February 24, 2004

Bush Administration Proposals for New Retirement and Tax-Free Savings Accounts*

	Lifetime Savings Accounts (LSAs)	Retirement Savings Accounts (RSAs)	Employer Retirement Savings Accounts (ERSAs)
In General	Effective January 1, 2005, the proposal would create Lifetime Savings Accounts (LSAs), a new tax-favored individual savings account/annuity from which tax-free distributions could be made at any age and for any use. Presumably, the rules that apply to IRAs regarding who may be a trustee or custodian would continue to apply.	Effective January 1, 2005, the proposal would replace traditional IRAs and Roth IRAs with Retirement Savings Accounts (RSAs), a new tax-favored individual retirement account/annuity. Presumably, the rules that apply to IRAs regarding who may be a trustee or custodian would continue to apply.	Effective for years beginning after December 31, 2004, the proposal would consolidate various forms of employer-sponsored retirement plans by creating Employer Retirement Savings Accounts (ERSAs). ERSAs could be sponsored by any employer. In general, the current rules for 401(k) plans would apply to ERSAs, subject to the simplified nondiscrimination rules and small employer exception described below.
Effect on Existing Arrangements	• Existing Coverdell Education Savings Accounts (ESAs) and Section 529 Qualified	• Existing Roth IRAs would be renamed RSAs and become subject to the RSA rules.	• Existing 401(k) and thrift plans would become ERSAs and would be subject to the

* Released as part of 2005 budget proposals.

	Lifetime Savings Accounts (LSAs)	Retirement Savings Accounts (RSAs)	Employer Retirement Savings Accounts (ERSAs)
	Tuition Plans ("529 Plans") could be converted tax-free to an individual's LSA before 1/1/06, subject to the following limitations: (1) the individual must have been a beneficiary of the ESA or 529 Plan as of 12/31/03, (2) for ESA conversions, the amount of the conversion is limited to the 12/31/03 balance plus contributions to, and earnings on, the account in 2004, (3) for 529 Plan conversions, the amount of the conversion is limited to the sum of (a) the lesser of $50,000 or the amount in the 529 Plan as of 12/31/03, plus (b) contributions and earnings to the 529 Plan in 2004, and (4) conversion of 2004 529 Plan or ESA contributions cannot exceed $5,000 (plus earnings thereon). • Contributions could still be made to ESAs and 529 Plans, but contributions made after	• Existing traditional IRAs could be converted to RSAs (with no income limits), with the conversion amount (less basis) includible in income in the year of conversion, except that conversions before 1/1/06 could be included in income ratably over 4 years. • Existing traditional IRAs that are not converted could not accept new contributions. • New traditional IRAs could be established to receive rollovers from employer plans, but could not accept new individual contributions. • Direct rollovers from an employer plan to an RSA would be permitted, with the rollover amount (excluding basis) taken into gross income.	ERSA rules. • Existing 403(b) plans, governmental 457(b) plans, SIMPLE 401(k) plans, SIMPLE IRAs, and SARSEPs could be converted to ERSAs and become subject to the ERSA rules, or be frozen with no new contributions after 2005 (with special transition rules for collectively bargained plans and state and local government plans). • Other types of defined contribution plans that do not permit employee deferrals or employee after-tax contributions would not be affected. • Defined benefit plans and tax-exempt 457(b) plans would not be affected.

GROOM LAW GROUP
www.groom.com

	Lifetime Savings Accounts (LSAs)	Retirement Savings Accounts (RSAs)	Employer Retirement Savings Accounts (ERSAs)
	2004 could not be converted. • No impact on existing Archer Medical Savings Accounts, Health Reimbursement Accounts, or Health Savings Accounts. • 529 Plans could be offered inside an LSA.		
Limit on Annual Contributions	An annual (calendar year) limit of $5,000 (indexed for inflation) would apply with respect to all accounts in an individual's name (rather than to contributors). Contributions could be made on behalf of others (e.g., children). The parent or legal guardian would exercise control over a minor's account for the exclusive benefit of the minor.	The annual limit for each individual would be $5,000 (indexed for inflation), or compensation includible in income, if less. For married spouses filing jointly, the compensation limit will only apply if combined includible compensation is less than $10,000.	• The current elective deferral limit, as increased by EGTRRA ($14,000 for 2005, increasing to $15,000 in 2006), would apply. • Maximum total employee and employer contributions would be the lesser of $41,000 or 100 percent of compensation.
Catch-up Contributions	No	No	Yes, as phased in by EGTRRA for non-SIMPLE plans ($4,000 for 2005, increasing to $5,000 in 2006).
Applicability of Income (AGI) or Age Limits	No	No	No

GROOM
LAW GROUP
www.groom.com

	Lifetime Savings Accounts (LSAs)	Retirement Savings Accounts (RSAs)	Employer Retirement Savings Accounts (ERSAs)
Type of Contributions	After-tax. Cash contributions only. The contributions are not eligible for the saver's credit.	After-tax. Cash contributions only. The contributions are eligible for the saver's credit.	Pre-tax, after-tax, or "Roth", depending upon design of plan; effective date of "Roth" contributions moved to 2005 (from 2006 under EGTRRA).
Taxation of Distributions	• Tax-free distributions at any age, for any use. No holding period or penalty tax would apply. • Tax-free rollovers would be permitted between spouses' LSAs.	• Distributions made after age 58 or in the event of death or disability would be tax-free. • Any other distributions would be includible in income (to the extent exceeding basis, but with distributions deemed to come from basis first) and subject to an additional 10% penalty tax. • Tax-free rollovers would be permitted between spouses' RSAs. • For conversions from a traditional IRA or ERSA, a 5-year holding period applies. Distributions attributable to the conversion (other than amounts in a Roth-type ERSA account) prior to the end of the 5-year	The treatment would depend upon the plan design/type of contributions. Generally, distributions would be includible in income, except that: • Distributions of Roth contributions and non-Roth after-tax employee contributions, and • Qualified distributions of earnings on Roth contributions, would not be taxable.

	Lifetime Savings Accounts (LSAs)	Retirement Savings Accounts (RSAs)	Employer Retirement Savings Accounts (ERSAs)
		period from the year of the conversion (or, if earlier, attainment of age 58, disability, or death), would be subject to an additional 10% tax on the entire distribution. The 5-year period is determined separately for each conversion contribution. For this purpose, the following ordering rules apply: (1) regular contributions, (2) conversion contributions (on a first-in-first-out basis, and first from taxable portion), and (3) earnings.	
Application of Minimum Required Distribution Rules	As with Roth IRAs, no minimum distributions would be required during the owner's life, but minimum distribution rules would apply at death.	As with Roth IRAs, no minimum distributions would be required during the owner's life, but minimum distribution rules would apply at death.	Present law rules would apply. Therefore, Roth accounts would not be subject to minimum distribution rules during owner's life.
Nondiscrimination Rules	N/A	N/A	• A single, simplified test would replace the ADP and ACP tests: • HCE average contribution percentage could not exceed 200% of NHCE

GROOM LAW GROUP
www.groom.com

	Lifetime Savings Accounts (LSAs)	Retirement Savings Accounts (RSAs)	Employer Retirement Savings Accounts (ERSAs)
			average contribution percentage if NHCE percentage is 6% or less; • If NHCE average percentage is more than 6%, there would be no limit on the HCE average percentage. • The contribution percentage would be calculated for each employee based on the sum of all employee and employer contributions divided by the employee's compensation. • A plan with a design-based safe harbor would satisfy the requirements if all eligible NCHEs are eligible to receive 100% vested: • 3% nonelective employer contributions; • matching contributions of 50% of employee elective contributions (up to 6% of compensation); or • matching contributions that (1) do not increase as

	Lifetime Savings Accounts (LSAs)	Retirement Savings Accounts (RSAs)	Employer Retirement Savings Accounts (ERSAs)
			the rate of employee elective contributions increase, (2) are at least equal to a 50% match up to 6% of compensation, and (3) the rate of match for any HCE at any rate of elective contribution cannot be greater than that of a NHCE.
Applicability of New Nondiscrimination Test	N/A	N/A	• Plans sponsored by state and local governments would not be subject to the test. • Plans sponsored by 501(c)(3) organizations would be subject to the new test only if the plan permits after-tax or matching contributions, but such plans would be required to permit all employees of the organization to participate.
Special Rule for Small Employers	N/A	N/A	• Employers with 10 or fewer employees making at least $5,000 during the prior year can fund the ERSA with a

GROOM
LAW GROUP
www.groom.com

	Lifetime Savings Accounts (LSAs)	Retirement Savings Accounts (RSAs)	Employer Retirement Savings Accounts (ERSAs)
			custodial account (rather than a trust), provided that employer contributions satisfy the safe harbor discrimination test described above. This would provide small employers with reporting relief and ERISA fiduciary relief (similar to current rules for SIMPLE IRAs).

H:\807\01\Chart Bush Admin Proposal-2004.doc