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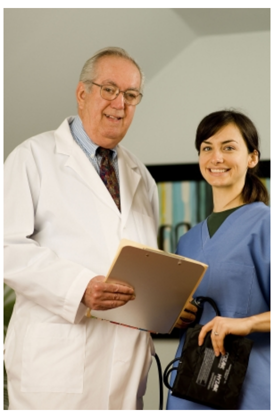
BUILDING AND SAFEGUARDING YOUR FINANCIAL WORLD

403(b) Plans



Depending on your income, you may be eligible for an income tax credit of up to $1,000 for amounts contributed to a 403(b) plan.

A 403(b) plan is an employer-sponsored retirement plan for certain employees of public schools, tax-exempt [501(c)(3)] organizations, and churches. The employer can purchase annuity contracts for eligible employees, or establish custodial accounts to be invested in mutual funds or other investments. In the case of annuity contracts, a 403(b) plan is sometimes referred to as a tax-sheltered annuity (TSA) plan. (Church plans are subject to several special rules not covered here.)

How does a 403(b) plan work?

Depending on the specific type of 403(b) plan, contributions may be made by the employee, the employer, or both. Many 403(b) plans are similar to 401(k) plans: you elect either to receive cash payments (wages) from your employer immediately, or to defer receipt of all or part of that income to your 403(b) account. The amount you defer (called an "elective deferral") can be either pre-tax or, if your plan permits, after-tax Roth contributions.

Employer contributions, if made, may be a fixed percentage of your compensation, or may match a specified percentage of your contribution, or may be discretionary on the part of the employer. One unique characteristic of 403(b) plans is that your employer is allowed to make contributions to your account for up to five years after you terminate employment.

Who can participate?

In general, if any employee is eligible to make elective deferrals, then all employees must be allowed to do so. This is called the "universal availability rule." However, your employer can exclude certain groups of employees from participation [for example, employees who normally work less than 20 hours per week, or who are eligible under another deferral plan — for example, a 401(k) plan — of the employer]. Your employer may also require that you attain age 21 and/or complete up to two years of service before you're eligible for employer contributions.

Some 403(b) plans provide for automatic enrollment once you've satisfied the plan's eligibility requirements. For example, the plan might provide that you'll be automatically enrolled at a 3% pre-tax contribution rate (or some other percentage) unless you elect a different deferral percentage, or choose not to participate at all. If you've been automatically enrolled in your 403(b) plan, make sure that the contribution rate and investments in your portfolio are appropriate for your circumstances.

What are the contribution limits?

You can defer up to $19,500 of your pay to a 403(b) plan in 2021 (unchanged from 2020). If your plan allows Roth contributions, you can split your contribution between pre-tax and Roth contributions any way you wish. Unlike 401(k) plans, employee elective deferrals to 403(b) plans aren't subject to discrimination testing [which in 401(k) plans can often significantly limit the amount higher-paid employees can defer].

If your plan permits, you may also be able to make "catch-up" contributions to your account. You can contribute up to an additional $6,500 in 2021 (unchanged from 2020) if you'll be age 50 or older by the end of the year. If you have 15 years of service with your employer (even if you haven't attained age 50) a special Section 403(b) rule may also allow you to make annual catch-up contributions of $3,000, up to $15,000 lifetime. If you're eligible for both rules, then any catch-up contributions you make count first against your 15-year $15,000 lifetime limit.

If you also contribute to a 401(k), 403(b), SIMPLE, or SARSEP plan maintained by the same or a different employer, then your total elective deferrals to all of these plans — both pre-tax and Roth — can't exceed $19,500 in 2021, plus catch-up contributions (unchanged from 2020). It's up to you to make sure you don't exceed the limits if you contribute to plans of more than one employer. Total contributions to your 403(b) account — both yours and your employer's — can't exceed $58,000 in 2021 (or 100% of your compensation, if less). Age 50 catch-up contributions

While your pre-tax elective deferrals aren't subject to income tax when made, they are subject to FICA tax. Your Social Security benefits are not affected by your decision to make pre-tax contributions to your account.

[1] If you have both a traditional IRA and a Roth IRA, your combined contributions to both cannot exceed $6,000 ($7,000 if age 50 or older) in 2021.

[2] When considering a rollover, to either an IRA or to another employer's retirement plan, you should consider carefully the investment options, fees and expenses, services, ability to make penalty-free withdrawals, degree of creditor protection, and distribution requirements associated with each option. A cash distribution will be subject to regular income taxes and, if taken prior to reaching age 59½, a 10% penalty, unless an exception applies.

[3] If you reach age 72 before July 1, 2021, you will need to take an RMD by December 31, 2021.

are not included in this limit, but special Section 403(b) catch-up contributions are. (Aggregation rules may apply if you also participate in a qualified retirement plan.)

Can I also contribute to an IRA?

Your participation in a 403(b) plan has no impact on your ability to contribute to an IRA. You can contribute up to $6,000 to an IRA in 2021 (unchanged from 2020), $7,000 if you'll be age 50 or older by the end of the year (or, if less, 100% of your taxable compensation). However, depending on your income level, your ability to make deductible contributions to a traditional IRA may be limited if you contribute to a 403(b) plan. (Your income and filing status may also impact your ability to contribute to a Roth IRA.)[1]

Income tax considerations

When you make pre-tax 403(b) contributions, you don't pay current income taxes on those dollars (which means more take-home pay compared to an after-tax contribution of the same amount). But your contributions and investment earnings are fully taxable when you receive a distribution from the plan.

In contrast, your after-tax Roth 403(b) contributions are subject to income taxes up front, but are tax free when distributed to you from the plan. And, if your distribution is qualified, then any earnings are also tax free.

In general, a distribution from your Roth 403(b) account is qualified only if it's made after the end of a five-year waiting period, and the payment is made after you turn 59½, become disabled, or die.

If your distribution is nonqualified, then you're deemed to receive a pro-rata portion of your tax-free Roth contributions and your taxable earnings.

Your employer's contributions are always made on a pre-tax basis, even if they match your Roth contributions. That is, your employer's contributions, and any investment earnings on those contributions, are always taxable to you when you receive a distribution from the plan.

If you receive a payment from your 403(b) account before you turn 59½ (55 in certain cases), the taxable portion may also be subject to a 10% early distribution penalty, unless an exception applies.

When can I access my money?

In general, you can't withdraw your elective deferrals from your 403(b) until you reach age 59½, become disabled, or terminate employment (deferrals to annuity contracts prior to 1989 aren't subject to these restrictions). Some plans allow you to make a withdrawal if you have an immediate and heavy financial need ("hardship"), but this should be a last resort. You withdrawal will be subject to regular income taxes and a possible 10% penalty tax. If your plan allows after-tax (non-Roth) contributions, your plan can let you withdraw these dollars at any time.

Employer contributions to 403(b) custodial accounts are subject to similar withdrawal restrictions. But employer contributions and pre-1989 deferrals to 403(b) annuity contracts are subject to somewhat more lenient distribution rules. Check with your plan administrator for your plan's specific rules.

If your plan permits loans, you may be able to borrow up to one-half of your vested 403(b) account balance (to a maximum of $50,000) if you need the money.

What happens when I terminate employment?

Generally, you forfeit all employer contributions that haven't vested. "Vesting" means that you own the contributions. Your plan may require up to six years of service before you're fully vested in employer contributions, although some plans have much faster vesting schedules. (Your own contributions are always 100% vested.) You can generally leave your money in your 403(b) account, transfer it to a new 403(b) account, roll your dollars over to an IRA or to another employer's retirement plan, or take a cash distribution.[2]

What else do I need to know?

- You must begin taking distributions ("required minimum distributions," or RMDs) from your 403(b) account after you reach age 72 (or after you terminate employment, if later). (The RMD rules don't apply to contributions made prior to 1987.)[3]
- If your employer offers 403(b)s from various vendors, you may be able to transfer your assets from one contract to another while you're still employed. This can be helpful if you're dissatisfied with a particular vendor's investment offerings.
- Your 403(b) account is fully protected from creditors under federal law in the event of your bankruptcy. If your plan is covered by ERISA, then your account is generally protected from all of your creditors' claims.