

Read Between the Numbers: 403(b)s & 457s

Need a quick cure for insomnia? Get a glass of warm milk, find a comfy chair, and curl up with a copy of the *IRS Code*. This 2,000-page tome, loaded with the kinds of facts, figures and prose only Tolstoy's accountant could love, will have you on the edge of your sleep in no time.

Even so, the U.S. tax code is where you'll find a pair of provisions that could really perk up your retirement savings. They're known (affectionately, we presume) as Sections 403(b) and 457, and they're the rules governing the predominant types of supplemental retirement savings plans offered to K-12 employees across the country. (Some educators can opt instead for 401(k)s — the tax-deferred retirement plans common to corporate America — which are similar in most ways to 403(b)s. Public schools with 401(k)s were grandfathered under the 1986 Tax Reform Act.) Indeed,



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thanks to rules incorporated into 2001's federal Economic Growth and Tax Relief and Reconciliation Act (EGTRRA), educators can now give their corporate cousins a run for their retirement money.

First, some history. When Congress established the 403(b) in 1958, plan investments were limited to annuities offered by insurance companies — one reason some people mistakenly continue to call any such plan a TSA,

or tax-sheltered annuity. But today's 403(b)s can expose you to a wide range of mutual funds as well as annuities.

For its part, the 457 plan came around in 1979. What's more, there are actually three kinds of 457s (fans of the old *Newhart* show brothers Larry, Darryl and Darryl will appreciate this): 457(b), available to employees of state and local governments, including public school districts (we'll call these "public 457" plans); the *other* 457(b), available to upper management and highly paid, so-called "top hat" employees of 501(c) tax-exempt organizations*; and 457(f), aka "ineligible" plans, which can be available to all employees (public plans) or just the high earners who can be, well, fitted for those "top hats" (private

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plans). What's more, that second 457(b), along with the 457(f), is subject to "constructive receipt": federal income tax is levied on the amount deferred when it is "made available" to an employee — whether the employee receives the money or not. Got all that? (Don't worry, there won't be a quiz later.)

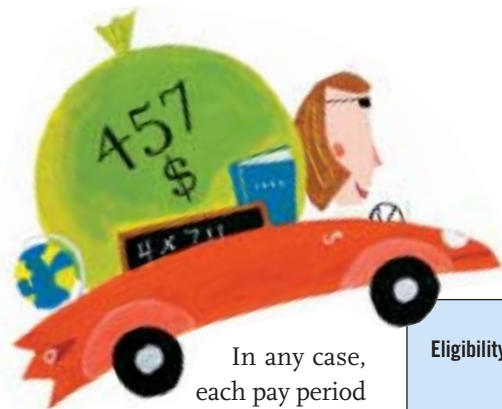
occur. What's more, if your district offers a 403(b) (or a 401(k)) *and* a 457, you now can contribute to both plans in the same year. So instead of \$12,000 — 2003's annual contribution limit for each account — this year you can sock away up to \$24,000 in pretax dollars toward retirement. Finally, EGTRRA expanded the "catch-up" provisions that allow older workers to contribute even more. Employees age 50 or older may contribute an extra \$2,000 to each account this year (the limit rises to \$5,000 by 2006), and they, or workers nearing their plan's stated retirement

age, may be able to catch up further.

True, President Bush's recent proposal to transform America's retirement savings plans would crack EGTRRA's flexibility and related rules — and, indeed, turn 403(b)s, 457s and even 401(k)s into one great big tax-favored omelette. But until that call becomes law — far from a sure thing — 403(b)s and 457s remain remarkable vehicles for fattening your nest egg.

Below is a quick comparison of 403(b) and public 457(b) plans.™

** If the tax-exempt group is church-related, all employees are eligible.*





In any case, each pay period you automatically set aside pretax dollars in funds or annuities you choose, then watch as your investment (hopefully) grows tax deferred until you take distributions later on. Many employers will even match some of your contributions — a gift you should take advantage of even if you don't participate otherwise.

Moreover, the 2001 tax law made 403(b)s and, in particular, 457s, even more attractive. For one thing, EGTRRA enhanced plan portability, enabling you to roll over 403(b) or public 457 dollars into IRAs, 401(k)s or other 403(b)s or 457s if you leave your job, or if other "qualifying events"

403(b)

457(b) (public)

	403(b)	457(b) (public)
Eligibility	Employees of public schools or nonprofit or tax-exempt organizations under IRS section 501(c)(3)	Employees of state and local governments, including school districts
Contribution limit (2003)	\$12,000 by employee (total employee and employer contribution can be lesser of 100% of taxable compensation or \$40,000)	Lesser of \$12,000 or 100% of compensation 
Loans available	Yes (subject to plan rules)	Yes (subject to plan rules)
Catch-up provisions (2003)	Age 50+, an additional \$2,000 (\$14,000 max)  -and- With 15 years' service, up to \$3,000/year (\$15,000 max lifetime)	Age 50+, an additional \$2,000 (\$14,000 max) -or- Within 3 years of plan's retirement age, up to twice annual contribution limit (could vary based on your circumstances)
Rollovers allowed	Yes	Yes
Distributions	Must meet qualifying event: ▶ Separation from service ▶ Age 59 ½ ▶ Financial hardship (e.g., tuition payment, home purchase)	Must meet qualifying event: ▶ Separation from service ▶ Age 70 ½ ▶ Unforeseeable emergency (e.g., unexpected illness)
IRS early-withdrawal penalty	10% before age 59 ½	None (457 plan money only)