Significant Index No. 72.20-04

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

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MAR 05 2002

In re: Request for ruling on behalf of

Taxpayer N =

This letter is in response to your request, dated September 28, 2001, for a ruling on behalf of yourself as to whether certain proposed distributions from an individual retirement account (IRA 1) owned by you are part of a series of substantially equal periodic payments and are therefore not subject to the 10 percent additional tax imposed on premature distributions under section 72(t) of the Internal Revenue Code (Code). The ruling request was amended by you in a telephone call with of our office on January 14, 2002, to clarify the facts and the methodology used to calculate distributions.

According to the facts as stated, following your retirement in 1998 you rolled over your benefit under a section 401(k) plan sponsored by your employer into an IRA (IRA 1) established with an investment firm to receive your benefit. You will attain age 56 in 2002. Taxpayer N is your spouse and is a beneficiary of IRA 1. After seeking advice from professional financial advisors with respect to retirement planning, you started receiving distributions from IRA 1 in July 1998. Because you wanted to avoid the additional tax imposed on early distributions under section 72(t) of the Code, you had your financial advisors calculate distribution amounts in a form intended to satisfy the section 72(t)(2)(A)(iv) exception for substantially equal periodic payments. After having your financial advisors calculate distribution amounts for three years, you decided to calculate the distribution amounts yourself using the same methodology, and to request a ruling from the Service that your method of calculating periodic payments produces substantially equal periodic payments as described in section 72(t)(2)(A)(iv) of the Code. You propose to calculate a monthly distribution for 2002 and subsequent years by first calculating a yearly distribution amount, which is then divided by 12 to yield a monthly distribution amount. The annual distribution amount for 2002 is calculated by amortizing the account balance of IRA 1 as of December 31, 2001, over a number of years (term certain) equal to your life expectancy (obtained from Table V of section 1.72-9 of the Income Tax regulations, using the age attained by you in 2002), at an assumed interest rate of earnings of 7 percent. The annual distribution amount is then

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divided by 12 to determine a monthly distribution amount. To determine the annual distribution amount for 2003 and subsequent years, similar methodology will be used. That is, the account balance of IRA 1 as of December 31 of the prior year will be amortized over a number of years equal to your life expectancy (obtained from Table V of section 1.72-9 of the regulations, using the age attained by you in the year for which you are calculating distributions), at an assumed interest rate. Beginning with the calculation of the 2003 annual distribution amount and continuing for subsequent years thereafter, the interest rate used each year will be 120 percent of the federal mid-term rate in effect for the month of January of the year for which distributions are being calculated. All distributions will be taken from IRA 1 and only from IRA 1.

Ruling Requested

Based on these facts, you have requested the following ruling.

The proposed method of determining periodic payments satisfies one of the methods described in Notice 89-25 and results in substantially equal periodic payments within the meaning of section 72(t)(2)(A)(iv) of the Code, and such payments will not be subject to the additional tax of section 72(t)(1) unless the requirements of section 72(t)(4) are not met.

Applicable Law

Section 408(d) of the Internal Revenue Code provides that amounts paid or distributed out of an individual retirement plan must be included in gross income by the payee or distributee in the manner provided under section 72 of the Code.

Section 72 of the Internal Revenue 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) of the Internal Revenue Code was added to the Code by the Tax Reform Act of 1986 (TRA '86), effective generally for taxable years beginning after December 31, 1986. 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 the joint lives (or joint life expectancies) of such employee and his 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 (1) the close of the 5-year period beginning with the date of the first payment, and (2) the employee's attainment of age 59 1/2, 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.

Section 1.72-9 of the Income Tax Regulations (Regulations) provides tables that are to be used in connection with computations under section 72 and the regulations thereunder. Included in this section are tables giving life expectancies for one life (Table V) and joint life and last survivor expectancies for two lives (Table VI). Excerpts from these tables can be found in Table I (Single Life Expectancy) and Table II (Joint Life and Last Survivor Expectancy) of Appendix E in IRS Publication 590, Individual Retirement Arrangements (IRAs).

Notice 89-25, 1989-1 C.B. 662, provides 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 for determining substantially equal periodic payments for purposes of section 72(t)(2)(A)(iv) of the Code. Two of these methods involve the use of an interest rate assumption that must be an interest rate that does not exceed a reasonable interest rate on the date payments commence.

Proposed Methodology

The proposed method for determining annual periodic payments described in the ruling request, as modified, is to calculate an end of year annual distribution amount for 2002 by amortizing the account balance of IRA 1 as of December 31, 2001, over a number of years (term certain) equal to your life expectancy (obtained from Table V of section 1.72-9 of the regulations, using the age attained by you in 2002), using an annual effective interest rate equal to 7 percent. The annual distribution amount divided by 12 is equal to the monthly distribution amount. To calculate an annual end of year distribution amount for 2003 and subsequent years, the account balance of IRA 1 as of December 31 of the prior year will be amortized over a number of years (term certain) equal to your life expectancy (obtained from Table V of section 1.72-9 of the regulations, using the age attained by you in the year for which distributions are being calculated), at an interest rate equal to 120 percent of the annual federal mid-term rate

(used for purposes of Code section 1274(d)) in effect for the month of January of the year for which calculations are being done. The monthly distribution amount is equal to the annual distribution amount divided by 12. All distributions will be taken from IRA 1, and only from IRA 1.

Conclusion

The interest rate and life expectancy used are such that they do not result in the circumvention of the requirements of sections 72(t)(2)(A)(iv) and 72(t)(4) of the Code (through the use of an unreasonably high interest rate or an unreasonable life expectancy).

Accordingly, we conclude that the proposed method (as modified) of determining periodic payments satisfies one of the methods described in Notice 89-25 and results in substantially equal periodic payments within the meaning of section 72(t)(2)(A)(iv) of the Code, and such payments will not be subject to the additional tax of section 72(t) unless the requirements of section 72(t)(4) are not met.

If you have questions you can contact at (not a toll-free number). In any correspondence with respect to this case, you should also refer to

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

Sincerely yours,

Martin L. Pippins

Martin L. Pippins, Manager
Employee Plans Actuarial Group 2
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