

Economic Growth and Tax Relief Reconciliation Act of 2001

On June 7, 2001, President Bush signed into law the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"). In addition to cutting federal income taxes, and reducing and then repealing the federal estate tax, EGTRRA also includes several provisions that affect qualified retirement plans.

The retirement plan changes are generally effective for plan years beginning after December 31, 2001. Some provisions, however, have delayed effective dates, and other provisions will be phased in over the next several years. In addition, all the provisions in EGTRRA will expire for taxable years, limitation years and plan years beginning after December 31, 2010. If Congress does not act to extend the EGTRRA provisions, the law will revert back to what it is currently.

Attached for your convenience is a chart summarizing the major provisions of EGTRRA that affect qualified retirement plans. Several of these provisions present important planning opportunities for sponsors of qualified retirement plans. We will be happy to discuss any of these planning opportunities with you.

Finally, as a reminder, qualified retirement plans must be updated for GUST changes and submitted to the IRS for review by the last day of the 2001 plan year (December 31, 2001 for calendar year plans) or, if you are using a prototype or volume submitter plan, one year after that plan is approved by the IRS. The IRS has stated that it does not intend to extend this deadline. We will be happy to assist you in updating your qualified retirement plans if you have not done so already.

* * * * *

If you have any questions concerning EGTRRA or need assistance with any GUST restatements, please feel free to call one of the following members of our Employee Benefits Practice Group:

WINSTON-SALEM OFFICE

Michael D. Gunter (336) 721-3607
331-4931
Patrick M. Allen (336) 721-3574
4993
William R. Whitehurst (336) 721-3653
331-4933
Janice C. Baldwin (336) 721-3654

CHARLOTTE OFFICE

James E. Daniel (704)
Donna W. Edwards (704) 331-
Keith D. Butcher (704)

WASHINGTON, DC OFFICE

Diane J. Fuchs (202) 857-4457
Gina M. Boscarino (202) 857-4418

RETIREMENT PLAN PROVISIONS OF H. R. 1836

**(THE ECONOMIC GROWTH AND TAX RELIEF RECONCILIATION ACT
OF 2001)**

Provisions	Current Law	H.R. 1836 (EGTRRA)												
1. Maximum Salary Reduction Contribution (Section 402(g))	Section 402(g) limits elective deferrals under most salary reduction plans (<i>e.g.</i> , Section 401(k) plans and Section 403(b) arrangements) to \$10,500 (in 2001).	<p>The limit on elective deferrals will be increased as follows:</p> <table border="1"> <thead> <tr> <th><u>Year</u></th> <th><u>Limit</u></th> </tr> </thead> <tbody> <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</td> <td>\$15,000 (indexed in \$500 increments)</td> </tr> </tbody> </table>	<u>Year</u>	<u>Limit</u>	2002	\$11,000	2003	\$12,000	2004	\$13,000	2005	\$14,000	2006	\$15,000 (indexed in \$500 increments)
<u>Year</u>	<u>Limit</u>													
2002	\$11,000													
2003	\$12,000													
2004	\$13,000													
2005	\$14,000													
2006	\$15,000 (indexed in \$500 increments)													
2. Defined Contribution Plan Limit (Section 415(c))	Section 415(c) currently limits maximum annual additions to defined contribution plans on behalf of an individual to the lesser of 25% of compensation or \$35,000. The \$35,000 limit is indexed for inflation in \$5,000 increments.	<p>The \$35,000 dollar limit will be increased to \$40,000 beginning in 2002. Future indexing of this limit will be in \$1,000 increments.</p> <p>Beginning in 2002, the 25% of compensation limit will be increased to 100%.</p>												
3. Compensation Taken Into Account (Section 401(a)(17))	Under Section 401(a)(17), compensation that may be taken into account in determining benefits under qualified plans is limited to \$170,000 (in 2001), indexed in \$10,000 increments.	The Section 401(a)(17) compensation limit will be increased to \$200,000 beginning in 2002 (with future indexing in \$5,000 increments).												
4. Defined Benefit Plan Limit (Section 415(b))	Maximum annual benefits under a defined benefit plan are limited by	Effective for years ending after December 31, 2001, the \$140,000 dollar limit in Section 415(b) will be increased to \$160,000. Indexing will continue as under current law (in \$5,000 increments).												

Provisions	Current Law	H.R. 1836 (EGTRRA)																								
	<p>Section 415(b) to the lesser of 100% of 3-year-high-average pay or \$140,000 (in 2001).</p> <p>Actuarial reduction of the limit is required if benefits start prior to Social Security normal retirement age.</p>	<p>under current law (in \$5,000 increments).</p> <p>Actuarial reduction of the Section 415(b) dollar limit will be required only for benefit commencement prior to age 62.</p>																								
<p>5. Additional Salary Reduction Catch-up Contributions</p>	<p>The Code imposes annual limits on the maximum amount that can be contributed by an employee to a Section 401(k) plan, a Section 403(b) arrangement, a SIMPLE plan, and certain other salary reduction arrangements. With certain limited exceptions, once an individual has missed the opportunity to make a contribution for a given year, the individual has no opportunity to "catch-up" in later years.</p>	<p>Individuals age 50 or older will be allowed to make annual catch-up contributions to salary reduction arrangements in the following amounts:</p> <table border="1" data-bbox="721 825 1440 1360"> <thead> <tr> <th data-bbox="721 825 829 863"></th> <th data-bbox="829 825 1036 863"><u>Year</u></th> <th data-bbox="1036 825 1268 863"><u>401(k)/403(b)</u></th> <th data-bbox="1268 825 1440 863"><u>SIMPLE</u></th> </tr> </thead> <tbody> <tr> <td data-bbox="721 863 829 989">0</td> <td data-bbox="829 863 1036 989">2002</td> <td data-bbox="1036 863 1268 989">\$1,000</td> <td data-bbox="1268 863 1440 989">\$ 50</td> </tr> <tr> <td data-bbox="721 989 829 1115">0</td> <td data-bbox="829 989 1036 1115">2003</td> <td data-bbox="1036 989 1268 1115">\$2,000</td> <td data-bbox="1268 989 1440 1115">\$1,00</td> </tr> <tr> <td data-bbox="721 1115 829 1241">0</td> <td data-bbox="829 1115 1036 1241">2004</td> <td data-bbox="1036 1115 1268 1241">\$3,000</td> <td data-bbox="1268 1115 1440 1241">\$1,50</td> </tr> <tr> <td data-bbox="721 1241 829 1367">0</td> <td data-bbox="829 1241 1036 1367">2005</td> <td data-bbox="1036 1241 1268 1367">\$4,000</td> <td data-bbox="1268 1241 1440 1367">\$2,00</td> </tr> <tr> <td data-bbox="721 1367 829 1493">0</td> <td data-bbox="829 1367 1036 1493">2006</td> <td data-bbox="1036 1367 1268 1493">\$5,000</td> <td data-bbox="1268 1367 1440 1493">\$2,50</td> </tr> </tbody> </table> <p>Amounts are indexed for inflation beginning in 2007 (in \$500 increments). Such catch-up contributions will not be subject to any other contribution limits and will not be subject to any nondiscrimination rules, except that plans will have to allow all eligible individuals to participate in the catch-up in the same manner.</p>		<u>Year</u>	<u>401(k)/403(b)</u>	<u>SIMPLE</u>	0	2002	\$1,000	\$ 50	0	2003	\$2,000	\$1,00	0	2004	\$3,000	\$1,50	0	2005	\$4,000	\$2,00	0	2006	\$5,000	\$2,50
	<u>Year</u>	<u>401(k)/403(b)</u>	<u>SIMPLE</u>																							
0	2002	\$1,000	\$ 50																							
0	2003	\$2,000	\$1,00																							
0	2004	\$3,000	\$1,50																							
0	2005	\$4,000	\$2,00																							
0	2006	\$5,000	\$2,50																							
<p>6. Faster Vesting of Employer Matching Contributions</p>	<p>Employer contributions to most retirement plans either must be fully vested after the employee has</p>	<p>Beginning in 2002, employer matching contributions will be required either to be fully vested after an employee has completed 3 years of service or to become vested in increments of 20% for each year beginning with the employee's second year of service, with full vesting after the employee has</p>																								

Provisions	Current Law	H.R. 1836 (EGTRRA)
	completed 5 years of service, or must become vested in increments of 20% for each year beginning with the employee's third year of service, with full vesting after the employee has completed 7 years of service.	completed 6 years of service.
7. Deduction Limit for Stock Bonus and Profit Sharing Plans	An employer's deduction for contributions to a profit-sharing or stock bonus plan is generally limited to 15% of the taxable compensation of the plan's participants. The limit on deductions to other types of plans is generally 25%.	Beginning in 2002, the annual limitation on the amount of deductible contributions to a profit-sharing or stock bonus plan will be increased from 15% to 25% of the compensation of the employees covered by the plan for the year.
8. Exclusion of Elective Deferrals from Deduction Limit	Elective deferrals are considered employer contributions for purposes of the Section 404 deduction limits.	Beginning in 2002, elective deferrals will no longer be considered employer contributions for purposes of the Section 404 deduction limits.
9. Definition of Compensation for Deduction Limits	For purposes of the Section 404 deduction limits, compensation does not include elective deferrals.	Beginning in 2002, for purposes of the Section 404 deduction limits, the definition of compensation will include elective deferrals.
10. Participant Loans for Small Business Owners	Generally, plans may make loans to participants. But, prohibited transaction rules prevent sole proprietors, partners, and Subchapter S corporation shareholders from taking participant loans.	The prohibited transaction rules are modified to allow for participant loans to sole proprietors, partners, and subchapter S corporation shareholders. The provision also applies prospectively to preexisting loans.

Provisions	Current Law	H.R. 1836 (EGTRRA)
11. Small Business Tax Credit for Administrative Expenses in Connection with new Retirement Plans	An employer's costs related to the establishment and maintenance of a retirement plan generally are deductible as business expenses. However, there is no tax credit for such expenses.	Certain small employers will be able to claim a non-refundable tax credit in connection with new retirement plans. The credit will apply to 50% of the first \$1,000 in administrative and retirement education expenses ("start-up expenses") for 3 years after establishing a new retirement plan and will be available to employers with 100 or fewer employees. No deduction will be allowed for the amount claimed as a credit. The credit will be available beginning for new plans established after December 31, 2001. There must be at least one nonhighly compensated participant.
12. Elimination of IRS User Fee for Determination Letters	Plan sponsors must pay a user's fee to the IRS in order to obtain a favorable determination letter.	The IRS user's fee for a favorable determination letter will be waived with respect to any retirement plan maintained by an employer with 100 or fewer employees. The waiver applies only for requests made during the first 5 plan years (or the end of the plan's remedial amendment period, if longer).
13. Rollovers of After-Tax Contributions	Employees are allowed to make after-tax contributions to 401(k) and other plans. They are not permitted to roll over distributions of those after-tax contributions into an IRA or another qualified retirement plan.	Beginning in 2002, after-tax employee contributions may be rolled over to other qualified retirement plans and IRAs.
14. Rollovers From Contributory IRAs To Qualified Plans	Rollovers of amounts originally contributed directly into an IRA ("contributory IRAs") into any type of employment-based plan generally are not allowed.	Beginning in 2002, contributory IRA amounts may be rolled over to a Section 401(a) plan, a Section 403(b) arrangement, a Section 457(b) plan maintained by a state or local government, or another IRA.
15. Employers May Disregard Rollovers for Purposes of Cash-Out Amounts	Terminated participants' benefits may be cashed out if the nonforfeitable present value of such benefits does not exceed \$5,000.	A plan is permitted to ignore amounts attributable to rollover contributions when determining the cash-out amount.
16. Repeal of "Same Desk Rule"	In some cases, 401(k) plan distributions are limited to separation	Beginning with respect to distributions made after December 31, 2001, the "same desk rule" will be eliminated by replacing "separation from service" in Section 401(k)(2)(B) with "severance from

Provisions	Current Law	H.R. 1836 (EGTRRA)
	<p>from service with the employer. The term "separation from service" has been interpreted to not include a situation where the employee performs the same functions for a successor employer (the "same desk" rule). The same desk rule also applies to Section 403(b) arrangements and Section 457(b) plans.</p>	<p>employment." Conforming changes will be made for Section 403(b) arrangements and Section 457(b) plans.</p>
<p>17. Repeal of Full Funding Limit</p>	<p>Contributions to a defined benefit plan are not deductible to the extent that plan assets exceed the lesser of (1) 160% (in 2001) of the plan's current liability, or (2) a limitation based on a reasonable projection of benefits. The 160% figure is scheduled to be phased up to 170% by the year 2005.</p>	<p>The full funding limit will be 165% of current liability for plan years beginning in 2002, 170% in 2003, and repealed in 2004 and thereafter.</p>
<p>18 Additional Disclosure Re: Significant Reduction in Benefit Accruals (Including Cash Balance Plan Conversions)</p>	<p>Under ERISA Section 204(h), a defined benefit plan or a money purchase pension plan may not be amended in a manner that results in a significant reduction in the rate of future benefit accrual unless, after the adoption of the plan amendment (and not less than 15 days before the effective date of the</p>	<p>A defined benefit plan or money purchase pension plan will be required to provide participants with a written notice concerning a plan amendment that provides for a significant reduction in future benefit accruals under the plan (including any elimination or reduction of an early retirement benefit). The Secretary of the Treasury could exempt or provide a simplified form of notice for a plan which has fewer than 100 participants who have accrued a benefit under the plan or which offers participants the option to choose between the new benefit formula and the old benefit formula.</p> <p>The notice will be required to describe the benefit</p>

Provisions	Current Law	H.R. 1836 (EGTRRA)
	<p>plan amendment), the plan administrator provides a written notice to affected participants and alternate payees. The notice must either (1) specify the plan amendment and its effective date, or (2) contain a summary of the amendment and effective date, written in a manner calculated to be understood by the average plan participant and containing the effective date.</p>	<p>reduction caused by the plan amendment in a manner calculated to be understood by the average plan participant, and generally would have to be provided within a reasonable time period prior to the effective date of the plan amendment.</p> <p>The penalty for failure to comply with the notice requirements will equal \$100 per day per omitted party with a maximum penalty of \$500,000 in any year (except in cases of willful neglect). The Secretary of the Treasury could waive this penalty if reasonable cause for failure is shown.</p> <p>Failure to comply with the notice requirement will subject the employer to an excise tax equal to \$100 per day per failure, up to \$500,000.</p>
<p>19. ESOP Dividends May Be Reinvested Without Loss of Dividend Deductions</p>	<p>Dividend deductions are allowed under Section 404(k) on dividends paid on employer stock to an unleveraged ESOP only if the dividends are paid to employees in cash; the deduction is denied if the dividends remain in the ESOP for reinvestment.</p>	<p>Beginning in 2002, an employer will be allowed to deduct dividends paid to an ESOP when its employees are allowed to elect to take the dividends in cash or leave them in the plan for reinvestment in employer stock.</p>
<p>20. Prohibited Allocations of Stock in an S Corporation ESOP</p>	<p>ESOPs may purchase S corporation stock. The ESOP is not subject to tax on distributable income from such S corporation stock. Income tax is deferred on the sale of certain employer securities to an ESOP. A 50 percent excise tax is imposed on certain</p>	<p>If there is a nonallocation year with respect to an S corporation ESOP:</p> <ul style="list-style-type: none"> • The value of the prohibited allocation is taxable to the person receiving such allocation; • The 50 percent excise tax will be imposed on the S corporation; and • An excise tax will be imposed on the S corporation with respect to any synthetic equity owned by a disqualified person. <p>These provisions are intended to ensure that S corporation ESOPs provide broad based employee coverage.</p>

Provisions	Current Law	H.R. 1836 (EGTRRA)								
	prohibited allocations of securities acquired in such a transaction.									
21. Automatic Rollovers of Certain Mandatory Distributions	A plan may provide for the automatic distribution ("cash-out") of certain vested accrued benefits that do not exceed \$5,000. The plan is not required to roll over such amounts to another retirement savings vehicle.	A plan that provides mandatory "cash-outs" of vested accrued benefits will be required to directly transfer such distributions to an IRA ("default IRA") or other qualified retirement vehicle unless the participant affirmatively elects to receive the distribution directly. The proposal would not apply to distributions of \$1,000 or less. Limited fiduciary relief will be provided to plan fiduciaries with respect to the selection of the default IRA. The Department of Labor (DOL) is directed to issue safe harbors with respect to the designation of an institution and investment of funds. The provision is not effective until final DOL regulations are published, and such regulations must be finalized not later than 3 years after the date of enactment.								
22. Modification of Timing of Plan Valuations	The valuation date for a defined benefit plan for a plan year must generally be in the same plan year.	Defined benefit plans will be permitted to use a valuation date up to one year prior to the beginning of the plan year. The change will apply at the election of the employer but will not be available to an underfunded plan.								
23. Repeal of the Multiple Use Test	In addition to two nondiscrimination tests (the ADP and ACP tests), some 401(k) plans must also satisfy the complicated multiple use test.	The multiple use test is repealed.								
24. IRA Contribution Limits	The maximum annual contribution permitted to IRAs (traditional or Roth) is generally the lesser of \$2,000 or 100% of the individual's compensation.	<p>The IRA contribution limit will be increased as follows:</p> <table border="1" data-bbox="721 1402 1446 1665"> <thead> <tr> <th data-bbox="721 1402 1166 1444"><u>Year</u></th> <th data-bbox="1166 1402 1446 1444"><u>Limit</u></th> </tr> </thead> <tbody> <tr> <td data-bbox="721 1444 1166 1528">2002-2004</td> <td data-bbox="1166 1444 1446 1528">\$3,000</td> </tr> <tr> <td data-bbox="721 1528 1166 1612">2005-2007</td> <td data-bbox="1166 1528 1446 1612">\$4,000</td> </tr> <tr> <td data-bbox="721 1612 1166 1665">2008</td> <td data-bbox="1166 1612 1446 1665">\$5,000</td> </tr> </tbody> </table> <p>Thereafter, the limit will be indexed for inflation annually (in \$500 increments).</p>	<u>Year</u>	<u>Limit</u>	2002-2004	\$3,000	2005-2007	\$4,000	2008	\$5,000
<u>Year</u>	<u>Limit</u>									
2002-2004	\$3,000									
2005-2007	\$4,000									
2008	\$5,000									
25. Catch-Up Contributions	Once an individual has missed the opportunity to make an IRA contribution	Individuals age 50 and over will be permitted to make catch-up contributions to IRAs as follows:								

Provisions	Current Law	H.R. 1836 (EGTRRA)	
	for a given year, the individual has no opportunity to "catch-up" in later years.	<u>Year</u>	<u>Limit</u>
		2002-2005	\$ 500
		2006+	\$1,000
26. SIMPLE Plan Contribution Limit (Section 408(p))	Maximum elective deferrals to SIMPLE retirement plans are limited to \$6,500 per year (in 2001), indexed for inflation in \$500 increments.	The limit on elective deferrals to SIMPLE plans will be increased as follows:	
		<u>Year</u>	<u>Limit</u>
		2002	\$7,000
		2003	\$8,000
		2004	\$9,000
		2005	\$10,000
27. Rollovers Among Various Types of Employment-Based Retirement Plans	Amounts in a Section 401(a) plan or Section 403(b) arrangement generally may only be rolled over to the same type of plan or arrangement or to an IRA. Amounts in Section 457(b) plans may only be transferred from one Section 457(b) plan to another Section 457(b) plan.	Beginning in 2002, amounts in Section 401(a) plans or Section 403(b) arrangements, or Section 457(b) plans maintained by a state or local government generally may be rolled over to another Section 401 plan, a Section 403(b) arrangement, a Section 457(b) plan maintained by a state or local government, or an IRA.	
28. Sunset	EGTRRA creates a supermajority point of order against provisions in a budget reconciliation bill that lose revenue after the initial 10-year period.	The provisions of EGTRRA will not apply to taxable, plan or limitation years beginning after December 31, 2010, unless extended by Congress.	