Federal Update 2004-2

February 2, 2004

TO: NCTR Members

FROM: Cindie Moore, Washington Counsel

RE: Administration's Savings Proposal Released

As expected, the Bush Administration released on February 2 its savings proposal as part of its Fiscal Year 2005 Budget. The proposal, issued through the Department of the Treasury, has two parts. The first part would create two new individual savings vehicles: Retirement Savings Accounts (RSAs) and Lifetime Savings Accounts (LSAs). The second part would set up an employer-provided vehicle known as an Employer Retirement Savings Account (ERSA). The ERSA would be a consolidation, into one plan, of existing types of plans such as 401(k)s, 403(b)s, and 457s. A brief summary of each item appears below. See http://www.treas.gov/press/releases/js1131.htm for a copy of Treasury's press release.

The proposal is similar to the ideas released last year with a few exceptions. Key differences are noted.

NCTR and other groups have begun to meet with key congressional offices about the potential effect of the proposal on state and local government retirement plans (especially the effect of ERSAs). Concerns include:

> -Eliminating favorable treatment for governmental 403(b)s and 457s, such as exemption from the nondiscrimination rules, special catch up rules, and exemption for 457s from the 10% penalty tax; and
>
> -Blurring the well-established line between federal regulation of 403(b) and 457s and state and local government regulation of them.

The reaction we've gotten so far is mixed – from outright opposition to significant interest. General agreement exists, however, that, because of the fall election, Congress will face a compressed schedule, which could prevent it from considering even small portions of the proposal.

NCTR's Legislative Committee will be in Washington on February 9 to visit their congressional offices. They will discuss a variety of issues, including the savings proposal. NCTR and NASRA hope to have a joint statement available for committee members to distribute.

RETIREMENT SAVINGS ACCOUNTS (RSAs)

- $5,000 annual contribution limit (indexed for inflation). [*2003 proposed limit was $7,500*]
- Available to all individuals – no income limits (contributions cannot exceed compensation), no age limits.
- Contributions would be nondeductible (like Roth IRAs).
- Earnings would accumulate tax-free, and qualified distributions would be excluded from gross income.
- Qualified distributions could be made after age 58 or in the event of death or disability.
- Nonqualified distributions: Distributions in excess of prior contributions would be included in income and subject to an additional tax.

LIFETIME SAVINGS ACCOUNTS (LSAs)

- $5,000 annual contribution limit (indexed for inflation). [*2003 proposed limit was $7,500*]
- Available to all individuals – no income limits, no age limits.
- Contributions would be nondeductible (like Roth IRAs).
- Earnings would accumulate tax-free and all distributions would be excluded from gross income.
- No minimum required distribution rules would apply at any age throughout owner's life.
- Contribution limit of $5,000 applies to the individual owner of the account, not the contributor.
- Contributors could make annual contributions to the accounts of other individuals.
- Annual aggregate contributions to an individual's accounts could not exceed $5,000.

EMPLOYER RETIREMENT SAVINGS ACCOUNTS (ERSAs)

ERSAs would combine 401(k)s, 403(b)s, 457s, and several other existing retirement vehicles into a single type of plan. Any employer could offer an ERSA. The Treasury press release states that ERSAs sponsored by state and local governments "would not be subject to nondiscrimination testing under certain circumstances."