Designated Roth Accounts

"Is it better for you to pay the tax on your retirement now, while you're working, or later during retirement?"

A designated Roth account is a separate account under a 403(b) plan.

- An advantage of a designated Roth account is that you pay tax on your contributions now, but later, when you receive a qualified distribution from the account, it is tax-free. Less tax on your plan distributions could mean more money in your pocket during your retirement.
- Designated Roth contributions are elective contributions that, unlike pre-tax elective contributions, are currently includible in your taxable gross income — you pay tax on these contributions now. The Plan was recently amended to specifically permit these contributions.
- Qualified distributions from a designated Roth account, including all earnings, are tax-free. Distributions from a designated Roth account must begin when you turn age 70½, unless you are still working for the Commonwealth.

Which types of retirement accounts are right for you?

PLAN FEATURE	PRE-TAX ELECTIVE CONTRIBUTION ACCOUNT	DESIGNATED ROTH ACCOUNT
Contributions	Pre-tax employee elective contributions are made with pre-tax dollars.	Designated Roth employee elective contributions are made with after-tax dollars.
Income Limits	No income limitation to participate.	No income limitation to participate.
Maximum Elective Contributions	Combined[2] employee elective contributions limited to: $18,500 ($24,500 for individuals 50 or over).	Combined[2] employee elective contributions limited to: $18,500 ($24,500 for individuals 50 or over).
Taxation of Withdrawals	Withdrawals of contributions and earnings are subject to federal and most state income taxes.	A withdrawal of contributions and earnings is not taxed if it is a qualified distribution —the account is held for at least 5 years and made: ✦ because of disability; ✦ after death; or ✦ after attainment of age 59½.
Required Distributions	Distributions must begin no later than age 70½, unless still working and not a 5% owner.	Distributions must begin no later than age 70½, unless still working and not a 5% owner.

[1] All dollar limitations are for 2018

[2] This limitation is by individual, rather than by plan. Although permissible to split the annual employee elective contribution between designated Roth contributions and pre-tax elective contributions, the combination cannot exceed the deferral limit — $18,500 in 2018 ($24,500 if age 50 or over).

FAQs

General Concerns

Q. Can I make both pre-tax elective and designated Roth contributions in the same year?

A. Yes. You can contribute to both a designated Roth account and a pre-tax elective contribution account under the Plan, in the same year and in any proportion you choose. However, the combined amount of all elective contributions you make in 2018 is limited to $18,500. An additional $6,000 in catch-up contributions, for persons 50 or older, can also be allocated between the pre-tax and designated Roth accounts

Q. Can I change my mind and have designated Roth contributions treated as pre-tax elective contributions?

A. No. Once you designate contributions as Roth contributions, you cannot later change them to pre-tax elective contributions.

Q. Does the Commonwealth need to establish a new account in the 403(b) plan to receive my designated Roth contributions?

A. Yes. Designated Roth contributions must be kept completely separate from previous and current 403(b) pre-tax elective contributions. So, the Commonwealth must establish a separate Provider account for each participant making designated Roth contributions; always segregating before-tax and after-tax assets for you.

Designated Roth Account Distributions

Q. What is a qualified distribution from a designated Roth account?

A. A qualified distribution is generally a distribution made after a 5-taxable-year period of participation. The 5-taxable-year period of participation begins on the first day of your taxable year for which you first made designated Roth contributions to your plan. It ends when 5-***consecutive***-taxable-years have passed., ***and*** is either:

- made on or after the date you attain age 59½,
- made on or after your death, or
- attributable to your being disabled.

A qualified distribution from a designated Roth account is not includible in your taxable gross income.

Q. What happens if I take a distribution from my designated Roth account before the end of the 5-taxable year period?

A. If you take a distribution from your designated Roth account before the end of the 5-taxable-year period, it is a nonqualified distribution. (The 5-taxable-year period of participation begins on the first day of your taxable year for which you first made designated Roth contributions to your plan. It ends when 5-***consecutive***-taxable-years have passed.) You must include the investment gain/interest portion of the nonqualified distribution in your taxable gross income and it ***may also*** be subject to the 10% early withdrawal penalty from the IRS. However, the contributions (your "basis") portion of the nonqualified distribution ***is not included*** in your taxable gross income. The basis portion of the distribution is determined by multiplying the amount of the nonqualified distribution by the ratio of designated Roth contributions to the total designated Roth account balance.

Example: If a nonqualified distribution of $5,000 is made from your designated Roth account when the account consists of $9,400 of designated Roth contributions and $600 of investment earnings, the distribution consists of $4,700 of designated Roth contributions (the basis not includible in your gross taxable income) and $300 of investment earnings (that are includible in your gross taxable income).

Q. Since I make designated Roth contributions from after-tax income (already taxed income), can I make tax-free withdrawals from my designated Roth account at any time?

A. No. The same restrictions on withdrawals that apply to pre-tax elective contributions also apply to designated Roth contributions. This includes hardship withdrawals. The hardship distribution will consist of a pro-rata share of earnings and basis and the earnings portion will be included in gross income unless you have had the designated Roth account for 5 years and are either disabled or over age 59½.

Q. May a qualified distribution of my Roth assets be rolled over, tax-free?

A. Yes. However, the assets may be rolled over only to either another designated Roth account or a Roth IRA. The rollover must be made *directly* from the Plan to another plan or Roth IRA.

Q. Is a distribution from my designated Roth account for reasons beyond my control (for example, plan termination or severance from employment) a qualified distribution even though it does not meet the criteria for a qualified distribution?

A. No. If you have not held the account for more than 5 years or if the distribution is not made after death, disability or age 59½, then the distribution is not a qualified distribution. However, you could roll the distribution over into a designated Roth account in another plan or into your

Roth IRA in order to avoid current taxation of the distribution. A transfer to another designated Roth account must be made through a rollover ***directly*** from this plan to the other plan/Roth IRA.

In-Plan Roth Rollover

Q. What is an "in-plan Roth rollover"?

A. An in-plan Roth rollover is a distribution from your current pre-tax retirement account (that doesn't hold designated Roth contributions) that you roll over to your designated Roth account ***within the plan***.

Q. Who is eligible to make an in-plan Roth rollover?

A. Participants, surviving spouse beneficiaries and alternate payees (who are current or former spouses) are eligible to make an in-plan Roth rollover in the plan. However, the individual making the in-plan Roth rollover must be eligible for a distribution from the non-Roth account. For example, they are at least age 59 ½ or have terminated employment with the Commonwealth. Your beneficiaries have this option upon your death.

Q. How can I make an in-plan Roth rollover?

A. In order to make an in-plan Roth rollover, you can make:

- **a direct rollover** — by asking the Plan Administrator to transfer an eligible rollover distribution from your non-Roth account or accounts in the plan to your designated Roth account in the same plan; or
- **a 60-day rollover** — by having the plan distribute an eligible rollover distribution to you from your non-Roth account or accounts in the plan and then depositing all or part of that distribution to your designated Roth account in the same plan within 60 days. Since designated Roth accounts hold only after-tax contributions (and earnings on those contributions), any pre-tax amount rolled into a designated Roth account from a non-Roth account must be included in your gross taxable income.

Make better decisions about your retirement today, and you'll thank yourself tomorrow!