

**Summary of Provisions of Interest
to State and Local Government Retirement Systems and their Participants
in H.R. 1836,
the Economic Growth and Tax Relief Reconciliation Act of 2001**

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On June 7, 2001, President George W. Bush signed into law the Economic Growth and Tax Relief Reconciliation Act of 2001. The Act affects more rules that govern state and local government plans than any other legislative measure in recent memory. It greatly expands pension portability for teachers and other public employees, opens new opportunities for retirement saving, and modernizes the treatment of Section 457 deferred compensation plans. Once the public law number is available, we will post it on www.nctr.org.

This summary lists the provisions of interest to state and local government retirement systems and their participants. It includes the effective dates. Citations are to the text of the "conference report" to H.R. 1836." (Congress calls the final version of an Act, the "Conference Report.")

The purpose of the summary is to review the changes, but not to provide a comprehensive analysis. Readers who wish to see the underlying documents used for the summary should visit www.nctr.org for the relevant text and the accompanying explanation. Note, some of the provisions in the summary affect plans other than those of state and local governments, but no reference to them is made.

Unlike previous tax bills, the Economic Growth and Tax Relief Reconciliation Act of 2001 has a sunset. Its provisions and amendments do not apply to taxable, plan, or limitation years beginning after December 31, 2010 because of the Congressional Budget Act. Later in this decade, Congress will need to decide whether it will extend these provisions, allow them to lapse, or take some other action.**

* I appreciate the assistance of Louis T. Mazawey, Attorney at Law, the Groom Law Group, in the preparation of this summary.

** See final page for information about H.R. 1727, the Fallen Hero Survivor Benefit Fairness Act of 2001, which, although not part of the final version of H.R. 1836, relates to public employee pensions.

Issue	Summary	Effective Date												
<i>Deemed IRAs Under Employer Plans Allowed (§ 602)</i>	Allows voluntary employee contributions made to a qualified retirement plan, 403(b) arrangement, or state or local government 457 plan to be treated as a traditional IRA or Roth IRA for all purposes of Internal Revenue Code, as applicable. <i>(Note, although not directly related to state and local government plans, the Act also raises the IRA contribution limit and provides for IRA catch-up contributions.)</i>	Plan years beginning after December 31, 2002.												
<i>Defined Benefit Limits Increased; Limits for TAMRA-Election Plans Changed; \$75,000 floor at Age 55 Eliminated (§ 611(a))</i>	Increases the annual benefit limit for defined benefit plans to \$160,000, indexed as under current law. For "TAMRA participants," lowers the age at which the benefit limit is actuarially reduced from Social Security retirement age to age 62 and makes age 65 the age beginning at which the benefit limit is actuarially increased, instead of Social Security retirement age. "TAMRA participants" are those hired on or after January 1, 1990 and whose plan is subject to the TAMRA election. (See www.nctr.org for an explanation of the TAMRA election.) These ages are already applicable to non-"TAMRA participants," so the Act makes no change affecting them with respect to this provision. Eliminates the \$75,000 floor at age 55 for non-public safety workers. The floor is no longer needed because, as noted above, the Act greatly increases the defined benefit limit.	Years ending after December 31, 2001. <i>(Note, most effective dates in the Act are "years beginning after December 31, 2001," although this particular one is "years ending after December 31, 2001.")</i>												
<i>Defined Contribution Limits Increased (§ 611(b))</i>	Increases annual dollar contribution limit under 415(c) to \$40,000, indexed in \$1,000 increments.	Years beginning after December 31, 2001.												
<i>401(k), 403(b), and 457 Annual Limits Increased (§ 611(d) & (e))</i>	<p>Increases the annual elective deferral limit for 401(k), 403(b), and 457 plans.</p> <table border="0" data-bbox="562 954 1465 1149"> <tr> <td>For taxable years beginning in:</td> <td>Maximum deferral amount:</td> </tr> <tr> <td>2002</td> <td>\$11,000</td> </tr> <tr> <td>2003</td> <td>\$12,000</td> </tr> <tr> <td>2004</td> <td>\$13,000</td> </tr> <tr> <td>2005</td> <td>\$14,000</td> </tr> <tr> <td>2006 and thereafter*</td> <td>\$15,000</td> </tr> </table> <p>*For taxable years beginning after December 31, 2006, the amount is indexed as under current law (\$500 increments). The special 457 catch up is changed to twice the dollar amount of the annual elective deferral limit. The special 403(b) catch up (see § 402(g)) is retained.</p>	For taxable years beginning in:	Maximum deferral amount:	2002	\$11,000	2003	\$12,000	2004	\$13,000	2005	\$14,000	2006 and thereafter*	\$15,000	Years beginning after December 31, 2001.
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2002	\$11,000													
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2006 and thereafter*	\$15,000													
<i>Compensation Cap Increased (§ 611(c))</i>	Increases the amount of compensation that may be taken into account under qualified retirement plans to \$200,000, indexed in \$5,000 increments.	Years beginning after December 31, 2001.												
<i>457 Coordination Requirements Repealed (§ 615)</i>	Repeals coordination requirements for 457 plans, so that 457 contributions are not limited by 401(k)/403(b) contributions.	Years beginning after December 31, 2001.												

Issue	Summary	Effective Date												
<i>Optional Treatment of Elective Deferrals as Roth Contributions Allowed (§ 617)</i>	Allows 401(k) or 403(b) plans to permit a participant to elect to have all or a portion of his/her elective deferrals to be treated as "Roth Contributions." Such contributions are not excludable from gross income, but earnings generally are tax-free.	Taxable years beginning after December 31, 2005.												
<i>Tax Credit for Low- and Middle-Income Savers Created (§ 618)</i>	Provides non-refundable income tax credit for contributions made by eligible low- and middle-income taxpayers to a qualified retirement plan, 403(b) plan, governmental 457 plan, or IRA. Sunsets after five years.	Taxable years beginning after December 31, 2001, and before January 1, 2007.												
<i>Catch-Up Contributions for Individuals Age 50 or Over Created (§ 631)</i>	<p>Increases the otherwise applicable dollar limit on elective deferrals under 401(k), 403(b), and 457 plans for individuals who have attained age 50 by the end of the year. The catch-up contributions do not apply to a 457 plan for any year to which the special 457 catch-up rules apply.</p> <table border="0" data-bbox="562 565 1325 760"> <tr> <td>For taxable years beginning in:</td> <td>Applicable dollar amount:</td> </tr> <tr> <td>2002</td> <td>\$1,000</td> </tr> <tr> <td>2003</td> <td>\$2,000</td> </tr> <tr> <td>2004</td> <td>\$3,000</td> </tr> <tr> <td>2005</td> <td>\$4,000</td> </tr> <tr> <td>2006 and thereafter*</td> <td>\$5,000</td> </tr> </table> <p>*Indexed thereafter in \$500 increments</p>	For taxable years beginning in:	Applicable dollar amount:	2002	\$1,000	2003	\$2,000	2004	\$3,000	2005	\$4,000	2006 and thereafter*	\$5,000	Contributions in taxable years beginning after December 31, 2001.
For taxable years beginning in:	Applicable dollar amount:													
2002	\$1,000													
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<i>25% of Compensation Limit for Defined Contribution Plans and 33-1/3% of Compensation Limit for 457 Plans Increased to 100%; 403(b) Maximum Exclusion Allowance Eliminated (§ 632)</i>	Increases the compensation-based limits on defined contribution plans from 25% to 100% of compensation and the compensation-based limits on 457 plans from 33-1/3% to 100% of "includible compensation." Eliminates the exclusion allowance applicable to 403(b)s and substitutes the applicable 415 limit. (403(b) providers and participants, see § 632(b) of the Act for special rules.)	Years beginning after December 31, 2001.												
<i>Minimum Distribution Rules To Be Modified (§ 634)</i>	Directs the Secretary of the Treasury to modify the life expectancy tables under the regulations relating to minimum distribution requirements under sections 401(a)(9), 408(a)(6) and (b)(3), 403(b)(10), and 457(d)(2) to reflect current life expectancy.	Date of enactment.												
<i>Tax Treatment of Division of 457 Plan Benefits upon Divorce Clarified (§ 635)</i>	Applies the taxation rules for qualified plan distributions under a qualified domestic relations order (QDRO) to distributions made pursuant to a domestic relations order from a section 457 plan; makes clear that a 457 plan does not violate the restrictions on distributions from such plans due to payments to an alternate payee under a QDRO; and applies the special rule applicable to governmental plans for purposes of determining whether a distribution is pursuant to a QDRO.	Applies to transfers, distributions, and payments made after December 31, 2001.												

Issue	Summary	Effective Date
<i>Hardship Rules Changed for Certain Purposes (§ 636)</i>	Makes two changes: 1) directs the Secretary of the Treasury to revise the regulations relating to hardship distributions for 401(k)s to provide that the period an employee is prohibited from making elective and employee contributions in order for a distribution to be deemed necessary to satisfy financial need is reduced from twelve to six months; and 2) treats hardship distributions as ineligible for rollover distributions (such as a hardship distribution from a 457 plan).	Revised regulations apply to years beginning after December 31, 2001; change regarding rollover distributions effective for distributions made after December 31, 2001.
<i>Portability of Voluntary Savings Plans Expanded (§ 641)</i>	Allows portability of retirement assets between all plans when employees change jobs, including 403(b) and 457 plans. Allows amounts from 457s to be moved into IRAs (as is currently allowed for 403(b)s and certain other types of plans). Requires the 457 plan administrator to separately account for amounts rolled into such plan from other eligible retirement plans (e.g., 403(b)s, 401(k)s). If the administrator does not do so, the plan could not accept transfers or rollovers from such other plans. Treats a distribution from a state or local government 457 as a distribution from a qualified retirement plan or 403(b) plan to the extent that such distribution is attributable to an amount transferred to an eligible deferred compensation plan from such a plan. Applies the 10% early withdrawal tax to distributions attributable to amounts rolled over to a 457 plan from a qualified plan or 403(b) plan.	Distributions after December 31, 2001.
<i>Rollovers of IRAs into Workplace Retirement Plans Allowed (§ 642)</i>	Allows rollovers of IRAs into workplace retirement plans, including 403(b)s and 457s.	Distributions after December 31, 2001.
<i>Rollovers of Employee After-Tax Contributions Allowed (§ 643)</i>	Allows direct rollovers of employee after-tax contributions to a defined contribution plan if the plan agrees to separately account for amounts so transferred. Also allows such contributions to be transferred to an IRA.	Distributions after December 31, 2001.
<i>Hardship Exception of 60-Day Rule Allowed (§ 644)</i>	Allows the Secretary of the Treasury to waive the 60-day requirement for rolling over, tax free, an amount received from an IRA, 403(b) plan, or qualified plan where the failure to waive such requirement would be against equity or good conscience, including casualty, disaster, or other events beyond the reasonable control of the individual subject to such requirement.	Distributions after December 31, 2001.
<i>Definition of Events at Which Distributions Allowed Modified (§ 646)</i>	Prohibits distribution of elective deferrals at time the employee “has severance from employment,” as opposed to “separates from service,” as under previous law. Applies to 401(k)s, 403(b)s, and 457s. The effect of this change is to permit distributions when the employee terminates service with the employer (and any controlled groups) provided that no part of the benefit is being transferred to the new employer's plan.	Distributions after December 31, 2001.

Issue	Summary	Effective Date
<i>Use of 403(b)/457 Assets for Purchase of Service Credit in Governmental Defined Benefit Plans Allowed (§ 647)</i>	Permits funds from 403(b) and 457 plans to be transferred on a pre-tax basis to purchase permissive service credit, or to repay prior cash outs, in governmental defined benefit plans.	Transfers after December 31, 2001.
<i>Distribution Rules and Inclusion Requirements for 457 Plans Changed (§ 649)</i>	Makes amounts under a 457 plan of a state or local government includible in income when paid. Applies to all 457 plans the minimum distribution rules of qualified plans. Changes withholding and reporting for governmental 457s from W-2 to 1099-R.	Distributions after December 31, 2001.
<i>Automatic Rollovers of Certain Mandatory Distributions Required (§ 657)</i>	Requires a mandatory distribution to be transferred into an IRA in the following situation: 1) the amount is in excess of \$1,000 and \$5,000 or less, and 2) the distributee does not elect either to make a rollover election or receive the distribution directly. Applies to plans that provide for mandatory cash outs of benefits valued up to \$5,000. <i>(Unclear whether this provision applies to state and local government plans.)</i>	Distributions made after final regulations by the U.S. Department of Labor are prescribed. The regulations will relate to how private plans are deemed to satisfy the ERISA fiduciary requirements in connection with the IRAs required by this section. <i>(The Labor Department does not regulate state and local government plans, nonetheless, the effective date of this section is tied to the Department's issuance of the regulations. As noted earlier, it is unclear whether this provision applies to state and local government plans.)</i>

Another recently passed bill (H.R. 1727) affecting public employees is the “Fallen Hero Survivor Benefit Fairness Act of 2001,” signed into law on June 5 (Public Law 107-15). It extends the treatment of survivor annuities for public safety officers killed in the line of duty on or before December 31, 1996. The Taxpayer Relief Act of 1997 provided that a survivor annuity paid on account of the death of a public safety officer who is killed in the line of duty is excluded from income for individuals dying after December 31, 1996. Thus, survivors of officers killed in the line of duty before that time are fully taxed on their annuities. The Act excludes from income the annuities of survivors of officers who died on or before December 31, 1996, but only for amounts received in taxable years beginning after December 31, 2001. “Public safety officers” are defined to include law enforcement officers, firefighters, or members of rescue squads or ambulance crews.