

[Our Services](#)

Nov. 2, 2012

[Office Locations](#)

**GOVERNMENTAL PLAN ALERT:
The Importance of Proper Coding
for Form 1099-R Reporting**

[Our People](#)

[Search Our Site](#)

The 2012 tax year is winding down and many retirement systems are continuing to gather information to report to the Internal Revenue Service (IRS) with regard to distributions made from their retirement plans. While processing distribution information to determine how to complete Form 1099-R for distribution recipients, retirement systems will also be looking at a significant list of codes that should appear in Box 7 of the Form. A list of these codes may be found in the [2012 Instructions](#) for the [Form 1099-R](#) (2012 Instructions).

It is important to recognize the significance of proper coding for Form 1099-R. Guidance in the 2012 Instructions states that the IRS uses the codes in Box 7 to determine if the recipient has properly reported the distribution on his/her personal taxes. The guidance further notes that if the distribution codes are not entered correctly on the Form, the IRS may improperly propose changes to the recipient's taxes. This alert provides some information about common reporting and coding fact scenarios and errors that may occur with respect to Form 1099-R.

[Read More](#)

If you have any questions or would like additional information about Form 1099-R reporting for 2012, please contact any member of Ice Miller's [Employee Benefits Group](#) or:



[Mary Beth
Braitman](#)



[Lisa Erb
Harrison](#)



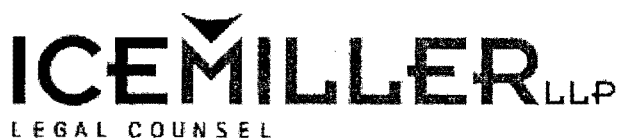
[Terry A.M.
Mumford](#)



[Tiffany
Sharpley](#)

This publication is intended for general information purposes only and does not and is not intended to constitute legal advice. The reader must consult with legal counsel to determine how laws or decisions discussed herein apply to the reader's specific circumstances.

Copyright (c) 2009-2012 Ice Miller LLP and its licensors. All rights reserved.



The Importance of Proper Coding for Form 1099-R Reporting

Nov. 2, 2012

Lisa Erb Harrison, Tiffany Sharpley, Terry A.M. Mumford, Mary Beth Braitman

The 2012 tax year is winding down and many retirement systems are continuing to gather information to report to the Internal Revenue Service (IRS) with regard to distributions made from their retirement plans. While processing distribution information to determine how to complete Form 1099-R for distribution recipients, retirement systems will also be looking at a significant list of codes that should appear in Box 7 of the Form. A list of these codes may be found in the 2012 Instructions for the Form 1099-R (2012 Instructions).

It is important to recognize the significance of proper coding for Form 1099-R. Guidance in the 2012 Instructions states that the IRS uses the codes in Box 7 to determine if the recipient has properly reported the distribution on his/her personal taxes. The guidance further notes that if the distribution codes are not entered correctly on the Form, the IRS may improperly propose changes to the recipient's taxes. This alert provides some information about common reporting and coding fact scenarios and errors that may occur with respect to Form 1099-R.

Here is a typical scenario for retirement distributions at normal retirement:

Example: In June 2012, Mr. Z, age 65, retires from a governmental employer that participates in Retirement System Y. Mr. Z does not plan to work any other place for that governmental employer. Mr. Z elects to receive a monthly annuity payable for his lifetime. Retirement System Y sends to the IRS and Mr. Z a 1099-R that provides the amount of Mr. Z's distributions for 2012 in Box 7 coded with a "7" for "normal distribution". This is the correct and very common procedure for issuing 1099-Rs.

In the remainder of this alert, we provide examples that address problems or unique scenarios involving lump sum distributions followed by examples of situations that affect annuity distributions.

Lump Sum Distribution Examples:

Example #1: Mr. B, age 62, separates from service from the governmental employer that participates in Retirement System X to work for another employer. Mr. B receives a lump sum distribution in 2012 and he does not rollover the distribution to an IRA or other eligible retirement plan. Retirement System X, while completing Mr. B's Form 1099-R, unintentionally completes Box 7 using code "1" (an early distribution prior to age 59½ with no known exceptions), instead of using code "7" (a normal distribution after age 59½). Retirement System X enters the taxable amount in Box 2a. Mr. B completes his 2012 tax forms and he files with the IRS. In this instance, Mr. B may receive an IRS notice seeking to adjust his return to include the 10% penalty tax on distributions made prior to age 59½.

Example #2: Ms. A, age 55, separates from service from the governmental employer that participates in Retirement System Y to work for another employer. Ms. A receives a lump sum distribution in 2012 and she does not rollover the distribution to an IRA or other eligible retirement plan. Retirement System Y, while completing Ms. A's Form 1099-R, unintentionally completes Box 7 using code "7" (a normal distribution on or after age 59½), instead of using code "2" (an "early distribution, exception applies"). Retirement System Y enters the taxable amount in Box 2a. Ms. A files her 2012 tax forms with the IRS. In this instance, Ms. A may receive an IRS inquiry about the coding.

Example #3: Mrs. C, age 62, separates from service from an employer that participates in Retirement System Z in 2012 and requests that her account in Retirement System Z's retirement plan be distributed in two portions – an amount to be distributed to Mrs. C and the remaining amount to be directly rolled to an IRA. Retirement System Z distributes Mrs. C's account balance as directed. However, when Retirement System Z completes Mrs. C's Form 1099-R, it inadvertently prepares only one Form 1099-R (instead of a separate Form 1099-R for each portion of the distribution). Retirement System Z unintentionally completes Box 1 for the total amount of the distribution (including the direct rollover portion), and completes Box 2a for only the taxable amount of the lump sum portion of the distribution. Box 7 is coded "7" ("normal distribution"). In this case, Mrs. C may receive IRS notice seeking to adjust her return to include taxes for the entire distribution amount reported.

In each of these examples, the Retirement System should provide corrected 1099-Rs if the Retirement System is aware of the IRS inquiry or otherwise becomes aware of the incorrect coding.

Annuity Distribution Examples:

It is important to note that the proper coding of Box 7 depends on facts like the member's age and whether he/she separated from service. Below are a couple of examples which highlight the importance of the facts in the context of annuity distributions.

Example #4: Ms. D, age 57, qualifies under the Retirement System B plan to begin her lifetime monthly distribution before she separates from service. Ms. D elects to begin this payment. Retirement System B commences the distribution payments and codes Box 7 of her Form 1099-R for that year as a "1" ("early distribution, no known exception"). This means that Ms. D will have to pay a 10% penalty on her distributions until she reaches age 59½. This is the correct method to code Box 7 in this situation. Ms. D should be informed of the penalty prior to her commencement of her monthly annuity.

In the year in which Ms. D turns 59½, Retirement System B must calculate the amount of retirement benefits Ms. D received during the year before she attained age 59½ and the amount she received upon attaining age 59½ and throughout the remainder of the year. The amount of her distributions prior to attaining age 59½ and at age 59½ and beyond are reported on two (2) separate Forms 1099-R. Box 7 of the Form 1099-R that includes the pre-59½ amount is coded with a "1" ("early distribution, no known exception"), while the other Form 1099-R is coded with a "7" ("normal distribution"). This is the correct process to follow when reporting in-service distributions for a member in the year in which he/she turns 59½ because the 10% penalty only applies to distributions prior to attaining age 59½.

Example #5: Mr. E, age 57, qualifies under Retirement System A to begin his lifetime monthly distribution after he separates from service. Retirement System A commences the distribution payments and codes Box 7 of his Form 1099-R for that year as a "2" ("early distribution, exception applies"). This means that Mr. E will have not to pay a 10% penalty on his distributions. In the year in which Mr. E turns 59½, Retirement System A must calculate the amount of retirement benefits Mr. E received during the year before he attained age 59½ and the amount he received upon attaining age 59½ and throughout the remainder of the year. The amount of his distributions prior to attaining age 59½ and at age 59½ and beyond are reported on two (2) separate Forms 1099-R. Box 7 of the Form 1099-R that includes the pre-59½ amount is coded with a "2" ("early distribution, exception applies"), while the other Form 1099-R is coded with a "7" ("normal distribution").

As you may expect, there are many more reporting and coding scenarios that affect Form 1099-R. This alert just addresses a few common occurrences. If you have any questions or would like additional information about Form 1099-R reporting for 2012, please contact Mary Beth Braitman, Terry A.M. Mumford, Lisa Erb Harrison, Tiffany Sharpley or any member of Ice Miller's Employee Benefits Group.

This publication is intended for general information purposes only and does not and is not intended to constitute legal advice. The reader should consult with legal counsel to determine how laws or decisions discussed herein apply to the reader's specific circumstances.

Resources

© 2003-2012, Ice Miller LLP

Web design and development by BitWise Solutions, Inc.