

Internal Revenue Service

Tax Exempt and
Government Entities

Employee Plans Division

403(b) Tax-Sheltered Annuity

for

Participant



Be Aware of Common Mistakes

As a 403(b) plan participant, you need to pay attention to the operation of your 403(b) tax-sheltered annuity so that you can:

- be compliant with the law,
- maximize your retirement benefits, and
- avoid additional taxes and penalties.

403(b) Tax-Sheltered Annuity

It is important to know the tax rules applicable to a 403(b) annuity to: 1) help you comply with the tax law; and 2) help you get the maximum 403(b) benefit.

In a national sample of audited 403(b) plans, the IRS found recurring mistakes in the following areas:

Maximum Elective Deferrals. The aggregate annual elective deferral limit per individual includes contributions to your 403(b) annuities (even if held under different employers), 401(k) plans, SIMPLE IRA plans, and SARSEP plans. Amounts contributed in excess of noted limits may be subject to additional taxes and penalties that may affect both the participant and the sponsor/employer. See the chart to the right for 403(b) provisions and requirements to maximize your retirement contributions.

Catch-Up Contributions. Plans may permit one or both of the following catch-up provisions. *Note: Catch-up contributions must be applied first to the years-of-service catch-up limits (for employees with 15 years of service) before being applied to the age-50 catch-up.*

Years of service catch-up—This catch-up is available through certain employers. Refer to the chart to the right to determine if, and how much of, this catch-up is available for you. The \$15,000 overall limit may have been exhausted through general contributions made during the first 15 years of service.



— COMMON MISTAKES

Age-50 catch-up— This catch-up is available for any participant who has attained age 50 or more by December 31st. See the chart to the right for amounts. This catch-up cannot exceed your includible compensation.

Distributions and Rollovers. New laws permit you to roll over (tax free) all or any part of your otherwise taxable eligible distribution from a 403(b) annuity into another 403(b) annuity, a 457(b) plan, a traditional IRA, or other eligible retirement plan. Likewise, if permitted by the 403(b) annuity, you may roll over your otherwise taxable distributions from another retirement plan into this 403(b) annuity. Refer to the chart to the right for the specific times/occasions when annuity distributions may be available. You should check your 403(b) annuity or consult your employer for other distribution options available to you, such as early retirement.

Loan Limitations. Earlier access to your contributions may be available through loans if offered under the 403(b) annuity. See the chart to the right for conditions. If any of these provisions are not adhered to, there is a deemed distribution that is subject to federal income tax. Additional taxes may apply if these distributions occur before age 59½. Loan defaults may violate distribution requirements.

Hardship Requirements. Hardship distributions may be permitted under a 403(b) annuity. Hardships must be the result of an immediate and heavy financial need. Failure to meet these criteria can jeopardize the status of the TSA. Hardship distributions may not be rolled over into another retirement plan or IRA.

As a participant, you need to be aware of these common mistakes. Notify your sponsor/ employer to correct mistakes timely to avoid additional taxes and penalties that may affect both you and your sponsor/employer.



Tax-Sheltered Annuity

Provisions and Requirements

Plan Provisions

403(b) Requirements

Eligible Participants

common-law employees of public school systems and 501(c)(3) organizations

General Contribution Limits

- **elective deferrals**
- \$14,000 (2005); \$15,000 (2006); indexed thereafter (plus catch-ups)
- **employer and employee contributions:**
- limited to the lesser of \$42,000 (2005); \$44,000 (2006) or 100% of includible compensation (elective deferrals and nonelective contributions)

Year of Service Catch-Up Contributions

- certain employers
- employee must have 15 years of service
- limited to least of:
 - \$3,000
 - \$15,000 less previously excluded special catch-ups
 - \$5,000 multiplied by years of service minus previously excluded deferrals

Age-50 Catch-Up Contributions

additional \$4,000 (2005);
\$5,000 (2006)

Loans

- if the TSA so provides
- \$50,000 aggregate limit of all loans at any time
- payments at least quarterly
- term not to exceed 5 years (except for purchase of principal residence)
- must bear reasonable rate of interest

Timing of Distributions

- generally,
- death
 - age 59½
 - severance from employment
 - disability
 - later of age 70½ or retirement

Other Distributions

- hardship
- qualified domestic relations order

Rollovers

- to and from other retirement plans and to IRAs
- must satisfy eligible distribution requirements

Trustee-to- Trustee Transfer

- while in service, employee can purchase certain permissive service credit in government defined benefit plans
- 403(b) to another 403(b)— in-service



403(b)
Tax-Sheltered
Annuity

for Participant

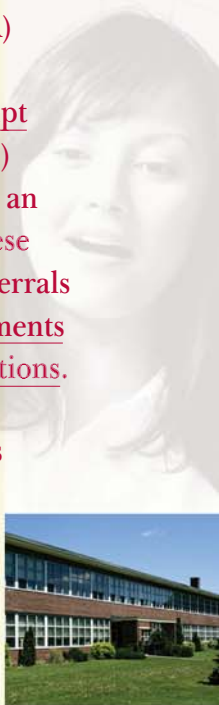
A 403(b) tax-sheltered annuity (TSA) plan is a retirement plan offered by public schools and certain tax-exempt organizations. An individual's 403(b) annuity can be obtained only under an employer's TSA plan. Generally, these annuities are funded by elective deferrals made under salary reduction agreements and non-elective employer contributions.

There are significant tax advantages for you, as a participant, in a 403(b) tax-sheltered annuity:

- your contributions to a 403(b) annuity are tax deferred,
- earnings on your retirement money are tax deferred, and
- you can carry your annuity with you when you change employers or retire.

Read on to learn about specific 403(b) topics where mistakes are common, and learn about Internal Revenue Service (IRS) products, services, and assistance to help you keep your 403(b) tax-sheltered annuity healthy.

Note: Underlined topics identify electronic links for detailed information on that topic. For those reading a print version of this product, you can access an electronic version on-line at www.irs.gov/ep to link to your topic of interest.



Customer Assistance

The following publications cover 403(b) tax-sheltered annuities and correction programs:

- Publication 571, *Tax-Sheltered Annuity Plans (403(b) Plans) for Employees of Public Schools and Certain Tax-Exempt Organizations*
- Publication 575, *Pension and Annuity Income*
- Publication 590, *Individual Retirement Arrangements (IRAs)*
- Publication 4050, *Retirement Plan Correction Programs* CD-ROM
- Publication 4224, *Retirement Plan Correction Programs* pamphlet

Download these publications at www.irs.gov/ep, or order a free copy through the IRS by dialing (800) 829-3676.

For assistance or information on retirement plan tax-related issues:

www.irs.gov/ep

See PLAN PARTICIPANT/EMPLOYEE

(877) 829-5500

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IRS

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