

Stop Repaying Loan From Retirement Fund Equals Income and Penalty

Gerard McEnroe was under 59.5. He had worked for the New York City School Construction Authority (SCA) for 15 years as of the year at issue in this case. He participated in SCA's retirement plan, New York City Employees Retirement System (NYCERS).

In July 2014 Mr. McEnroe borrowed a little over \$26,000 from NYCERS to pay college tuition expense for one of his children. He immediately started paying it back through biweekly payroll withholding.

During May 2015, Mr. McEnroe left SCA and went to work for a new employer. During September 2015, after growing disillusioned with his new employer, Mr. McEnroe went back to SCA.

He did not make the loan repayments during the time he was not employed with SCA. When he returned he found out NYCERS had determined that the outstanding loan balance of \$22,284 would be treated as a distribution. He contacted SCA's HR department which sent an email to NYCERS explaining Mr. McEnroe's departure and subsequent return to SCA. NYCERS replied that it would "process a revision and it will be done for 11/20/15." In early 2015, Mr. McEnroe resumed making loan payments through biweekly payroll withholding.

A Form 1099-R was issued by NYCERS showing the entire \$22,284 as a distribution. Mr. McEnroe filed his 2015 return without reporting this 1099-R. IRS assessed tax and the 10% early distribution penalty on this \$22,284. Mr. McEnroe claimed it was not taxable since the loan was "reinstated."

Tax Court sided with IRS that the amount was deemed to have been distributed in 2015. Tax Court referred to Regulation 1.72(p)-1, Q&A 10(a) which provides that in the event of an overdue payment, plan administrators may allow a cure (grace) period to make up the missing payment(s). The regulation further states this grace period cannot continue beyond the last day of the calendar quarter following the calendar quarter in which the required installment payment was due. Since Mr. McEnroe failed to make payments starting in June, the second quarter of the year, the grace period would have expired September 30, 2015, the last day of the third quarter of the year. Further Mr. McEnroe did not make a lump sum payment to try to cure the earlier default. Since Mr. McEnroe did not resume making payments until December 2015, the \$22,284 balance of the loan is required to be considered distributed.

Gerard & Regina McEnroe, T.C. Summary 2019-21. This case can be found by going to ustaxcourt.gov, clicking on the Opinion Search tab, and entering McEnroe in the Case Name box.

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