HOUSE PASSES BILL TO ALLOW ROTH 457

September 24, 2010

The House accepted the Senate Amendments to HR 5297, the Small Business Lending Fund Act of 2010 on September 23, 2010.

This bill includes a provision to allow those participating in Section 457 plans to do so through a Roth retirement plan. Those who use Roth Plans do not receive a deduction from their current income for a contribution to the plan, but they do earn returns within the plan tax free and the withdrawals from the plan are tax free.

'I am just thrilled that the Roth 457 option will soon be available for state and local government employees. NAGDCA has worked extremely hard to get a Roth for its members, and to see it come to fruition is very exciting. By providing another avenue to save for retirement, I believe it will be very appealing to our younger employees and will also increase enrollment in 457 plans. NAGDCA will plan a webcast in 2011 on the Roth 457', says Gay Lynn Bath, NAGDCA President.

The Joint Committee on Taxation's description of the provision follows:

B. Promoting Retirement Preparation
1. Allow participants in government section 457 plans to treat elective deferrals as Roth contributions (sec. 2111 of the bill and sec. 402A of the Code)

Present Law Section 401(k) plans and section 403(b) plans are permitted to have qualified Roth contribution programs under which participants may elect to make non-excludable contributions to 'designated Roth accounts' and, if certain conditions are met, to exclude from gross income distributions from these accounts.
A qualified Roth contribution program is a program under which a participant may elect to make designated Roth contributions in lieu of all or a portion of the elective deferrals that he or she otherwise would be eligible to make under the applicable retirement plan. To qualify as a qualified Roth contribution program a plan must:
1) establish a separate designated Roth account for the designated Roth contributions of each participant (and for the earnings allocable to these contributions); (2) maintain separate records for each account; and (3) refrain from
allocating to the designated Roth account amounts from non-designated Roth accounts.

Generally, if an 'applicable retirement plan' includes a qualified Roth contribution program then any contribution that a participant makes under the program is treated as an 'elective deferral,' but is not excludable from gross income.144 For purposes of the qualified Roth contribution program rules, the term 'applicable retirement plan' means: (1) an employee trust described in section 401(a) which is tax-exempt under section 501(a);145 and (2) a plan under which amounts are contributed by an individual's employer for a section 403(b) annuity contract.146 An 'elective deferral' is any deferral described in: (1) section 402(g)(3)(A) (employer contributions to section 401(k) plans not includible in employee's gross income); or
(2) section 402(g)(3)(C) (employer contributions to purchase an annuity contract under a section 403(b) salary reduction agreement).

Explanation of Provision
The provision amends the definition of 'applicable retirement plan' to include eligible deferred compensation plans (as defined under section 457(b)) maintained by a State, a political

subdivision of a State, an agency or instrumentality of a State, or an agency or instrumentality of a political subdivision of a State (collectively, 'governmental 457(b) plans'). The provision also amends the definition of 'elective deferral' in section 402A to include amounts deferred under governmental 457(b) plan.

144 Sec. 402A(a)(1).
145 That is, a trust created or organized in the United States and forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of its employees or their beneficiaries.

146 That is, an annuity purchased by a section 501(c)(3) organization or a public school.

Effective Date
The provision is effective for taxable years beginning after December 31, 2010.