a retirement account: A surviving spouse can take the distribution and pay ordinary income tax. If paid to a surviving spouse on account of the death of a plan participant or IRA owner, a distribution is not subject to the 10% early withdrawal additional tax.

If a surviving spouse is the sole designated beneficiary, he or she can treat the IRA of a decedent as his or her own IRA. Once it’s the surviving spouse’s IRA, funds continue to grow tax-deferred and distributions are not required until the spouse's required beginning date, unless it's a Roth IRA.  A surviving spouse can do this even if the participant had begun taking required minimum distributions. Early distributions from the surviving spouse's IRA are subject to the 10% early withdrawal additional tax.

Another option is that any beneficiary can opt to disclaim his or her interest in the decedent's IRA or plan account.  A valid disclaimer must be accomplished within nine months after the year of death of the decedent.  Disclaiming the IRA or plan account allows the account to pass to a secondary beneficiary.  This could make sense depending on the beneficiary's tax planning strategy.

Slide 9




Now, we’re on to a non-spouse beneficiary.

If the beneficiary is a non-spouse beneficiary, the distribution options are a little more complicated.

Plan documents may contain language that allows for distributions after a participant’s death to be made in a lump sum, or over a five year period, or under the life expectancy rule when the participant died before his or her required beginning date, (RBD). Plans need not, and many do not permit distributions to be made to beneficiaries under the life-expectancy rule. Most plans only provided for non-spouse beneficiaries to be paid in lump sum distributions or by distributions under the five year rule (funds have to be paid to the non-spouse beneficiary no later than December 31 of the calendar year which contains the fifth anniversary of the death of the decedent). No distributions made to non-spouses prior to 2007 were eligible for rollover. Distributions to beneficiaries are not subject to the 20% withholding requirement or the 10% early distribution tax.

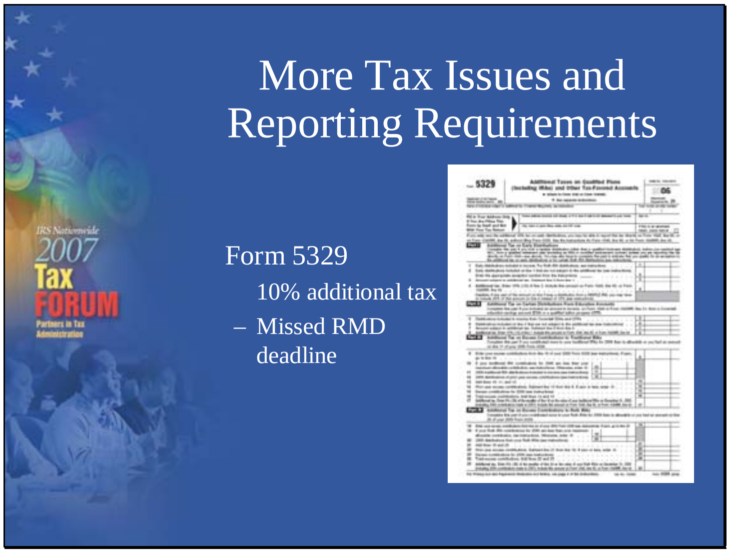
Beginning in 2007, a non-spouse beneficiary may roll over, but only by means of a trustee-to-trustee transfer, the inherited retirement plan account to an IRA. Beneficiaries who may take advantage of this new rollover option include parents, children, friends, and domestic partners. It's not limited. A plan is allowed to adopt language allowing non-spouse beneficiaries to roll over distributions to an IRA, but they aren't required to make that change. A distribution paid directly to a non-spouse beneficiary may not be rolled over. A recipient/transferee IRA should be titled "John Jones as beneficiary of Jill Smith" or something very similar. Such language reflects that Jill Smith is deceased and that John Jones is receiving amounts from the IRA as Jill Smith's beneficiary. John Jones is not the owner of the IRA. Generally, the RMD rules in the IRA are the same as those in effect in the plan document at the time of death. However, the IRS has issued guidance that allows payouts under the IRA to be made using the life expectancy rule in certain cases, regardless of what the plan required.

If the plan participant died prior to attaining his/her RBD, distributions from the transferee IRA need to begin, using the life expectancy rule, by the end of the year following the year of the participant's death. If the plan participant dies after attaining his or her RBD, beginning with the year after the year of death, distributions will be made based on the life expectancy of the beneficiary.

How does this differ from an IRA where the IRA owner dies leaving the account to a non-spouse beneficiary? An inherited IRA cannot be rolled over and it is required to make distributions according to the terms of the IRA. Thus, as with qualified plans, RMDs may be made using the 5-year rule or the life-expectancy rule where the IRA owner dies prior to attaining his or her RBD. If an IRA owner dies after attaining his or her RBD, beginning with the year after the year of death, distributions will be made based on the life expectancy of the beneficiary.

If you or your clients have funds in a retirement plan, you should check with the plan administrator to see if the plan will allow for the non-spouse beneficiary direct rollover.  If not, a distribution to a non-spouse is likely to be made in an immediate lump sum, taxable all at once.

Slide 10




In some cases, Form 5329 is used to report and pay the early distribution additional tax for distributions from IRAs and retirement plans that we have discussed in earlier slides.  If the Form 5329 is not required and the tax applies, it’s paid on line 60 of Form 1040.

Exceptions for early distributions from an IRA or qualified plan include:

- Rollovers to a new retirement account.
- Participant dies or is disabled.
- Substantially equal periodic payments.
- Qualified Reservist Distributions.
- Under the PPA, effective for plan years beginning after December 31, 2007, contributions under an Automatic Enrollment Safe Harbor plan may be distributed during the 90 days following the first automatic contribution made on behalf of the employee.
- Also under the PPA, effective for plan years beginning after December 31, 2007, distributions of excess contributions from an Automatic Enrollment Safe Harbor plan that are distributed within 6 months after the close of the plan year of the testing failure.

What happens if a participant missed their RMD deadline? They may owe a 50% excise tax on the amount of the missed RMD. It goes without saying that we're not that interested in taking a big piece of money grandma planned to live on for the rest of her life. So what needs to be done if a deadline has been missed is to go ahead and start making corrections. First, calculate the total RMD due and withdraw it from the IRA or retirement plan account. Next, the participant will need to file a Form 5329 with their 1040. If the deadline was missed due to a reasonable cause, a waiver of the excise tax may be requested. Again, we're not here to take grandma's retirement savings, so you'll find many of these requests are accepted by the IRS and the tax waived. Even though we are a kinder, gentler IRS, if you keep forgetting, or the amounts are substantial, the 50% excise tax may not be waived.

Slide 11


IRS sponsors a voluntary correction program, the Employee Plans Compliance Resolution System (EPCRS). Under this correction program, plan sponsors are allowed to correct a variety of errors, many times without ever contacting the IRS or paying any sanction. The basic premise with this program is to have the plan sponsor become more involved in making certain the plan is being properly operated. There are three different programs available:

- Self-Correction is available for many errors discovered within two years of the year the error occurred and generally include more common operational errors. These errors can be fixed by the sponsor without IRS involvement.
- Voluntary Correction is available for more significant operational errors and errors in form. These errors do require an application to the IRS and involve a sanction.
- Audit CAP – This piece is available for errors found during an IRS audit of the plan. Sanction amounts can be significantly higher than the other programs, but the plan does retain its qualified status.

As we attempt to expand this program to smaller businesses and make it more accessible to plan sponsors who don't have an ERISA attorney on the payroll, you can expect a more simplified look at EPCRS on our web site. Publication 4050, *Retirement Plan Correction Programs CD-ROM,* contains all of the information that you will need to use these programs. The CD can be ordered from our web site or you may pick up a copy at the TE/GE booth in the Exhibit Hall.

Let's look at a couple of mistakes from our presentation today and see how they might fit into the EPCRS Correction Program.

If the mistake is a failure to roll over a distribution from an IRA or retirement plan within the 60-day period, the only option available is to request a private letter ruling. Lay out the facts, pay the fee and get the ruling. EPCRS is not available for this error.

If the mistake is a failure to make the required minimum distributions from a retirement plan, EPCRS may be used to make correction. There are basically two different errors here. Not only were the RMDs not made, but the plan contains language requiring the RMDs. So if they weren't made, the plan was not operated in accordance with a plan requirement and could lose its tax-qualified status for the error. Under EPCRS, the plan can use Self-Correction by making the required distributions as long as correction is made within two years following the year the error occurred. Each individual would be required to file a Form 5329 and request a waiver of the 50% additional tax.

If the plan files a Voluntary Correction application with the IRS, it will still correct by making the required distributions. But it can also use the correction application to request a waiver of the 50% additional tax for all the affected participants. If approved, a Form 5329 and waiver request is not required by the individual participants. EPCRS is not available for a missed RMD from an IRA.

EPCRS is only available for errors involving retirement plans, and IRA-based plans, such as SEPs or SIMPLEs.

Slide 12


We at the IRS have developed many tools to assist you and your clients in the retirement plan area, whether your question is “How do I choose a retirement plan?” or “How much money can I contribute to my retirement plan?” or “This plan isn’t working for me anymore.  How do I terminate it?”

You can visit our web site at www.irs.gov/ep.  The Retirement Plans Community web page can be found on the main www.irs.gov landing page.  You will find information for “Benefits Practitioner,” “Plan Participant/Employee” and “Plan Sponsor/Employer.”  The pages are populated with all of the retirement plan information that you have come to expect from EP. One recent addition to the web page is the page dedicated to the Pension Protection Act of 2006.

There are two different ways that you can discuss your questions with a retirement plan specialist.  You can call our Customer Account Services at (877) 829-5500. This is a toll-free number. The call center is open 8:30am to 4:30pm Eastern Time.

If you would prefer, you can e-mail your questions to RetirementPlanQuestions@irs.gov. All questions submitted via e-mail must be responded to via telephone, so please remember to include your phone number in your message and a customer service representative will call you with the answer to your questions.

Finally, we have two free Newsletters that you can subscribe to. The first is the *Employee Plans News*. This newsletter is geared toward the practitioner community and is more technical and involved than our newsletter geared toward plan sponsors, *Retirement News for Employers*. Each is an electronic newsletter and is posted on our web site as a PDF document each quarter. Being a web-based product, the newsletters make an excellent reference guide as they are chock-full of embedded links to guidance sources, products and other sites.

Subscribing to these newsletters will keep you and your clients abreast of all the latest news regarding retirement plans, legislation, trends and tips on various subjects, as well as keeping you informed of the latest product releases from the office of Employee Plans Customer Education & Outreach!

Subscribing is easy. Just go to “Newsletters” under our web page, www.irs.gov/ep, click on “Employee Plans News” or “Retirement News for Employers,” click on “Subscribe,” then provide us with your e-mail address. That’s all it takes.

You will receive a message in your e-mail inbox alerting you to when our latest issues or Special Editions are posted on our web page with a link directing you to the newsletter when you are ready to read it.

Please be sure to attend our presentation on “Automatic Enrollment and Other Need-To-Know Provisions of the Pension Protection Act of 2006,” which will focus on the need-to-know provisions of the PPA that are currently effective and relate to defined contribution plans.  As a bonus feature, it will discuss the Automatic Enrollment provisions effective in 2008.

Thank you for your attention and please stop by the TE/GE booth for additional retirement plan information.