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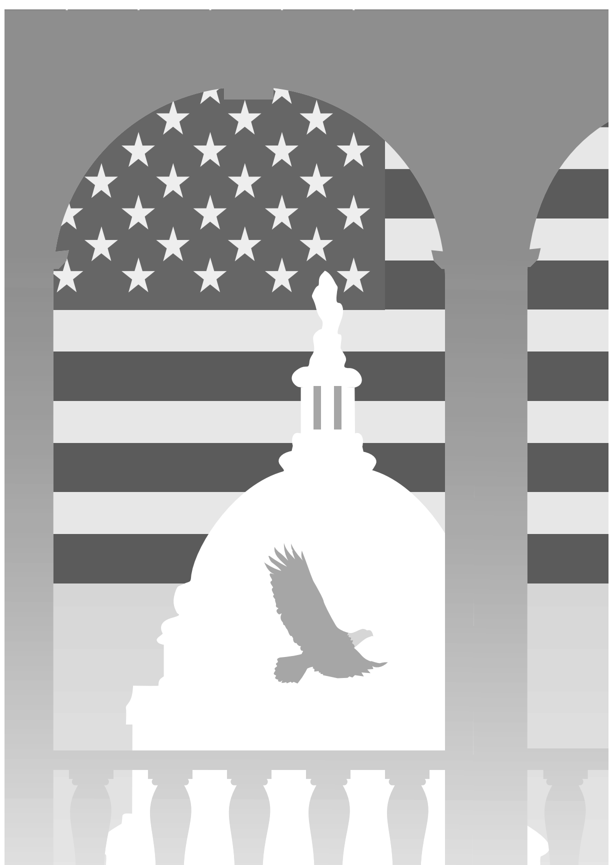
Tax-Sheltered Annuity Plans (403(b) Plans)

For Employees of Public Schools and Certain Tax-Exempt Organizations



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Contents

Important Changes

Changes effective after 2001. Recent legislation made several changes to 403(b) plans that will take effect for years beginning after 2001. Among these changes are the repeal of the maximum exclusion allowance and the alternative limits on annual additions. These changes as well as other changes that may affect your participation in a 403(b) plan, will be discussed in Publication 553, *Highlights of 2001 Tax Changes*, which will be available in January 2002, and in the next edition of Publication 571.

Amounts previously excludable. Effective January 1, 2000, your amounts previously excludable for purposes of figuring your maximum exclusion allowance (MEA) does not include contributions to a defined benefit plan. See chapter 3.

Increase in limit on annual additions. Effective January 1, 2001, the limit on annual additions, as figured under the general rule, is the lesser of $35,000 or your compensation. This is an increase from the lesser of $30,000 or your compensation. See chapter 4.

Increase in limit on contributions to 403(b) plan and 457 plan. Effective January 1, 2001, the general limit on contributions in the same year to both a 403(b) plan and a 457 plan is the lesser of $8,500 or one-third of your includible compensation. This is an increase from the lesser of $8,000 or one-third of your includible compensation. See chapter 8.

Includible compensation. Your includible compensation for purposes of figuring your maximum exclusion allowance (MEA) includes the value of qualified transportation fringe benefits received from your employer. Your MEA is the amount of employer contributions (including elective deferrals) to your 403(b) account that you can exclude from income. See chapter 3.

Compensation. Your compensation for purposes of figuring your limit on annual additions includes the value of qualified transportation fringe benefits received from your employer. Your limit on annual additions restricts the amount of employer contributions (including elective deferrals) that can be made to your 403(b) account and that you can exclude from income. See chapter 4.

Important Reminder

Photographs of missing children. The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children. Photographs of missing children selected by the Center may appear in this publication on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling **1–800–THE–LOST (1–800–843–5678)** if you recognize a child.

Introduction

This publication has been revised to help you better understand the tax rules that apply to your 403(b) (tax-sheltered annuity) plan.

In this publication you will find information to help you:

1) Determine the maximum amount that can be contributed to your 403(b) account in the current year,
2) Determine the maximum amount that could have been contributed to your 403(b) account in the previous year,
3) Identify excess contributions,
4) Determine the contribution limits for years in which contributions are made to both a 403(b) plan and a 457 plan, and
5) Understand the basic rules for distributions and rollovers from 403(b) accounts.

This publication does not provide specific information on the following topics.

- Distributions from 403(b) accounts. This is covered in Publication 575, *Pension and Annuity Income.*
- Rollovers. This is covered in Publication 590, *Individual Retirement Arrangements (IRAs).*

How to use this publication. This publication is organized into chapters to help you find information easily.

Chapter 1 will answer questions frequently asked by 403(b) plan participants.

Chapters 2 through 5 will explain the terms and rules you will need to figure the maximum amount that can be contributed to your 403(b) account.

Chapter 6 will discuss alternative methods of figuring the maximum amount that can be contributed to your 403(b) account.

Chapter 7 will provide information for ministers and church employees regarding their 403(b) accounts.

If you contribute to both a 403(b) plan and a 457 deferred compensation plan in the same year, chapter 8 will provide needed information on your contribution limits. Chapter 8 will not give you detailed information on 457 plans. For additional information on 457 plans, contact your plan administrator.

Chapter 9 will provide general information on the prevention and correction of excess contributions to your 403(b) account.

Chapter 10 will provide general information on distributions and rollovers.

Chapter 11 will provide blank worksheets that you will need to accurately and actively participate in your 403(b) plan. The blank worksheets are the same as the filled-in worksheets that are found throughout this publication.

Comments and suggestions. We welcome your comments about this publication and your suggestions for future editions.

You can e-mail us while visiting our web site at **www.irs.gov/help/email2.html**.

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We respond to many letters by telephone. Therefore, it would be helpful if you would include your area code and daytime phone number in your correspondence.

Useful Items

You may want to see:

Publication

- ☐ **517** Social Security and Other Information for Members of the Clergy and Religious Workers
- ☐ **575** Pension and Annuity Income
- ☐ **590** Individual Retirement Arrangements (IRAs)

Form (and Instructions)

- ☐ **W–2** Wage and Tax Statement
- ☐ **1099–R** Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.
- ☐ **5330** Return of Excise Taxes Related to Employee Benefit Plans

1. 403(b) Plan Basics

This chapter will introduce you to 403(b) plans and accounts. Specifically, the chapter will answer the following questions.

- What is a 403(b) plan?
- Who can participate in a 403(b) plan?
- Who can set up a 403(b) account?
- How can contributions be made to my 403(b) account?
- Do I report contributions on my tax return?
- How much can be contributed to my 403(b) account?

What is a 403(b) Plan?

A 403(b) plan, also known as a tax-sheltered annuity (TSA) plan, is a retirement plan for certain employees of public schools, employees of certain tax-exempt organizations, and certain ministers.

Individual accounts in a 403(b) plan can be any of the following types.

- An annuity contract, which is a contract provided through an insurance company,
- A custodial account, which is an account invested in mutual funds, or
- A retirement income account set up for church employees. Generally, retirement income accounts can invest in either annuities or mutual funds.

Note. Throughout this publication, wherever the term ***403(b) account*** is used, it refers to any one of these funding arrangements, unless otherwise specified.

What are the Benefits of Contributing to a 403(b) Plan?

There are two benefits to contributing to a 403(b) plan.

- The first benefit is that you do not pay tax on the contributions in the year they are made. You do not pay tax on them until you begin making withdrawals from the plan, usually after you retire. Contributions to a 403(b) plan are either excluded or deducted from your income.
- The second benefit is that earnings and gains on amounts in your 403(b) account are not taxed until you withdraw them.

Excluded. If an amount is excluded from your income, it is not included in your total wages on your Form W-2. This means that you do not report the excluded amount on your tax return.

Deducted. If an amount is deducted from your income, it is included with your other wages on your Form W-2. You report this amount on your tax return, but you are allowed to subtract it when figuring the amount of income on which you must pay tax.

Who Can Participate in a 403(b) Plan?

Any eligible employee can participate in a 403(b) plan.

Eligible employees. The following employees are eligible to participate in a 403(b) plan.

1) Employees of tax-exempt organizations established under section 501(c)(3) of the Internal Revenue Code. These organizations are usually referred to as ***section 501(c)(3) organizations*** or simply ***501(c)(3) organizations***.
2) Certain employees of public school systems. These are employees involved in the day-to-day operations of a school.
3) Employees of cooperative hospital service organizations.
4) Civilian faculty and staff of the Uniformed Services University of the Health Sciences (USUHS). (Contributions made after 1979 for the benefit of faculty and staff of USUHS are subject to the rules described in this publication.)
5) Employees of public school systems organized by an Indian tribal government.
6) Certain ministers (explained later).

Ministers. The following ministers are eligible employees for whom a 403(b) account can be established.

1) Ministers employed by section 501(c)(3) organizations.
2) Self-employed ministers. A self-employed minister is treated as employed by a tax-exempt organization that is a qualified employer.
3) Ministers who meet all three of the following requirements.
    a) Are employed by organizations that are not section 501(c)(3) organizations.
    b) Function as ministers in their day-to-day professional responsibilities with their employers.
    c) Do not share common religious bonds with their employers.

Note. Throughout this publication, the term ***chaplain*** will be used to mean ministers described in the third category in the list above.

Example. A minister employed as a chaplain by a state-run prison and a chaplain in the United States Armed Forces are eligible employees because their employers are not section 501(c)(3) organizations, they are employed as ministers, and their employers do not share their religious affiliation.

Who Can Set Up a 403(b) Account?

You cannot set up your own 403(b) account. Only employers can set up 403(b) accounts.

How Can Contributions Be Made to My 403(b) Account?

Generally, only your employer can make contributions to your 403(b) account. However, some plans will allow you to make after-tax contributions (defined later).

The following types of contributions can be made to 403(b) accounts.

1) **Elective deferrals**. These are contributions made under a salary reduction agreement. This agreement allows your employer to withhold money from your paycheck to be contributed directly into a 403(b) account for your benefit. You do not pay tax on these contributions until you withdraw them from the account.
2) **Nonelective contributions** . These are employer contributions that are not made under a salary reduction agreement. You do not pay tax on these contributions until you withdraw them from the account. Nonelective contributions include matching contributions, discretionary contributions and mandatory contributions from your employer.
3) **After-tax contributions**. These are contributions you make with funds that you must include in income on your tax return. A salary payment on which income tax has been withheld is a source of these contributions. If your plan allows you to make after-tax contributions, they are not excluded from income and you cannot deduct them on your tax return.
4) **A combination** of any of the three contribution types listed above.

Self-employed minister. If you are a self-employed minister, you are considered both an employee and an employer, and you can contribute to a retirement income account for your own benefit.

Do I Report Contributions on My Tax Return?

Generally, you do not report contributions to your 403(b) account on your tax return. Your employer will report contributions, other than after-tax contributions, on your Form W-2. The amount contributed to your 403(b) account will be shown in box 13 and the ***Pension plan*** box will be checked. If you are a self-employed minister or chaplain, see the discussions below.

Self-employed ministers. If you are a self-employed minister, you must report the total contributions as a deduction on your tax return. Deduct your contributions on line 29 of Form 1040.

Chaplains. If you are a chaplain and your employer does not exclude contributions made to your 403(b) account from your earned income, you may be able to take a deduction for those contributions on your tax return.

However, if your employer has agreed to exclude the contributions from your earned income, you will not be allowed a deduction on your tax return.

If you can take a deduction enter your contributions on line 32 of Form 1040. Write ***403(b)*** on the dotted line next to line 32.

How Much Can Be Contributed to My 403(b) Account?

There are limits on the amount of contributions that can be made to your 403(b) account each year. If contributions made to your 403(b) account are more than these contribution limits, penalties may apply.

Chapters 2 through 6 will provide information on how to determine the amount that can be contributed to your 403(b) account.

CAUTION *For years in which you contribute to both a 403(b) plan and a 457 plan, the information discussed in chapters 2 through 6 does not apply to you. You will need to read Chapter 8,* Contributing to Both a 403(b) Plan and a 457 Plan.

Worksheets are provided in chapter 11 to help you determine the maximum amount that can be contributed to your 403(b) account each year. Chapter 9, *Excess Contributions,* describes steps you can take to prevent excess contributions and to get an excess contribution corrected.

2. Maximum Amount Contributable (MAC)

Throughout this publication, the limit on the amount that can be contributed to your 403(b) account for any year is referred to as your maximum amount contributable (MAC). This chapter will:

- Introduce you to the components of your MAC,
- Tell you how to figure your MAC, and
- Tell you when to figure your MAC,

For years in which you contribute to both a 403(b) plan and a 457 plan, the information discussed in this chapter does not apply to you. You will need to read chapter 8.

Components of Your MAC

Generally, before you can determine your MAC, you must first figure the three components of your MAC. The three components of your MAC are the:

1) Maximum exclusion allowance (MEA) (chapter 3),
2) Limit on annual additions (chapter 4), and
3) Limit on elective deferrals (chapter 5).

How Do I Figure My MAC?

Generally, contributions to a 403(b) account are limited to the least of:

- The MEA,
- The limit on annual additions, or
- The limit on elective deferrals.

Depending upon the type of contributions made to your 403(b) account, only two of the limits may apply to you for a given tax year.

General contribution limits. If all of the contributions made to your 403(b) account are elective deferrals (salary reductions), you will need to figure all three of the limits listed above. Your MAC is the least of the three limits.

Only nonelective contributions. If all of the contributions made to your 403(b) account are nonelective contributions, you will need to figure only the MEA and the limit on annual additions. Your MAC is the smaller of these two limits.

Elective deferrals and nonelective contributions. If the contributions made to your 403(b) account are a combination of both elective deferrals and nonelective contributions, you will need to figure the MEA, the limit on annual additions, and the limit on elective deferrals. Your MAC is the lesser of your MEA or your limit on annual additions.

However, you need to figure the limit on elective deferrals to determine whether the amount contributed to your 403(b) account is more than your allowable limit. For information on the limit on elective deferrals, see chapter 5.

Alternative limits. If you are an employee of certain tax-exempt organizations, you may be eligible to figure your MAC using the following limits.

- An alternative limit (explained in Chapter 6, *Alternative Limits*).
- An increased limit on elective deferrals (explained in Chapter 5, *Limit on Elective Deferrals*).

You may be able to use the limits listed above if you are an eligible employee (described in chapter 1) of one of the following organizations.

- An educational organization.
- A hospital.
- A home health service agency.
- A health and welfare service agency.
- A church, convention, or association of churches.

Church employees. In addition to the alternative limits and the increased limit on elective deferrals, certain church employees may be able to figure the components of MAC using different methods. See Chapter 7, *Ministers and Church Employees*.

Worksheets. Worksheets are available in chapter 11 to help you figure your MAC.

When Should I Figure My MAC?

You should figure your MAC at the beginning of each tax year using a conservative estimate of your earned income. If your earned income changes during the year, you should refigure your MAC based on a revised conservative estimate. By doing this, you will be able to determine if contributions to your 403(b) account should be increased or decreased for the year.

At the beginning of the following year, you should refigure your MAC based on your actual earned income. This will allow you to determine if the amount that has been contributed to your 403(b) account has exceeded the allowable limits and, in some cases, avoid penalties and additional taxes. See chapter 9.

3. Maximum Exclusion Allowance (MEA)

The maximum exclusion allowance (MEA) is the first component of MAC. Your MEA is the limit on the amount of contributions your employer can make to your 403(b) account for any year.

You need to figure your MEA separately for each employer who has established a 403(b) account for your benefit. When figuring your MEA, do not mix the information of one employer with the information of another employer.

CAUTION ***More than one account, same employer.*** *If during any tax year, you have two or more 403(b) accounts maintained by the same employer, figure only one MEA for all 403(b) accounts maintained by that employer because they are considered one account.*

More than one employer. *If more than one employer contributes to a 403(b) account for you, you must figure a separate MEA for each employer.*

MEA formula. To figure your MEA you will need to understand the following concepts.

- Years of service.
- Includible compensation for your most recent year of service.
- Amounts previously excludable.

Your MEA is ***20% of your includible compensation for your most recent year of service*** multiplied by your ***years of service***, and then reduced by ***amounts previously excludable***.

You can use Worksheet A, *Maximum Exclusion Allowance (MEA),* in chapter 11 to figure your MEA.

Church employees. If you are a church employee, you may be able to use different rules when figuring your MEA. For more information see chapter 7.

Years of Service

The first step in figuring your MEA is to determine your ***years of service***. How you figure your years of service depends on whether you were a full-time or a part-time employee, whether you worked for the full year or only part of the year, and whether you have worked for your employer for an entire year.

You must figure years of service for each year during which you worked for the employer who is maintaining your 403(b) account.

If more than one employer maintains a 403(b) account for you in the same year, you must figure years of service separately for each employer.

Definition

Your years of service are the total number of years you have worked for the employer maintaining your 403(b) account as of the end of the year for which you are figuring your MEA.

Figuring Your Years of Service

Take the following rules into account when figuring your years of service.

Status of employer. Your years of service will only include periods during which your employer was a qualified employer. Your plan administrator can tell you whether or not your employer was qualified during all your periods of service.

Service with one employer. Generally, you cannot count service for any employer other than the one who maintains your 403(b) account.

Church employee. If you are a church employee, treat all of your years of service with related church organizations as years of service with the same employer. For more information about church employees, see chapter 7.

Self-employed ministers. If you are a self-employed minister, your years of service include full and part years in which you have been treated as employed by a tax-exempt organization that is a qualified employer.

Less than one year of total service. Your years of service cannot be less than one year. If at the end of your tax year, you have less than one year of service (including service in any previous years), figure your MEA as if you have one year.

Total years of service. When figuring years of service, figure each year individually and then add the individual years of service to determine your total years of service, which will be used when figuring your MEA.

Example. The annual work period for full-time teachers employed by ABC Public Schools is September through December and February through May. Marsha began working with ABC schools in September 1997. She has always worked full time for each annual work period. At the end of 2001, Marsha will have 4.5 years of service with ABC Public Schools, as shown in Table 3-1.

Table 3-1. **Marsha's Years of Service**

Note: *This table shows how Marsha figures her years of service, as explained in the previous example.*

Year	Period Worked	Portion of Work Period	Years of Service
1997	Sept.—Dec.	.5 year	.5 year
1998	Feb.—May	.5 year	1 year
	Sept.—Dec.	.5 year	
1999	Feb.—May	.5 year	1 year
	Sept.—Dec.	.5 year	
2000	Feb.—May	.5 year	1 year
	Sept.—Dec.	.5 year	
2001	Feb.—May	.5 year	1 year
	Sept.—Dec.	.5 year	
Total years of service			**4.5 years**

To figure your years of service, you must analyze each year individually and determine whether you worked full time for the full year or something other than full time. When determining whether you worked full time or something other than full time, you use your employer's annual work period as the standard.

Employer's annual work period. Your employer's annual work period is the usual amount of time an individual working full time in a specific position is required to work. Generally, this period of time is expressed in days, weeks, months, or semesters and can span two calendar years.

Example. All full-time teachers at ABC Public Schools are required to work both the September through December semester and the February through May semester. Therefore, the annual work period for full-time teachers employed by ABC Public Schools is September through December and February through May. Teachers at ABC Public Schools who work both semesters in the same calendar year are considered working a full year of service in that calendar year.

Full-Time Employee for the Full Year

Count each full year during which you were employed full time as one year of service. In determining whether you were employed full time, compare the amount of work you were required to perform with the amount of work normally required of others who held the same position with the same employer and who generally received most of their pay from the position.

How to compare. You can use any method that reasonably and accurately reflects the amount of work required. For example, if you are a teacher, you can use the number of hours of classroom instruction as a measure of the amount of work required.

In determining whether positions with the same employer are the same, consider all of the facts and circumstances concerning the positions, including the work performed, the methods by which pay is determined, and the descriptions (or titles) of the positions.

Example. An assistant professor employed in the English department of a university will be considered a full-time employee if the amount of work that he or she is required to perform is the same as the amount of work normally required of assistant professors of English at that university who get most of their pay from that position.

If no one else works for your employer in the same position, compare your work with the work normally required of others who held the same position with similar employers or similar positions with your employer.

Full year of service. A full year of service for a particular position means the usual annual work period of anyone employed full time in that general type of work at that place of employment.

Example. If a doctor works for a hospital 12 months of a year except for a one-month vacation, the doctor will be considered as employed for a full year if the other doctors at that hospital also work 11 months of the year with a one-month vacation. Similarly, if the usual annual work period at a university consists of the fall and spring semesters, an instructor at that university who teaches these semesters will be considered as working a full year.

Other Than Full Time for the Full Year

If, during any year, you were employed full time for only part of your employer's annual work period, part time for the entire annual work period, or part time for only part of the work period, your year of service for that year is a fraction of your employer's annual work period.

Full time for part of the year. If, during a year, you were employed full time for only part of your employer's annual work period, figure the fraction for that year as follows.

- The numerator (top number) is the number of weeks, months, or semesters you were a full-time employee.
- The denominator (bottom number) is the number of weeks, months, or semesters considered the normal annual work period for the position.

Example. Jason was employed as a full-time instructor by a local college for the 4 months of the 2000 spring semester (February 2000 through May 2000). The annual work period for the college is 8 months (February through May and July through October). Given these facts, Jason was employed full time for part of the annual work period and provided ½ of a year of service. Jason's years of service computation for 2000 is as follows.

$$\frac{\text{Number of months Jason worked}}{\text{Number of months in annual work period}} = \frac{4}{8} = \frac{1}{2}$$

Part time for the full year. If, during a year, you were employed part time for the employer's entire annual work period, you figure the fraction for that year as follows.

- The numerator (top number) is the number of hours or days you worked.
- The denominator (bottom number) is the number of hours or days required of someone holding the same position who works full time.

Example. Vance teaches one course at a local medical school. He teaches 3 hours per week for two semesters. Other faculty members at the same school teach 9 hours per week for two semesters. The annual work period of the medical school is two semesters. An instructor teaching 9 hours a week for two semesters is considered a full-time employee. Given these facts, Vance has worked part time for a full annual work period. Vance has completed ⅓ of a year of service, figured as shown below.

$$\frac{\text{Number of hours per week Vance worked}}{\text{Number of hours per week considered full time}} = \frac{3}{9} = \frac{1}{3}$$

Part time for part of the year. If, during any year, you were employed part time for only part of your employer's annual work period, you figure your fraction for that year by multiplying two fractions.

Figure the first fraction as though you had worked full time for part of the annual work period. The fraction is as follows.

- The numerator (top number) is the number of weeks, months, or semesters you were a full-time employee.
- The denominator (bottom number) is the number of weeks, months, or semesters considered the normal annual work period for the position.

Figure the second fraction as though you had worked part time for the entire annual work period. The fraction is as follows.

- The numerator (top number) is the number of hours or days you worked.
- The denominator (bottom number) is the number of hours or days required of someone holding the same position who works full time.

Once you have figured these two fractions, multiply them together to determine the fraction representing your partial year of service for the year.

Example. Maria, an attorney, teaches a course for one semester at a law school. She teaches 3 hours per week. The annual work period for teachers at the school is two semesters. All full-time instructors at the school are required to teach 12 hours per week. Based on these facts, Maria is employed part time for part of the annual work period. Her year of service for this year is determined by multiplying two fractions. Her computation is as follows.

Maria's first fraction:

$$\frac{\text{Number of semesters Maria worked}}{\text{Number of semesters in annual work period}} = \frac{1}{2}$$

Maria's second fraction:

$$\frac{\text{Number of hours Maria worked per week}}{\text{Number of hours per week considered full time}} = \frac{3}{12} = \frac{1}{4}$$

Maria would multiply these fractions to obtain the fractional year of service:
$\frac{1}{2} \times \frac{1}{4} = \frac{1}{8}$.

Includible Compensation for Your Most Recent Year of Service

After you have figured your years of service, the next step in figuring your MEA is determining your includible compensation for your most recent year of service. When figuring includible compensation for your most recent year of service, do not mix compensation or service of one employer with compensation or service of another employer.

Most Recent Year of Service

Your most recent year of service is your last full year of service, ending on the last day of your tax year that you worked for the employer that maintains a 403(b) account on your behalf. To figure your most recent year of service, you will need to understand the rules discussed under *Years of Service*, earlier.

When determining your includible compensation, for purposes of figuring your MEA, keep in mind that your most recent year of service may not be the same as your employer's most recent annual work period. This can happen if your tax year is not the same as your employer's annual work period.

Tax year different from employer's annual work period. If your tax year is not the same as your employer's annual work period, your most recent year of service is made up of parts of at least two of your employer's annual work periods.

Example. A professor who reports her income on a calendar-year basis is employed on a full-time basis by a university that operates on an academic year (October through May). For purposes of figuring her MEA for 2000, the professor's most recent year of service consists of her service performed during January through May of 2000 and her service performed during October through December of 2000.

Figuring Your Most Recent Year of Service

To figure your most recent year of service, begin by determining what constitutes a full year of service for your position. A full year of service is equal to full-time employment for your employer's annual work period.

After identifying a full year of service, begin counting the service you have provided for your employer starting with the service provided in the year for which you are figuring your MEA. To help you count your years of service, follow the rules discussed under *Figuring Your Years of Service*, earlier.

Part-time or employed only part of year. If you are a part-time employee, or a full-time employee who is employed for only part of the year, your most recent year of service consists of your service this year and your service for as many previous years as is necessary to total one full year of service. You add up your most recent periods of service to determine your most recent year of service. First, take into account your service during the year for which you are figuring the MEA. Then add your service during your next preceding tax year, and years before that, until your total service equals one year of service.

Example. You were employed on a full-time basis during the months July through December 1998 (1/2 year of service), July through December 1999 (1/2 year of service), and October through December 2000 (1/4 year of service). Your most recent year of service for purposes of computing your MEA for 2000 is the total of your service during 2000 (1/4 year of service), your service during 1999 (1/2 year of service), and your service during the months October through December 1998 (1/4 year of service).

Not yet employed for one year. If, at the close of the year for which you are figuring your MEA, you have not yet worked for your employer for one year (including time you worked for the same employer in earlier years), use the period of time you have worked for the employer as your most recent year of service.

Includible Compensation

After identifying your most recent year of service, the next step is to identify the includible compensation associated with that full year of service.

Includible compensation is not the same as income included on your tax return. Compensation is a combination of income and benefits received in exchange for services provided to your employer.

Generally, includible compensation is the amount of pay:

1) Received from the employer who maintains your 403(b) account, and
2) That you must include in income.

You determine the amount you must include in income without taking into account the foreign earned income exclusion.

For purposes of figuring your MEA, includible compensation ***does*** include the following amounts.

1) Elective deferrals (employer's contributions made on your behalf under a salary reduction agreement).
2) Amounts contributed or deferred by your employer under a section 125 cafeteria plan.
3) Amounts contributed or deferred, at the election of the employee, under an eligible section 457 nonqualified deferred compensation plan (state or local government or tax-exempt organization plan).
4) Wages, salaries, and fees for personal services earned with the employer maintaining your 403(b) account.
5) Income otherwise excluded under the foreign earned income exclusion.
6) The value of qualified transportation fringe benefits.

Includible compensation ***does not*** include the following items.

1) Your employer's contributions to your 403(b) account.
2) Compensation earned while your employer was not an eligible employer.
3) Your employer's contributions to a qualified plan that:
   a) Are on your behalf, and
   b) You can exclude from income.
4) Contributions that are more than your MEA.
5) The cost of incidental life insurance.

Note. If you are a church employee or a foreign missionary, you will figure includible compensation using the method explained in chapter 7.

Cost of Incidental Life Insurance

Includible compensation does not include the cost of incidental life insurance.

Note. If all of your 403(b) accounts invest only in mutual funds, then you have no incidental life insurance.

If you have an annuity contract, a portion of the cost of that contract may be for incidental life insurance. If so, the cost of the insurance is taxable to you in the year contributed and is considered part of your basis when distributed. Your employer will include the cost of your insurance as taxable wages in box 1 of Form W-2.

Not all annuity contracts include life insurance. Contact your plan administrator to determine if your account includes incidental life insurance. If it does, you will need to figure the cost of life insurance each year the policy is in effect.

Figuring the cost of incidental life insurance. If you have determined that part of the cost of your annuity contract is for an incidental life insurance premium, you will need to determine the amount of the premium and subtract it from your includible compensation.

To determine the amount of the life insurance premiums you will need to know the following information.

- The value of your life insurance contract, which is the amount payable upon your death.
- The cash value of your life insurance contract at the end of the tax year.
- Your age on your birthday nearest the beginning of the policy year.
- Your current life insurance protection under an ordinary retirement income life insurance policy, which is the amount payable upon your death minus the cash value of the contract at the end of the year.

Example. Your new contract provides that your beneficiary will receive $10,000 if you should die anytime before retirement. Your cash value in the contract at the end of the first year is zero. Your current life insurance protection for the first year is $10,000 ($10,000 minus 0).

The cash value in the contract at the end of year two is $1,000, and the current life insurance protection for the second year is $9,000 ($10,000 – $1,000).

You can use Worksheet B in chapter 11 to determine the cost of your life insurance.

The one-year cost of the protection can be calculated by using Figure 3-1, *Uniform One-Year Term Premiums for $1,000 Life Insurance Protection*. The premium rate is determined according to your age on your birthday nearest the beginning of the policy year.

Figure 3-1. **Uniform One-Year Term Premiums for $1,000 Life Insurance Protection**

[Based on Table 38, U.S. Life Table and Actuarial Table (U.S. Government Printing Office, Washington, D.C.–1946), and 2½% interest.]

Age	Cost	Age	Cost
15	$1.27	49	$8.53
16	1.38	50	9.22
17	1.48	51	9.97
18	1.52	52	10.79
19	1.56	53	11.69
20	1.61	54	12.67
21	1.67	55	13.74
22	1.73	56	14.91
23	1.79	57	16.18
24	1.86	58	17.56
25	1.93	59	19.08
26	2.02	60	20.73
27	2.11	61	22.53
28	2.20	62	24.50
29	2.31	63	26.63
30	2.43	64	28.98
31	2.57	65	31.51
32	2.70	66	34.28
33	2.86	67	37.31
34	3.02	68	40.59
35	3.21	69	44.17
36	3.41	70	48.06
37	3.63	71	52.29
38	3.87	72	56.89
39	4.14	73	61.89
40	4.42	74	67.33
41	4.73	75	73.23
42	5.07	76	79.63
43	5.44	77	86.57
44	5.85	78	94.09
45	6.30	79	102.23
46	6.78	80	111.04
47	7.32	81	120.57
48	7.89		

Note. *If the current published premium rates per $1,000 of insurance protection* *charged by an insurer for individual one-year term life insurance premiums available to all standard risks are lower than those in the preceding table, you can use the lower rates for figuring the cost of insurance in connection with individual policies issued by the same insurer.*

Example. Lynne Green and her employer enter into a 403(b) plan that will provide her with a $500 a month annuity upon retirement at age 65. The agreement also provides that if she should die before retirement, her beneficiary will receive the greater of $20,000 or the cash surrender value in the life insurance contract. Using the facts presented we can determine the cost of Lynne's life insurance protection as shown in Table 3-2.

Table 3-2. **Worksheet B. Cost of Life Insurance**

Note: *Use this worksheet to figure the cost of incidental life insurance included in your annuity contract. This amount will be used to figure includible compensation for your most recent year of service.*

1.	Enter the value of the contract (amount payable upon your death)	$ 20,000.00
2.	Enter the cash value in the contract at the end of the year	$ 0
3.	Subtract line 2 from line 1. This is the **value of your current life insurance protection** .	$ 20,000.00
4.	Enter your age on your birthday nearest the beginning of the policy year	44
5.	Enter the 1-year term premium for $1,000 of life insurance based on your age (Figure 3-1) .	$ 5.85
6.	Divide line 3 by **$1,000** .	$ 20
7.	Multiply line 6 by line 5. This is the **cost of your incidental life insurance**	$ 117.00

Lynne's employer has included $117 for the cost of the life insurance protection in her current year's income. When figuring her includible compensation for this year, Lynne will subtract $117.

Example. Lynne's cash value in the contract at the end of the second year is $1,000. In year two, the cost of Lynne's life insurance is calculated as shown in Table 3-3.

Table 3-3. **Worksheet B. Cost of Life Insurance**

Note: *Use this worksheet to figure the cost of incidental life insurance included in your annuity contract. This amount will be used to figure includible compensation for your most recent year of service.*

1.	Enter the value of the contract (amount payable upon your death)	$ 20,000.00
2.	Enter the cash value in the contract at the end of the year. . . .	$ 1,000.00
3.	Subtract line 2 from line 1. This is the **value of your current life insurance protection**	$ 19,000.00
4.	Enter your age on your birthday nearest the beginning of the policy year	45
5.	Enter the 1-year term premium for $1,000 of life insurance based on your age. (Figure 3-1)	$ 6.30
6.	Divide line 3 by **$1,000**	$ 19
7.	Multiply line 6 by line 5. This is the **cost of your incidental life insurance**. . . .	$ 119.70

In year two Lynne's employer will include $119.70 in her current year's income. Lynne will subtract this amount when figuring her includible compensation.

Figuring Includible Compensation for Your Most Recent Year of Service

You can use Worksheet C in chapter 11 to determine your includible compensation for your most recent year of service.

Example. Floyd has been periodically working full time for a local hospital since September 1998. He needs to figure his MEA for 2001. The hospital's normal annual work period for employees in Floyd's general type of work runs from January to December.

During the periods that Floyd was employed with the hospital, the hospital has always been eligible to provide a 403(b) plan to employees. Additionally, the hospital has never provided the employees with a 457 deferred compensation plan, transportation benefits, or a cafeteria plan.

Floyd has never worked abroad. There is no life insurance provided under the plan and contributions to Floyd's account have never been more than his MEA.

Table 3-4 shows the service Floyd provided to his employer, his compensation for the periods worked and his elective deferrals. The increase between 2000 and 2001 is due to new skills.

Table 3-4. **Floyd's Compensation**

Note: *This table shows information Floyd will use to figure includible compensation for his most recent year of service.*

Year	**Years of Service**	**Taxable Wages**	**Elective Deferrals**
2001	6/12 of a year	$42,000	$2,000
2000	4/12 of a year	$16,000	$1,650
1999	4/12 of a year	$16,000	$1,650

Before Floyd can figure his MEA, he must figure includible compensation for his most recent year of service.

Because Floyd will not work for the entire year in 2001, his most recent year of service will include the time he will work in 2001 plus time he worked in earlier years until the time he worked for the hospital totals one year. If the total is less than one year, Floyd will treat it as if it were one year. He figures his most recent year of service shown in the following list.

- Time worked in 2001 is $\frac{6}{12}$ of a year.
- Time worked in 2000 is $\frac{4}{12}$ of a year. All of this time will be used to determine Floyd's most recent year of service.
- Time worked in 1999 is $\frac{4}{12}$ of a year. Floyd only needs 2 months of the 4 months he worked in 1999 to have enough time to total one full year. Because he needs only one-half of the actual time he worked, Floyd will use only one-half of his income earned during that period to calculate wages that will be used in figuring his includible compensation.

Using the information provided in Table 3-4, wages for Floyd's most recent year of service are $66,000 ($42,000 + $16,000 + $8,000) and his includible compensation for his most recent year of service is figured as shown in Table 3-5.

Amounts Previously Excludable

To figure your MEA, you must know the amounts previously excludable from your income.

Amounts previously excludable are the total of all contributions for retirement benefits made for you by your employer that you excluded from your gross income in prior years. Amounts previously excludable do not include amounts excluded for the year for which you are figuring your MEA.

Amounts previously excludable include contributions in earlier years by your employer to:

- Your 403(b) account,
- A qualified annuity plan or a qualified pension, profit-sharing plan, or stock bonus trust,

Table 3-5. **Worksheet C. Includible Compensation for Your Most Recent Year of Service***

Note: *Use this worksheet to figure includible compensation for your most recent year of service. This amount will be used to figure your MEA.*

1.	Enter your includible wages from the employer maintaining your 403(b) account for your most recent year of service	$ 66,000
2.	Enter elective deferrals for your most recent year of service	$ 4,475
3.	Enter amounts contributed or deferred by your employer under a cafeteria plan for your most recent year of service	$ 0
4.	Enter amounts contributed or deferred by your employer to your 457 account for your most recent year of service	$ 0
5.	Enter the value of qualified transportation benefits you received from your employer	$ 0
6.	Enter your foreign earned income exclusion for your most recent year of service	$ 0
7.	Add lines 1, 2, 3, 4, 5, and 6	$ 70,475
8.	Enter the cost of incidental life insurance that is part of your annuity contract for your most recent year of service	$ 0
9.	Enter compensation that was **both:**	
	• Earned during your most recent year of service, and	
	• Earned while your employer was not qualified to maintain a 403(b) plan	$ 0
10.	Enter contributions that are more than your MEA	$ 0
11.	Add lines 8, 9, and 10	$ 0
12.	Subtract line 11 from line 7. This is your **includible compensation for your most recent year of service**	$ 70,475

**Use estimated amounts if figuring includible compensation before the end of the year.*

- A qualified bond-purchase plan,
- A retirement plan under which the contributions originally were excludable by you only because your rights to the contributions were forfeitable when made, and which also were excludable by you when your rights became nonforfeitable. (This does not apply to contributions to purchase an annuity contract if your employer was an exempt organization when the contributions were made.),
- An eligible section 457 deferred compensation plan, even if maintained by a separate employer, or
- Excess contributions made to your 403(b) account that are more than your limit on annual additions.

For years beginning in 2000 or 2001, contributions to a defined benefit plan do not have to be treated as amounts previously excludable. Your employer can tell you if any contributions were made on your behalf to a defined benefit plan.

Figuring MEA

You need to figure MEA separately for each employer who contributes to a 403(b) account for your benefit. When figuring your MEA, do not include amounts contributed, compensation, or years of service for one employer with those for another employer. Special rules apply to church employees, as explained in chapter 7.

The following example shows how to figure MEA. The facts presented in this example will also be used in examples in chapters 4 and 5.

Example

Jerry has been working full time for a local hospital since the beginning of July 1997. Except for 1997, when he worked for one half of the hospital's annual work period, Jerry has worked for the hospital's entire annual work period. Jerry's wages from the hospital are shown in the following chart.

1997	$16,000
1998	32,000
1999	32,000
2000	35,000
2001	35,000

Jerry's employer has set up a 403(b) account for him. In this account, Jerry has chosen to invest 8% of his salary each year in mutual funds through payroll reductions. For 2001, this is $2,800. Jerry is not using an alternative limit on annual additions.

Figure Jerry's years of service. The first thing Jerry will need to do is figure his years of service. In 1997, Jerry worked ½ of the year for his employer. For the years 1998 through 2001, Jerry has been a full-time employee for each of the hospital's entire annual work periods.

Jerry's years of service at the end of 2001 total 4.5 years.

Figure Jerry's includible compensation. The second thing for Jerry to figure is his includible compensation for his most recent year of service. Before he can do this, he must identify his most recent year of service. Jerry is a full-time employee who works the entire annual work period. Jerry's most recent year of service is 2001. Jerry figures his includible compensation as shown in Table 3-6.

Figure Jerry's amounts previously excludable. Jerry's next step is to figure his amounts previously excludable. The 8% contributions made through a salary reduction agreement equal $9,200.

Jerry's MEA. Using the figures for years of service, includible compensation, and amounts previously excludable, Jerry can now use Worksheet A to figure his MEA as shown in Table 3-7.

Figuring Jerry's MAC

Jerry's estimated MEA for 2001 is $24,820.00. However, this is not the maximum amount that can be contributed to his 403(b) account. To determine his MAC, Jerry will need to figure his limit on annual additions (chapter 4) and his limit on elective deferrals (chapter 5).

Table 3-6. **Worksheet C. Includible Compensation for Your Most Recent Year of Service***

Note: *Use this worksheet to figure includible compensation for your most recent year of service. This amount will be used to figure your MEA.*

1.	Enter your includible wages from the employer maintaining your 403(b) account for your most recent year of service	$ 35,000
2.	Enter elective deferrals for your most recent year of service	$ 2,800
3.	Enter amounts contributed or deferred by your employer under a cafeteria plan for your most recent year of service	$ 0
4.	Enter amounts contributed or deferred by your employer to your 457 account for your most recent year of service	$ 0
5.	Enter the value of qualified transportation benefits you received from your employer	$ 0
6.	Enter your foreign earned income exclusion for your most recent year of service	$ 0
7.	Add lines 1, 2, 3, 4, 5, and 6	$ 37,800
8.	Enter the cost of incidental life insurance that is part of your annuity contract for your most recent year of service	$ 0
9.	Enter compensation that was **both:**	
	• Earned during your most recent year of service, and	
	• Earned while your employer was not qualified to maintain a 403(b) plan	$ 0
10.	Enter contributions that are more than your MEA	$ 0
11.	Add lines 8, 9, and 10	$ 0
12.	Subtract line 11 from line 7. This is your **includible compensation for your most recent year of service**	$ 37,800

**Use estimated amounts if figuring includible compensation before the end of the year.*

Table 3-7. **Worksheet A. Maximum Exclusion Allowance (MEA)**

Note: *Use this worksheet to figure your MEA, which is the first component of your MAC.*

1.	Enter your **includible compensation for your most recent year of service**	$ 37,800.00
2.	Percentage limit	20%
3.	Multiply line 1 by line 2	$ 7,560.00
4.	Enter your **years of service** as of the end of the year for which you are figuring your MEA	4.5
5.	Multiply line 3 by line 4	$ 34,020.00
6.	Enter your **amounts previously excludable** (prior years contributions)	$ 9,200.00
7.	Subtract line 6 from line 5. This is your **MEA**	$ 24,820.00

4.

Limit on Annual Additions

The second component of MAC is the limit on annual additions. This is a limit on the total contributions (elective deferrals, nonelective deferrals, and after-tax contributions) that can be made to your account each year. You can figure the limit on annual additions using either of the following.

- The general rule, or
- An alternative limit.

This chapter will discuss figuring the limit on annual additions using the general rule. For information on the alternative limits, see chapter 6.

Under the general rule, the limit on annual additions is the lesser of:

- $30,000 ($35,000 for 2001), or
- 25% of your compensation for your limitation year.

Generally, your limitation year is the calendar year. However, you can elect to change your limitation year to any consecutive 12-month period. To do this, attach a statement to your individual income tax return for the year you make the change.

You can use Worksheet D in chapter 11 to figure your limit on annual additions under the general rule.

CAUTION ***More than one 403(b) account.*** *If you contribute to more than one 403(b) account you must combine the contributions made to all 403(b) accounts made on your behalf by your employer.*

Participation in a qualified plan. *If you participate in a 403(b) plan and a qualified plan, you must combine contributions made to your 403(b) account with contributions to a qualified plan and simplified employee pensions of all corporations, partnerships, and sole proprietorships in which you have more than 50% control.*

Figuring the Limit on Annual Additions

To figure the limit on annual additions under the general rule, you will need to determine what is and is not compensation. Generally, compensation ***includes:***

- Wages, salaries, and fees for personal services with the employer maintaining the plan, even if excludable as foreign earned income,
- Certain taxable accident and health insurance payments,
- Moving expense payments or reimbursements paid by your employer, if such payments are not deductible by you,
- The value of nonqualified stock options granted to you that are includible in your gross income in the year granted,
- Elective deferrals,
- Amounts contributed or deferred (at your election) by your employer under a cafeteria plan or an eligible section 457 plan, and
- The value of qualified transportation fringe benefits.

Generally, compensation ***does not include:***

- Contributions toward a TSA contract (other than elective deferrals),
- Contributions toward a deferred compensation plan if, before applying the limit on employer contributions, the contributions are not taxable,
- Distributions from a deferred compensation plan,
- Proceeds from the disposition of stock acquired under a qualified stock option, and
- Certain other amounts that are excludable from your income, such as group term life insurance premiums that are not taxable.

Note. Compensation for purposes of the limit on annual additions is not the same as includible compensation discussed in chapter 3.

Worksheet E. *Compensation Calculation – Limit on Annual Additions*, in chapter 11, can help you figure your compensation for the limit on annual additions.

Table 4-1. **Worksheet E. Compensation Calculation—Limit on Annual Additions**

Note: *Use this worksheet to figure compensation that will be used to figure your limit on annual additions.*

1.	Enter your wages, salaries, and fees for personal services with the employer who maintains your 403(b) account	$ 35,000
2.	Enter taxable accident and health insurance payments	$ 0
3.	Enter nondeductible moving expense payments or reimbursements paid by your employer	$ 0
4.	Enter the value of nonqualified stock options that are includible in your gross income in the year received	$ 0
5.	Enter elective deferrals (payroll reductions)	$ 2,800
6.	Enter amounts contributed by your employer to a cafeteria plan on your behalf	$ 0
7.	Enter amounts contributed at your election by your employer to an eligible 457 plan on your behalf	$ 0
8.	Enter the value of any qualified transportation fringe benefits	$ 0
9.	Add lines 1 through 8. This is your **compensation** for the current year	$ 37,800

Example

Using the same facts presented in the last *Example* in chapter 3, Jerry is now ready to figure the second component of his MAC, the limit on annual additions.

Figure Jerry's compensation. The first step in determining the limit on annual additions is to figure compensation. Jerry's compensation is shown in Table 4-1.

Figure Jerry's limit on annual additions. After determining compensation, Jerry is now ready to figure the limit on annual additions.

Jerry's limit on annual additions is $9,450 as shown in Table 4-2.

Table 4-2. **Worksheet D. Limit on Annual Additions**

Note: *Use this worksheet to figure your limit on annual additions, which is the second component of your MAC.*

1.	Enter your total **compensation** for the year	$ 37,800
2.	Compensation limit	25%
3.	Multiply line 1 by line 2	$ 9,450
4.	**Maximum** • For 2000, enter $30,000 • For 2001, enter $35,000	$ 35,000
5.	Enter the lesser of line 3 or line 4. This is your **limit on annual additions**	$ 9,450

Figuring Jerry's MAC

Jerry has figured both his MEA and his limit on annual additions. To figure his MAC, Jerry must figure his limit on elective deferrals. This limit is explained in chapter 5.

5.

Limit on Elective Deferrals

The third component of MAC is the limit on elective deferrals. This is a limit on the amount of contributions that can be made to your account through a salary reduction agreement.

A salary reduction agreement is an agreement between you and your employer allowing for a portion of your compensation to be directly invested in a 403(b) account on your behalf. You can enter into more than one salary reduction agreement during a year.

This chapter will discuss:

- The general limit on elective deferrals, and
- The 15-year rule, an increased limit on elective deferrals.

CAUTION

More than one 403(b) account. *If, for any year elective deferrals are contributed to more than one 403(b) account for you (whether or not with the same employer), you must combine all the elective deferrals to determine whether the total is more than the limit for that year.*

403(b) plan and another retirement plan. *If, during the year, contributions in the form of elective deferrals are made to other retirement plans on your behalf, you must combine all of the elective deferrals to determine if they are more than your limit on elective deferrals. The limit on elective deferrals applies to amounts contributed to:*

- *401(k) plans, to the extent excluded from income,*
- *Section 501(c)(18) plans created before June 25, 1959, to the extent excluded from income,*
- *SIMPLE Plans,*
- *Simplified employee pension (SEP) plans, and*
- *All 403(b) plans.*

Table 5-1. **Worksheet F. Limit on Elective Deferrals**

Note: *Use this worksheet to figure your limit on elective deferrals, which is the third component of your MAC.*

1.	**Maximum contribution**	$ 10,500
	NOTE: If you have at least 15 years of service with a qualifying organization, complete lines 2 through 12; if not, enter (0) on line 11 and go to line 12.	
2.	Amount per years of service	$ 5,000
3.	Enter your years of service	
4.	Multiply line 2 by line 3	$
5.	Enter the total of all elective deferrals made by your employer on your behalf for earlier years	$
6.	Subtract line 5 from line 4; if zero or less, enter (0)	$
7.	Maximum increase in limit for long service	$ 15,000
8.	Enter all prior year increases to the general limit for long service	$
9.	Subtract line 8 from line 7	$
10.	**Maximum additional contributions**	$ 3,000
11.	Enter the least of lines 6, 9, or 10. This is the increase in limit for long service	$ 0
12.	Add lines 1 and 11. This is your **limit on elective deferrals**	$ 10,500

General Limit

Under the general limit on elective deferrals, the most that can be contributed to your 403(b) account through payroll reductions for 2000 and 2001 is $10,500. This limit applies without regard to community property laws.

Excess elective deferrals. If the amount contributed is more than the allowable limit, you must include the excess in your gross income for the year contributed. This is explained in chapter 9.

15-Year Rule

If you have at least 15 years of service with a public school system, hospital, home health service agency, health and welfare service agency, church or convention or association of churches (or associated organization), and you are an eligible employee (as described in chapter 1) the limit on elective deferrals to your 403(b) account is the least of:

- $3,000,
- $15,000, reduced by increases to the general limit you were allowed in earlier years because of this rule, or
- $5,000 times the number of your years of service for the organization, minus the total elective deferrals made by your employer on your behalf for earlier years.

If you qualify for the 15-year rule, your limit on elective deferrals for 2000 and 2001 can be as high as $13,500.

Excess elective deferrals. If the amount contributed is more than the allowable limit, you must include the excess in your gross income for the year contributed. This is explained in chapter 9.

Figuring the Limit on Elective Deferrals

Worksheet F in chapter 11 can be used to figure the limit on elective deferrals.

Example

Jerry has figured his MEA and his limit on annual additions. The last component needed before he can determine his MAC is the limit on elective deferrals.

Figure Jerry's limit on elective deferrals. Jerry has been employed with his current employer for less than 15 years. He is not eligible for the special 15-year increase. Therefore, his limit on elective deferrals is $10,500, as shown in Table 5-1.

Figuring Jerry's MAC

Jerry has determined his MEA to be $24,820. His limit on annual additions is $9,450 and his limit on elective deferrals is $10,500. Based on this, the maximum amount that can be contributed to a 403(b) account on Jerry's behalf in 2001 is $9,450, the least of the three limits.

All three components are pulled together in Table 5-2.

Table 5-2. **Worksheet 1. Maximum Amount Contributable (No Alternatives)**

Note: *Use this worksheet to figure your MAC if you are not using an alternative limit on annual additions. If you are using an alternative limit, you must use Worksheet 2, 3, or 4.*

	Part I. Maximum Exclusion Allowance (MEA)		
1.	Enter your **includible compensation for your most recent year of service**	$ 37,800.00	
2.	Percentage limit	20%	
3.	Multiply line 1 by line 2	$ 7,560.00	
4.	Enter your **years of service** as of the end of the year for which you are figuring your MEA	4.5	
5.	Multiply line 3 by line 4	$ 34,020.00	
6.	Enter your **amounts perviously excludable** (prior years contributions)	$ 9,200.00	
7.	Subtract line 6 from line 5. This is your **MEA**		$ 24,820.00
	Part II. Limit on Annual Additions		
8.	Enter your total **compensation** for the year	$ 37,800.00	
9.	Compensation limit	25%	
10.	Multiply line 8 by line 9	$ 9,450.00	
11.	**Maximum** • For 2000, enter $30,000 • For 2001, enter $35,000	$ 35,000.00	
12.	Enter the lesser of line 10 or line 11. This is your **limit on annual additions**		$ 9,450.00
	Caution: If you had only elective deferrals, complete Part III and figure your MAC using line 25. Do not complete line 26. If you had only nonelective contributions, skip Part III and figure MAC using line 26. If you had both elective deferrals and nonelective contributions, stop here and go to Worksheet 5 to figure your MAC.		
	PART III. Limit on Elective Deferrals		
13.	**Maximum contributions**		$ 10,500.00
	NOTE: If you have at least 15 years of service with a qualifying organization, complete lines 14 through 24; if not, enter (0) on line 23 and go to line 24.		
14.	Amount per years of service	$ 5,000.00	
15.	Enter your years of service		
16.	Multiply line 14 by line 15	$	
17.	Enter the total of all elective deferrals made by your employer on your behalf for earlier years	$	
18.	Subtract line 17 from line 16; if zero or less, enter (0).	$	
19.	Maximum increase in limit for long service	$ 15,000.00	
20.	Enter all prior year increases to the general limit for long service	$	
21.	Subtract line 20 from line 19	$	
22.	**Maximum additional contributions**	$ 3,000.00	
23.	Enter the least of lines 18, 21, or 22. This is the increase in the limit for long service		$ 0
24.	Add lines 13 and 23. This is your **limit on elective deferrals.** Complete line 25		$ 10,500.00
	PART IV. Maximum Amount Contributable (MAC)		
25.	Enter the least of lines 7, 12, or 24. This is your **MAC**		$ 9,450.00
26.	Enter the lesser of line 7 or line 12. This is your **MAC**		$

6. Alternative Limits on Annual Additions

Certain employees can choose to increase their MAC by electing an alternative limit on annual additions. There are three alternative limits.

- The year of separation from service limit.
- The any year limit.
- The overall limit.

This chapter will discuss the following topics.

- Who is eligible to use an alternative limit.
- Each of the alternative limits.
- How to elect an alternative limit.

The general limit on annual additions is discussed in chapter 4.

Effect of election. Generally, the election to use either the any year limit or the year of separation limit allows you to exclude from gross income a larger amount of employer contributions than would have been allowed under the general rule that limits employer contributions to 25% of your compensation. If you elect to use the overall limit, you may be able to exclude a larger amount because you can disregard the MEA that would otherwise apply.

Excess contributions. If employer contributions are included in your income for a tax year because they exceed any of these alternative limits for that year, the excess reduces the amount of your MEA for future years, even though the excess has already been included in your income.

Who is Eligible to Use an Alternative Limit

If you are an eligible employee (as described in chapter 1) of one of the following organizations, you can use an alternative limit on annual additions.

- Public schools or public school systems.
- Hospitals.
- Home health service agencies.
- Health and welfare agencies.
- Churches or church-related organizations.

You can elect any one of the three alternative limits, but with certain restrictions. For example, you cannot make more than one election per employer and, once an election is made, it is irrevocable and another alternative limit cannot be selected in a subsequent year. However, you can still choose to apply the general rule in any year.

Additionally, certain employees of churches or church-related organizations might be eligible for other special elections that can be used to figure MAC. See chapter 7.

Year of Separation From Service Limit

If you have not elected to use an alternative limit in a prior year, you can use the year of separation from service limit for the limitation year that ends with or within the year you stop working for the employer who maintains your 403(b) account. If you elect this limit, you use a different method to figure your MEA and your limit on annual additions.

Changes to the MEA. If you elect the year of separation from service limit, you figure your MEA taking into account only your last 10 years of service with the employer who is maintaining your 403(b) account and only amounts excludable during your last 10 years of service with that employer.

If you do not have 10 years with your employer, your years of service is the actual amount of years you do have with your employer. Your amount previously excludable is the total contributions excluded in previous years plus any excess contributions for those years that were more than your limit on annual additions.

Changes to the limit on annual additions. Under the year of separation from service limit, your limit on annual additions is the lesser of:

- $30,000 ($35,000 for 2001), or
- Your MEA.

Figuring MAC using the year of separation from service limit. If you have elected the year of separation from service limit, use Worksheet 2 to figure your MAC.

Any Year Limit

If you have not elected to use another alternative limit in an earlier year, you can use the any year limit on annual additions.

Changes in the limit on annual additions. Your limit on annual additions under the any year limit is the least of:

- $15,000,
- $4,000 plus 25% of your includible compensation for the year in which the limitation year ends, or
- Your MEA for the year in which the limitation year ends.

Figuring MAC using the any year limit. You can use Worksheet 4 to figure your MAC using the any year limit.

Overall Limit

If you have not elected to use another alternative limit in a prior year, you can use the overall limit.

If you elect the overall limit, you must combine employer contributions to your 403(b) plan with all employer contributions to qualified plans to determine if the limit on annual additions has been exceeded. Additionally, in the year that you use the overall limit, you do not figure the MEA.

Figuring MAC using the overall limit. You can use Worksheet 3 to figure your MAC using the overall limit.

How to Elect an Alternative Limit

You make the election to use an alternative limit on annual additions by figuring your tax using that limit. The election is considered made only if use of the alternative limit is needed to support the exclusion from income shown on your income tax return.

Election is irrevocable. If you elect to use an alternative limit, you cannot change the election.

One election allowed. If you elect one of the alternative limits, you cannot elect to have any of the others apply for any future year for any 403(b) contract purchased for you by the employer.

If you elect either the any year limit or the overall limit, that limit is the only alternative limit you can use for later years with the employer.

Example. Janice is employed as a teacher. In 1999, she uses the any year limit. In 2000, and all later years with the same employer, Janice can use only the general rule or the any year limit on annual additions.

Amending a return to take advantage of an alternative limit. You can amend an earlier year's tax return to elect an alternative limit on annual additions.

Generally, you must file an amended return by the later of the following.

- 3 years from the date you filed your original return for the year.
- 2 years from the time you paid your tax for that year.

A return filed early is considered filed on the due date.

If you amend an earlier year's return to elect an alternative limit and use of that limit increases your tax for that year, any additional tax due to the use of the alternative limit is not treated as an underpayment of tax for the penalty for failure to pay estimated income tax.

7. Ministers and Church Employees

Self-employed ministers and church employees are eligible to participate in 403(b) plans. In general, self-employed ministers and church employees follow the rules explained in chapters 2 through 6. Generally, their MAC is the least of the following amounts.

- Maximum exclusion allowance (MEA).
- Limit on annual additions.
- Limit on elective deferrals.

Although, in general, the same rules apply, there are changes in how the MEA and the limit on annual additions is calculated. This chapter will explain those changes.

Who is a church employee? A church employee is anyone who is an employee of a church or a convention or association of churches, including an employee of a tax-exempt organization controlled by or associated with a convention or association of churches.

Maximum Exclusion Allowance (MEA)

For most church employees, the MEA is figured without any changes. However, if your adjusted gross income is less than $17,000 (figured without regard to community property laws), you can exclude from income a minimum exclusion allowance. The minimum exclusion allowance is the lesser of:

- $3,000, or
- Your includible compensation.

Changes to Includible Compensation

Includible compensation is figured differently for foreign missionaries and self-employed ministers.

Self-employed minister. If you are a self-employed minister, you are treated as an employee of a tax-exempt organization that is a qualified employer. Your includible compensation is your net earnings from your ministry minus the contributions made to the retirement plan on your behalf and the deduction for one-half of the self-employment tax.

Foreign missionary. If you are a foreign missionary, your includible compensation includes contributions made by the church during the year to your 403(b) account.

You are a foreign missionary if you are either a lay person or a duly ordained, commissioned, or licensed minister of a church and you meet both of the following requirements.

- You are an employee of a church or convention or association of churches.
- You are performing services for the church outside the United States.

Changes to Years of Service

Generally, only service with the employer who maintains your 403(b) account can be counted when figuring your MEA. If you are a church employee, treat all of your years of service with related church organizations as years of service with one employer.

If, during your church career, you transfer from one organization to another within the church or to an associated organization, treat all this service as service with a single employer. When these organizations make contributions to your 403(b) account, treat them as made by the same employer.

Self-employed minister. If you are a self-employed minister, your years of service include full and part years during which you were self-employed.

Limit on Annual Additions

Generally, as a church employee, you can figure your limit on annual additions under either the general limit or one of the alternative limits.

You can also elect an increased amount for the limit on annual additions. Under this election, you can increase your limit on annual additions to $10,000 a year. Total contributions over your lifetime under this election cannot be more than $40,000. You cannot use this special election in the year you elect the year of separation from service limit.

Excess contributions. Generally, the same rules that apply to other participants regarding contribution limits also apply to you. If you are a church employee who figures your MAC using the minimum exclusion allowance and your contributions are more than your limit on annual additions, your excess contributions are the amount that is more than the minimum exclusion allowance. For more information on excess contributions, see chapter 9.

8. Contributing to Both a 403(b) Plan and a 457 Plan

This chapter will help participants figure the maximum amount that can be contributed in the same year to both a 403(b) account and a 457 account.

CAUTION

403(b) plan contributions only. *If, in the current year, you are eligible to participate in both a 457 plan and a 403(b) plan but you choose to contribute only to the 403(b) plan, the discussions in this chapter do not apply to you. Read chapters 2 through 6 to determine your MAC.*

457 plan contributions only. *If, you are eligible to participate in both a 457 plan and a 403(b) plan, but you choose* **not** *to defer any compensation under the 403(b) plan, you will need to contact your plan administrator to determine your 457 plan limits.*

Definition of 457 plan. A 457 plan is a nonqualified, deferred compensation plan established by state and local governments and tax-exempt employers. In many cases, employers that allow employees to participate in 403(b) plans also offer 457 plans to their employees.

In the year you participate in both a 403(b) plan and a 457 plan, the 457 plan limits apply to the total combined contributions under both plans. This means that the total contributed to both your 403(b) account and your 457 account for the year cannot be more than the 457 plan limits.

Contribution Limits

The maximum amount that can be contributed is determined using either the general limit or the catch-up limit.

General Limit

Under the general limit, the most that can be contributed to your 403(b) account and your 457 account combined is the lesser of the following amounts:

- $8,000 ($8,500 for 2001), or
- One-third of your includible compensation.

This limit is reduced by elective deferrals under a 401(k) plan, SEP plan, or a SIMPLE IRA.

Includible Compensation

Includible compensation under a 457 plan is ***not*** the same as includible compensation under a 403(b) plan.

Generally, includible compensation for a 457 plan is the taxable wages on your Form W-2 from the employer who set up the 457 account on your behalf.

Contributions to a 403(b) plan, 457 plan, 401(k) plan, or a SEP plan, made in the current year, are not part of your includible compensation.

Example. Sylvia is employed by a local school district. In 2000, her estimated compensation was $24,000. Sylvia would like to have $6,000 contributed to her 457 account through a salary reduction agreement. If Sylvia does contribute $6,000, her includible compensation would be $18,000 ($24,000 – $6,000).

Catch-Up Limit

Under the catch-up limit, contributions for the last 3 years prior to your employer's normal retirement age can be more than the general limit.

Normal retirement age. Your employer's normal retirement age is generally set by the plan. If no normal retirement age has been specified in the plan, then your normal retirement age is the latest of:

- Age 65, or
- The latest age specified in your employer's basic pension plan.

Maximum contribution. Under the catch-up limit, the most that can be contributed to your 457 account for a year is the lesser of:

1) $15,000, or
2) The sum of the following two amounts:
   a) The general limit for the year for which you are figuring the catch-up limit, plus
   b) The unused portion of the general limit in prior years.

Add the unused portion of the general limit only for prior years in which all three of the following requirements were met.

1) The year began after 1978.
2) You were eligible to participate in the 457 plan during the year.
3) The general limit applied to contributions made to your account for the year.

403(b) contributions only. If you are eligible to participate in both a 457 plan and a 403(b) plan during a taxable year and you choose to contribute only to a 403(b) plan, contributions to your 403(b) account are taken into consideration in applying the 457 catch-up limit.

If, for each year that you are eligible to participate in both a 457 plan and a 403(b) plan, you elect to defer the maximum amount, through elective deferrals to your 403(b) account, you cannot use the catch-up limit. However, if you do not defer the maximum each year, you may have unused contributions and therefore be eligible to use the catch-up limit.

Example. Although eligible to participate in both a 457 plan and a 403(b) plan, Jessica has only contributed to a 403(b) plan and has deferred the maximum amount each year. Jessica is now within 3 years of her employer's normal retirement age and wants to take advantage of the 457 catch-up limit and defer $15,000. Because Jessica has contributed the maximum amount allowable under the 403(b) plan, she has no unused contributions and cannot use the catch-up limit.

However, if Jessica had deferred nothing under the 457 plan and $2,500 under the 403(b) plan, she would have unused contributions, and would therefore be eligible to use the 457 catch-up limit.

Excess 457 Contributions

If there are excess contributions in the year you contribute to both a 457 plan and a 403(b) plan, the contributions are considered excess 457 contributions.

If you have an excess 457 contribution, contact your plan administrator.

9. Excess Contributions

If your actual contributions are greater than your MAC, you have an excess contribution. Excess contributions can result in income tax, additional taxes, and penalties. The effect of excess contributions depends on the type of excess contribution. This chapter discusses excess contributions to your 403(b) account.

Preventing Excess Contributions

To prevent excess contributions, you should figure your MAC at the beginning of each year using a reasonable estimate of compensation. If, at any time during the year, your employment status or your compensation changes, you should refigure your MAC using a revised estimate of compensation.

How Do I Know If I Have Excess Contributions?

At the end of the year or the beginning of the next year, you should refigure your MAC based on your actual compensation and actual contributions made to your account.

If the actual contributions to your account are greater than your MAC, you have excess contributions.

Worksheet 6. *Calculation of Excess 403(b) Contributions*, can be used to figure the amount, if any, of excess contributions and help you identify the type of excess contribution.

What Happens If I Have Excess Contributions?

Certain excess contributions in a 403(b) account can be corrected. The effect of an excess 403(b) contribution will depend on the type of excess contribution.

Types of excess contributions. If, after checking your actual contributions, you determine that you have an excess, the first thing is to identify the type of excess that you have. Excess contributions to a 403(b) account are categorized as either an:

- Excess deferral, or
- Excess amount.

Excess Amount

An excess amount is a contribution that is more than your MEA or your limit on annual additions.

Amounts in excess of MEA. Amounts that are more than your MEA will be included in your income in the year of the excess contribution.

Amounts in excess of limit on annual additions. In the year that your contributions are more than your limit on annual additions, the excess amount will be included in your income. It will lower your MEA in future years, because it will also be included in your amounts previously excludable.

Amounts in excess of the limit on annual additions that are due to elective deferrals may be distributed if the excess contributions were made for several reasons, including:

- A reasonable error in determining the amount of elective deferrals that could be made under the limit on annual additions, or
- A reasonable error in estimating your compensation.

Excess Deferral

An excess deferral is the amount that is more than your limit on elective deferrals. To determine your limit on elective deferrals see chapter 5.

Your employer's 403(b) plan may contain language permitting it to distribute excess deferrals. If so, it may require that, in order to get a distribution of excess deferrals, you either notify the plan of the amount of excess deferrals or designate a distribution as an excess deferral. The plan may require that the notification or designation be in writing and may require that you certify or otherwise establish that the designated amount is an excess deferral. A plan is not required to permit distribution of excess deferrals.

Correction of excess deferrals during year. If you have excess deferrals for a year, a corrective distribution may be made only if both of the following conditions are satisfied.

- You or your employer designate the distribution as an excess deferral to the extent you have excess deferrals for the year.
- The correcting distribution is made after the date on which the excess deferral was made.

Correction of excess deferrals after the year. If you have excess deferrals for a year, you may receive a corrective distribution of the excess deferral no later than April 15 of the following year. The plan can distribute the excess deferral (and any income allocable to the excess) no later than April 15 of the year following the year the excess deferral was made.

Tax treatment of excess deferrals. If the excess deferral is distributed no later than April 15, it is included in your earned income in the year contributed and the earnings on the excess deferral will be taxed in the year distributed.

Example. William's MAC for 2000 was $10,500. All of William's contributions were made through salary reductions. He contributed $11,500 in 2000, an excess deferral of $1,000. He notified his plan administrator and his employer of the excess contribution on March 15, 2001, and the excess deferral was distributed on April 13, 2001. Because the excess deferral was distributed before April 15, 2001, the excess deferral will be included in his earned income for 2000, and any earnings on the excess is included in his income in the year they are distributed.

If you do not receive a distribution of excess elective deferrals by April 15 of the year following the year it is contributed, it will be included in your earned income in the year contributed and in the year distributed.

Example. Assume that, in the previous example, a distribution of the excess deferral was not made to William by April 15, 2001. Because the distribution was not made timely, the excess deferral will be taxed in 2000 (the year contributed) and again in the year the excess deferral is distributed. The earnings on the distribution will be taxed in the year they are distributed.

Excise Taxes

If your 403(b) account invests in mutual funds, and you exceed either your limit on annual additions or your MEA, you may be subject to a 6% excise tax on the excess contribution. The excise tax does not apply to funds in an annuity account.

You must pay the excise tax each year in which there are excess contributions in your account. Excess contributions can be corrected by contributions less than the applicable limit in later years or by making permissible distributions.

You cannot deduct the excise tax.

Permissible distributions. A permissible distribution is a distribution that can be made when one of the following events occurs.

- You reach age 59½.
- You separate from service.
- You die.
- You become disabled.
- In the case of salary reduction contributions, you encounter financial hardships.

Reporting requirement. You must file Form 5330 if there has been an excess contribution to a custodial account and that excess has not been corrected.

10. Distributions and Rollovers

Generally, a distribution cannot be made from a 403(b) account until the employee:

- Reaches age 59½,
- Separates from service,
- Dies,
- Becomes disabled, or
- In the case of salary reduction contributions, encounters financial hardship.

In most cases, the payments you receive or that are made available to you under your 403(b) account are taxable in full as ordinary income. In general, the same tax rules apply to distributions from 403(b) plans that apply to distributions from other retirement plans. These rules are explained in Publication 575. Publication 575 also discusses the additional tax on early distributions from retirement plans.

Minimum Required Distributions

You must receive all, or at least a certain minimum, of your interest accruing after 1986 in the 403(b) plan by April 1 of the calendar year following the later of the calendar year in which you become age 70½ or the calendar year in which you retire.

Check with your employer, plan administrator, or provider to find out whether this rule also applies to pre-1987 accruals. If not, a minimum amount of these accruals must begin to be distributed by the later of the end of the calendar year in which you reach age 75 or April 1 of the calendar year following retirement, whichever is later. For each year thereafter, the minimum distribution must be made by the last day of the year. If you do not receive the required minimum distribution, you are subject to a nondeductible 50% excise tax on the difference between the required minimum distribution and the amount actually distributed.

For more information on minimum distribution requirements and the additional tax that applies if too little is distributed each year, see Publication 575.

No Special 10-Year Tax Option

A distribution from a 403(b) plan does not qualify as a lump-sum distribution. This means you cannot use the special 10-year tax option to calculate the taxable portion of a 403(b) distribution. For more information, see Publication 575.

Transfer of Interest in 403(b) Contract

If you transfer all or part of your interest from a 403(b) account to another 403(b) account, the transfer is tax free. However, this treatment applies only if the transferred interest is subject to the same or stricter distribution restrictions. This rule applies regardless of whether you are a current employee, a former employee, or a beneficiary of a former employee.

Transfers that do not satisfy this rule are plan distributions and are generally taxable as ordinary income.

Tax-free transfers for certain cash distributions. A tax-free transfer may also apply to a cash distribution of your 403(b) account from an insurance company that is subject to a rehabilitation, conservatorship, insolvency, or similar state proceeding. To receive tax-free treatment, you must do all of the following.

1) Reinvest the cash in an annuity contract or account issued by another insurance company.
2) Withdraw all the cash to which you are entitled in full settlement of your contract rights or the maximum permitted by the state.
3) Reinvest the cash distribution into another annuity contract or account issued by another insurance company or single custodial account not later than 60 days after you receive the cash distribution.
4) Assign all future distribution rights to the new contract or account for investment in that contract or account if you received an amount that is less than what you are entitled to because of state restrictions.
5) Reinvest in an annuity contract or account subject to the same or stricter distribution restrictions as the original contract.

In addition to the preceding requirements, you must provide the new insurer with a written statement containing the following information:

1) The gross amount of cash distributed under the old contract,
2) The amount of cash reinvested in the new contract, and
3) Your investment in the old contract on the date you receive your first cash distribution.

Also, you must attach the following items to your timely filed income tax return in the year you receive the first distribution of cash.

1) A copy of the statement you gave the new insurer.
2) A statement that includes:
   a) The words ***ELECTION UNDER REV. PROC. 92-44***,
   b) The name of the company that issued the new contract, and
   c) The new policy number.

Tax-Free Rollovers

You can generally roll over tax free all or any part of a distribution from a 403(b) plan to a traditional IRA or another 403(b) plan. The most you can roll over is the amount that, except for the rollover, would be taxable. The rollover must be completed by the 60th day following the day on which you receive the distribution.

Nonqualifying distributions. Under these rules, you cannot roll over:

1) Minimum distributions (generally required to begin at age 70½),
2) Substantially equal payments over your life or life expectancy,
3) Substantially equal payments over the joint lives or life expectancies of you and your beneficiary,
4) Substantially equal payments for a period of 10 years or more, or
5) Hardship distributions.

Direct rollovers for 403(b) plan distributions. You have the option of having your 403(b) plan make the rollover directly to the IRA or new plan. Before you receive a distribution, your plan will give you information on this. It is generally to your advantage to choose this option because your plan will not withhold tax on the distribution if you choose it.

Withholding. If you ***receive*** a distribution that qualifies to be rolled over, the payer must withhold 20% of it for taxes (even if you plan to roll the distribution over). You cannot choose to have no withholding unless you elect the direct rollover option.

Distribution received by you. If you receive a distribution that qualifies to be rolled over, you can roll over all or any part of the distribution. Generally, you will receive only 80% of the distribution because 20% must be withheld. If you roll over only the 80% you receive, you must pay tax on the 20% you did not roll over. You can replace the 20% that was withheld with other money within the 60-day period to make a 100% rollover.

Voluntary deductible contributions. For tax years 1982 through 1986, employees could make deductible contributions to a 403(b) plan under the individual retirement arrangement (IRA) rules instead of deducting contributions to a traditional IRA.

If you made voluntary deductible contributions to a 403(b) plan under these traditional IRA rules, the distribution of all or part of the accumulated deductible contributions may be rolled over assuming it otherwise qualifies as a distribution you can roll over. Accumulated deductible contributions are the deductible contributions plus income and gain allocable to the contributions, minus expenses and losses allocable to the contributions, and minus distributions from the contributions, income, or gain.

Excess employer contributions. The portion of a distribution from a 403(b) plan transferred to a traditional IRA that was previously included in income as excess employer contributions (discussed earlier) is not an eligible rollover distribution.

Its transfer does not affect the rollover treatment of the eligible portion of the transferred amounts. However, the ineligible portion is subject to the traditional IRA contribution limits and may create an excess IRA contribution subject to a 6% excise tax (see chapter 1 of Publication 590).

Qualified Domestic Relations Order. You may be able to roll over tax free all or any part of an eligible rollover distribution from a 403(b) plan that you receive under a qualified domestic relations order (QDRO). If you receive the interest in the 403(b) plan as an employee's spouse or former spouse under a QDRO, all of the rollover rules apply to you as if you were the employee. You can roll over your interest in the plan to a traditional IRA or another 403(b) plan. For more information on the treatment of an interest received under a QDRO, see Publication 575.

Spouses of deceased employees. If you are the spouse of a deceased employee, you can roll over the qualifying distribution attributable to the employee. You can make the rollover only to a traditional IRA, not to another 403(b) plan or a qualified plan. You cannot roll it over to a Roth IRA.

Second rollover. If you roll over a qualifying distribution to a traditional IRA, you can, if certain conditions are satisfied, later roll the distribution into another 403(b) plan. For more information, see *IRA as a holding account (conduit IRA) for rollovers to other eligible plans*, in Publication 590.

Frozen deposits. The 60-day period usually allowed for completing a rollover is extended for any time that the amount distributed is a frozen deposit in a financial institution. The 60-day period cannot end earlier than 10 days after the deposit ceases to be a frozen deposit.

A frozen deposit is any deposit that on any day during the 60-day period cannot be withdrawn because:

1) The financial institution is bankrupt or insolvent, or

2) The state where the institution is located has placed limits on withdrawals because one or more banks in the state are (or are about to be) bankrupt or insolvent.

Gift Tax

If, by choosing or not choosing an election, or option, you provide an annuity for your beneficiary at or after your death, you may have made a taxable gift equal to the value of the annuity.

Joint and survivor annuity. If the gift is an interest in a joint and survivor annuity where only you and your spouse have the right to receive payments, the gift will generally be treated as qualifying for the unlimited marital deduction.

More information. For information on the gift tax, see Publication 950, *Introduction to Estate and Gift Taxes.*

11. Worksheets

Chapter 3 introduced you to the term maximum amount contributable (MAC). Generally, MAC is the lesser of your:

- Maximum exclusion allowance (chapter 3),
- Limit on annual additions (chapter 4 for the general rule or chapter 6 for alternative limits), or
- Limit on elective deferrals (chapter 5).

Worksheets 1 through 4 in this chapter pull all three of these components together to help you figure your MAC.

Figuring MAC

After completing the worksheets, you should maintain them with your 403(b) records for that year. Do not attach them to your tax return. At the end of the year or the beginning of the next year, you should compare your estimated compensation figures with your actual figures.

If your compensation is the same as, or more than, the projected amounts and the calculations are correct, then you should simply file these worksheets with your other tax records for the year.

If your compensation was lower than your estimated figures, you will need to check the amount contributed during the year to determine if contributions are more than your MAC.

When Should I Figure MAC?

At the beginning of each year, you should figure your MAC using a conservative estimate of your compensation. Should your income change during the year, you should refigure your MAC based on a revised conservative estimate. By doing this, you will be able to determine if contributions to your 403(b) account should be increased or decreased for the year.

Figuring MAC for the Current Year

If you are figuring your MAC for the current year, you should use a conservative estimate of your compensation. Use the gross income before salary reductions to determine both your includible compensation (for purposes of figuring your MEA) and your total compensation (for purposes of figuring your limit on annual additions).

If you have chosen an alternative limit you should figure your MAC using one of the three alternative limits, you should figure your MAC using both the selected alternative limit and the general limit.

CAUTION *Before selecting an alternative limit, read Chapter 7,* Alternative Limits.

Checking the Previous Year's Contributions

At the beginning of the following year, you should refigure your MAC based on your actual earned income.

At the end of the current year or the beginning of the next year, you should check your contributions to be sure you did not exceed your MAC. This means refiguring your limit based on your actual compensation figures for the year. This will allow you to determine if the amount contributed is more than the allowable amounts, and avoid additional taxes.

Available Worksheets

The following worksheets have been provided to help you figure components of your MAC.

- Worksheet A. Maximum Exclusion Allowance (MEA).
- Worksheet B. Cost of Life Insurance.
- Worksheet C. Includible Compensation for Your Most Recent Year of Service.
- Worksheet D. Limit on Annual Additions.
- Worksheet E. Compensation Calculation — Limit on Annual Additions.
- Worksheet F. Limit on Elective Deferrals.

Worksheets 1 through 5 will help you figure MAC, and Worksheet 6 will help your determine if you have excess contributions.

- Worksheet 1. Maximum Amount Contributable (No Alternatives).
- Worksheet 2. Year of Separation From Service Limit.
- Worksheet 3. Overall Limit.
- Worksheet 4. Any Year Limit.
- Worksheet 5. Limit on Nonelective Contributions.
- Worksheet 6. Calculation of Excess 403(b) Contributions.

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Worksheet A. **Maximum Exclusion Allowance (MEA)**

Note: *Use this worksheet to figure your MEA, which is the first component of your MAC.*

1.	Enter your **includible compensation for your most recent year of service**	$ ______
2.	Percentage limit	20%
3.	Multiply line 1 by line 2	$ ______
4.	Enter your **years of service** as of the end of the year for which you are figuring your MEA	______
5.	Multiply line 3 by line 4	$ ______
6.	Enter your **amounts previously excludable** (prior years contributions)	$ ______
7.	Subtract line 6 from line 5. This is your **MEA**	$ ______

Worksheet B. **Cost of Life Insurance**

Note: *Use this worksheet to figure the cost of incidental life insurance included in your annuity contract. This amount will be used to figure includible compensation for your most recent year of service.*

1.	Enter the value of the contract (amount payable upon your death)	$ ______
2.	Enter the cash value in the contract at the end of the year	$ ______
3.	Subtract line 2 from line 1. This is the **value of your current life insurance protection**	$ ______
4.	Enter your age on your birthday nearest the beginning of the policy year	______
5.	Enter the 1-year term premium for $1,000 of life insurance based on your age. (Figure 3-1)	$ ______
6.	Divide line 3 by **$1,000**	$ ______
7.	Multiply line 6 by line 5. This is the **cost of your incidental life insurance**	$ ______

Worksheet C. **Includible Compensation for Your Most Recent Year of Service***

Note: *Use this worksheet to figure includible compensation for your most recent year of service. This amount will be used to figure your MEA.*

1.	Enter your includible wages from the employer maintaining your 403(b) account for your most recent year of service	$ ______
2.	Enter elective deferrals for your most recent year of service	$ ______
3.	Enter amounts contributed or deferred by your employer under a cafeteria plan for your most recent year of service	$ ______
4.	Enter amounts contributed or deferred by your employer to your 457 account for your most recent year of service	$ ______
5.	Enter the value of qualified transportation fringe benefits you received from your employer	$ ______
6.	Enter your foreign earned income exclusion for your most recent year of service	$ ______
7.	Add lines 1, 2, 3, 4, 5, and 6	$ ______
8.	Enter the cost of incidental life insurance that is part of your annuity contract for your most recent year of service	$ ______
9.	Enter compensation that was **both:**	
	• Earned during your most recent year of service, and	
	• Earned while your employer was not qualified to maintain a 403(b) plan	$ ______
10.	Enter contributions that are more than your MEA	$ ______
11.	Add lines 8, 9, and 10	$ ______
12.	Subtract line 11 from line 7. This is your **includible compensation for your most recent year of service**	$ ______

**Use estimated amounts if figuring includible compensation before the end of the year.*

Worksheet D. **Limit on Annual Additions**

Note: *Use this worksheet to figure your limit on annual additions, which is the second component of your MAC.*

1.	Enter your total **compensation** for the year	$ ________
2.	Compensation limit .	25%
3.	Multiply line 1 by line 2	$ ________
4.	**Maximum**	$ ________
	• For 2000, enter $30,000 • For 2001, enter $35,000	
5.	Enter the lesser of line 3 or line 4. This is your **limit on annual additions**	$ ________

Worksheet E. **Compensation Calculation—Limit on Annual Additions**

Note: *Use this worksheet to figure compensation that will be used to figure your limit on annual additions.*

1.	Enter your wages, salaries, and fees for personal services with the employer who maintains your 403(b) account	$ ________
2.	Enter taxable accident and health insurance payments	$ ________
3.	Enter nondeductible moving expense payments or reimbursements paid by your employer.	$ ________
4.	Enter the value of nonqualified stock options that are includible in your gross income in the year received.	$ ________
5.	Enter elective deferrals (payroll reductions)	$ ________
6.	Enter amounts contributed by your employer to a cafeteria plan on your behalf	$ ________
7.	Enter amounts contributed at your election by your employer to an eligible 457 plan on your behalf.	$ ________
8.	Enter the value of any qualified transportation fringe benefits . . .	$ ________
9.	Add lines 1 through 8. This is your **compensation** for the current year.	$ ________

Worksheet F. **Limit on Elective Deferrals**

Note: *Use this worksheet to figure your limit on elective deferrals, which is the third component of your MAC.*

1.	**Maximum contribution**	$ 10,500
	Note: *If you have at least 15 years of service with a qualifying organization, complete lines 2 through 12; if not, enter (0) on line 11 and go to line 12.*	
2.	Amount per years of service	$ 5,000
3.	Enter your years of service	________
4.	Multiply line 2 by line 3	________
5.	Enter the total of all elective deferrals made by your employer on your behalf for earlier years.	$ ________
6.	Subtract line 5 from line 4; if zero or less, enter (0)	$ ________
7.	Maximum increase in limit for long service.	$ 15,000
8.	Enter all prior year increases to the general limit for long service . . .	$ ________
9.	Subtract line 8 from line 7.	$ ________
10.	**Maximum additional contributions**	$ 3,000
11.	Enter the least of lines 6, 9, or 10. This is the increase in limit for long service	$ ________
12.	Add lines 1 and 11. This is your **limit on elective deferrals**	$ ________

Worksheet 1. **Maximum Amount Contributable (No Alternatives)**

Note: *Use this worksheet to figure your MAC if you are not using an alternative limit on annual additions. If you are using an alternative limit, you must use Worksheet 2, 3, or 4.*

	Part I. Maximum Exclusion Allowance (MEA)		
1.	Enter your **includible compensation for your most recent year of service**	$	
2.	Percentage limit	20%	
3.	Multiply line 1 by line 2	$	
4.	Enter your **years of service** as of the end of the year for which you are figuring your MEA		
5.	Multiply line 3 by line 4	$	
6.	Enter your **amounts perviously excludable** (prior years contributions)	$	
7.	Subtract line 6 from line 5. This is your **MEA**		$
	Part II. Limit on Annual Additions		
8.	Enter your total **compensation** for the year	$	
9.	Compensation limit	25%	
10.	Multiply line 8 by line 9.	$	
11.	**Maximum** • For 2000, enter $30,000 • For 2001, enter $35,000	$	
12.	Enter the lesser of line 10 or line 11. This is your **limit on annual additions**		$
	Caution: If you had only elective deferrals, complete Part III and figure your MAC using line 25. Do not complete line 26. If you had only nonelective contributions, skip Part III and figure MAC using line 26. If you had both elective deferrals and nonelective contributions, stop here and go to Worksheet 5 to figure your MAC.		
	PART III. Limit on Elective Deferrals		
13.	**Maximum contributions**		$ 10,500
	NOTE: If you have at least 15 years of service with a qualifying organization, complete lines 14 through 23; if not, enter (0) on line 23 and go to line 24.		
14.	Amount per years of service	$ 5,000	
15.	Enter your years of service		
16.	Multiply line 14 by line 15	$	
17.	Enter the total of all elective deferrals made by your employer on your behalf for earlier years	$	
18.	Subtract line 17 from line 16; if zero or less, enter (0).	$	
19.	Maximum increase in limit for long service	$ 15,000	
20.	Enter all prior year increases to the general limit for long service	$	
21.	Subtract line 20 from line 19	$	
22.	**Maximum additional contributions**.	$ 3,000	
23.	Enter the least of lines 18, 21, or 22. This is the increase in the limit for long service		$
24.	Add lines 13 and 23. This is your **limit on elective deferrals.** Complete line 25		$
	PART IV. Maximum Amount Contributable (MAC)		
25.	Enter the least of lines 7, 12, or 24. This is your **MAC**		$
26.	Enter the lesser of line 7 or line 12. This is your **MAC**		$

Worksheet 2. **Year of Separation From Service Limit**

Note: *Use this worksheet to figure your MAC if you are using the year of separation from service limit.*

	Part I. Maximum Exclusion Allowance (MEA)		
1.	Enter your **includible compensation for your most recent year of service**	$	
2.	Percentage limit	20%	
3.	Multiply line 1 by line 2	$	
4.	Enter your **years of service** (limited to 10 years) as of the end of the year for which you are figuring your MEA		
5.	Multiply line 3 by line 4	$	
6.	Enter your **amounts previously excludable** during the last 10 years (including prior years excess contributions)	$	
7.	Subtract line 6 from line 5. This is your **MEA**		$
	Part II. Limit on Annual Additions		
8.	**Maximum**		$
	• For 2000, enter $30,000		
	• For 2001, enter $35,000		
	Caution: If you had only elective deferrals, complete Part III and figure your MAC using line 21. Do not complete line 22. If you had only nonelective contributions, skip Part III and figure MAC using line 22. Do not complete line 21. If you had both elective deferrals and nonelective contributions, stop here and go to Worksheet 5 to figure your MAC.		
	Part III. Limit on Elective Deferrals		
9.	**Maximum contribution**		$ 10,500
	NOTE: If you have at least 15 years of service with a qualifying organization, complete lines 10 through 20; if not, enter (0) on line 19 and go to line 20.		
10.	Amount per years of service	$ 5,000	
11.	Enter your years of service		
12.	Multiply line 10 by line 11	$	
13.	Enter the total of all elective deferrals made by your employer on your behalf for earlier years	$	
14.	Subtract line 13 from line 12; if zero or less, enter (0)	$	
15.	Maximum increase in limit for long service	$ 15,000	
16.	Enter all prior year increases in the limit for long service	$	
17.	Subtract line 16 from line 15	$	
18.	**Maximum additional contributions**	$ 3,000	
19.	Enter the least of lines 14, 17, or 18. This is the increase in limit for long service		$
20.	Add lines 9 and 19. This is your **limit on elective deferrals.** Complete line 21		$
	Part IV. Maximum Amount Contributable (MAC)		
21.	Enter the least of lines 7, 8, or 20. This is your **MAC**		$
22.	Enter the lesser of line 7 or line 8. This is your **MAC**		$

Worksheet 3. **Overall Limit**

Note: *Use this worksheet to figure your MAC if you are using the overall limit.*

	Part I. Limit on Annual Additions		
1.	Enter your total **compensation** for the year	$	
2.	Compensation limit	25%	
3.	Multiply line 1 by line 2	$	
4.	**Maximum** • For 2000, enter $30,000 • For 2001, enter $35,000		$
5.	Enter the lesser of line 3 or line 4. This is your **limit on annual additions**		$
	Caution: If you had only elective deferrals, complete Part II and figure your MAC using line 18. If you had only nonelective contributions, skip Part II and enter the amount from line 5 on line 19. If you had both elective deferrals and nonelective contributions, stop here and go to Worksheet 5 to figure your MAC.		
	Part II. Limit on Elective Deferrals		
6.	**Maximum contribution**		$ 10,500
	NOTE: If you have at least 15 years of service with a qualifying organization, complete lines 7 through 17; if not, enter (0) on line 16 and go to line 17.		
7.	Amount per years of service	$ 5,000	
8.	Enter your years of service		
9.	Multiply line 7 by line 8	$	
10.	Enter the total of all elective deferrals made by your employer on your behalf for earlier years	$	
11.	Subtract line 10 from line 9; if zero or less, enter (0)	$	
12.	Maximum increase in limit for long service	$ 15,000	
13.	Enter all prior year increases to the general limit for long service	$	
14.	Subtract line 13 from line 12	$	
15.	**Maximum additional contributions**	$ 3,000	
16.	Enter the least of lines 11, 14, or 15. This is the increase in limit for long service		$
17.	Add lines 6 and 16. This is your **limit on elective deferrals.** Complete line 18		$
	Part III. Maximum Amount Contributable (MAC)		
18.	Enter the lesser of lines 5 or 17. This is your **MAC**		$
19.	Enter the amount from line 5. This is your **MAC**		$

Worksheet 4. **Any Year Limit**

Note: *Use this worksheet to figure your MAC if you are using the any year limit.*

	Part I. Maximum Exclusion Allowance (MEA)		
1.	Enter your **includible compensation for your most recent year of service**	$	
2.	Percentage limit	20%	
3.	Multiply line 1 by 2	$	
4.	Enter your **years of service** as of the end of the year for which you are figuring your MEA		
5.	Multiply line 3 by line 4	$	
6.	Enter your **amounts previously exludable** (prior years contributions)	$	
7.	Subtract line 6 from line 5. This is your **MEA**		$
	Part II. Limit on Annual Additions		
8.	Enter your total **compensation** for the year	$	
9.	**Compensation limit**	25%	
10.	Multiply line 8 by line 9.	$	
11.	**Additional amount**	$ 4,000	
12.	Add lines 10 and 11. This is a tentative limit	$	
13.	**Maximum**	$ 15,000	
14.	Enter the least of lines 7, 12, or 13. This is your **limit on annual additions**		$
	Caution: If you had only elective deferrals, complete Part III and figure your MAC using line 27. Do not complete line 28. If you had only nonelective contributions, skip Part III and enter the amount from line 14 on line 28. Do not complete line 27. If you had both elective deferrals and nonelective contributions, stop here and go to Worksheet 5 to figure your MAC.		
	Part III. Limit on Elective Deferrals		
15.	**Maximum contribution**		$ 10,500
	NOTE: If you have at least 15 years of service with a qualifying organization, complete lines 16 through 26; if not, enter (0) on line 25 and go to line 26.		
16.	Amount per years of service	$ 5,000	
17.	Enter your years of service		
18.	Multiply line 16 by line 17	$	
19.	Enter the total of all elective deferrals made by your employer on your behalf for earlier years	$	
20.	Subtract line 19 from line 18; if zero or less, enter (0).	$	
21.	Maximum increase in limit for long service	$ 15,000	
22.	Enter all prior year increases to the general limit for long service	$	
23.	Subtract line 22 from line 21	$	
24.	**Maximum additional contributions**	$ 3,000	
25.	Enter the least of lines 20, 23 or 24. This is your increase in limit for long service		$
26.	Add lines 15 and 25. This is your **limit on elective deferrals**. Complete line 27		$
	Part IV. Maximum Amount Contributable (MAC)		
27.	Enter the lesser of lines 14 or 26. This is your **MAC**		$
28.	Enter the amount from line 14. This is your **MAC**		$

Worksheet 5. **Limit on Nonelective Contributions**

Note: *Use this worksheet to figure your limit on nonelective contributions for years in which you have both nonelective contributions and elective deferrals. Before completing this worksheet, unless you are using the overall limit, figure your MEA and your limit on annual additions using Worksheet 1, 2, or 4. If you are using the overall limit, figure your limit on annual additions using Worksheet 3 before completing this worksheet.*

1. Enter your **MEA.** If you used:
- Worksheet 1, 2, or 4—This is the amount from line 7 of the worksheet.
- Worksheet 3—Leave this line blank and go on to line 2. **$** ________

2. Enter your **limit on annual additions.** If you used:
- Worksheet 1—This is the amount from line 12 of that worksheet.
- Worksheet 2—This is the amount from line 8 of that worksheet.
- Worksheet 3—This is the amount from line 5 of that worksheet.
- Worksheet 4—This is the amount from line 14 of that worksheet. **$** ________

3. If you used Worksheet 1, 2, or 4, enter the lesser of line 1 or line 2 of this worksheet. If you used Worksheet 3, enter the amount from line 2 of this worksheet . . . **$** ________

4. Enter the amount of your actual **elective deferrals** (defined in chapter 1) for the year . . . . **$** ________

5. Subtract line 4 from line 3. If zero (0) or less, enter zero (0). This is the maximum amount of **nonelective contributions** that can be contributed to a 403(b) account on your behalf for the year. . . . . **$** ________

Worksheet 6. **Calculation of Excess 403(b) Contributions**

Note: *Use this worksheet to figure excess contributions to your 403(b) account.*

Part I. Excess Contributions

1. Enter the actual amount contributed to your 403(b) account for the year . . . $ ________

2. Enter your MAC for the year (from Worksheet 1, 2, 3, or 4) . . . . $ ________

3. Subtract line 2 from line 1. If zero or less, enter zero (0). This amount is your excess contribution. If you entered zero, you do not have excess contributions, *stop here* . . . . $ ________

Part II. Excess Deferrals

4. Enter the actual amount of elective deferrals contributed to your 403(b) account for the year . . . . $ ________

5. Enter the total amount of elective deferrals contributed, for the year, to a 401(k) plan, a section 501(c)(18) plan (created before June 25, 1959), a SIMPLE plan, and a SEP plan, on your behalf . . . . $ ________

6. Add line 4 and line 5 . . . . $ ________

7. Enter your limit on elective deferrals (from Worksheet F) . . . . $ ________

8. Subtract line 7 from line 6. If zero or less, enter zero (0). . . . . $ ________

- If you entered zero, you do not have an excess deferral. Continue to line 9.
- If you entered more than zero, this is your excess deferral. See *Excess Deferral* in chapter 9, for actions you should take and continue to line 9.

Part III. Excess Amount

9. Enter the nonelective contributions made to your account . . . . $ ________

10. Enter your after-tax contributions. . . . . $ ________

11. Enter your elective deferrals . . . . $ ________

12. Enter amounts contributed, on your behalf, to a qualified plan or a SEP plan of all corporations, partnerships, and sole proprietorships in which you had more than 50% control, for the year . . . . $ ________

13. Add lines 9, 10, 11, and 12 . . . . $ ________

14. Enter your limit on annual additions (from Worksheet D) . . . . $ ________

15. Subtract line 14 from line 13. If zero or less, enter zero (0) . . . . $ ________

- If you entered zero, you do not have excess annual additions. Continue to line 16.
- If you entered more than zero, this is your excess annual additions. See *Amount in excess of limit on annual additions* in chapter 9 for actions you should take and continue to line 16.

16. Add lines 9, 10, and 11. . . . . $ ________

17. Enter your MEA (from Worksheet A) . . . . $ ________

18. Subtract line 17 from line 16. If zero or less, enter zero (0) . . . . $ ________

- If you entered zero, you do not have an excess MEA.
- If you entered more than zero, this is your excess MEA. See *Amount in excess of MEA* in chapter 9 for actions you should take.

12. How To Get Tax Help

You can get help with unresolved tax issues, order free publications and forms, ask tax questions, and get more information from the IRS in several ways. By selecting the method that is best for you, you will have quick and easy access to tax help.

Contacting your Taxpayer Advocate. If you have attempted to deal with an IRS problem unsuccessfully, you should contact your Taxpayer Advocate.

The Taxpayer Advocate represents your interests and concerns within the IRS by protecting your rights and resolving problems that have not been fixed through normal channels. While Taxpayer Advocates cannot change the tax law or make a technical tax decision, they can clear up problems that resulted from previous contacts and ensure that your case is given a complete and impartial review.

To contact your Taxpayer Advocate:

- Call the Taxpayer Advocate at **1–877–777–4778.**
- Call the IRS at **1–800–829–1040.**
- Call, write, or fax the Taxpayer Advocate office in your area.
- Call **1–800–829–4059** if you are a TTY/TDD user.

For more information, see Publication 1546, *The Taxpayer Advocate Service of the IRS.*

Free tax services. To find out what services are available, get Publication 910, *Guide to Free Tax Services.* It contains a list of free tax publications and an index of tax topics. It also describes other free tax information services, including tax education and assistance programs and a list of TeleTax topics.

Personal computer. With your personal computer and modem, you can access the IRS on the Internet at **www.irs.gov**. While visiting our web site, you can select:

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- *Fill-in Forms* (located under *Forms & Pubs)* to enter information while the form is displayed and then print the completed form.
- *Tax Info For You* to view Internal Revenue Bulletins published in the last few years.
- *Tax Regs in English* to search regulations and the Internal Revenue Code (under *United States Code (USC)).*
- *Digital Dispatch* and *IRS Local News Net* (both located under *Tax Info For Business)* to receive our electronic newsletters on hot tax issues and news.
- *Small Business Corner* (located under *Tax Info For Business)* to get information on starting and operating a small business.

You can also reach us with your computer using File Transfer Protocol at **ftp.irs.gov**.

TaxFax Service. Using the phone attached to your fax machine, you can receive forms and instructions by calling **703–368–9694.** Follow the directions from the prompts. When you order forms, enter the catalog number for the form you need. The items you request will be faxed to you.

Phone. Many services are available by phone.

- *Ordering forms, instructions, and publications.* Call **1–800–829–3676** to order current and prior year forms, instructions, and publications.
- *Asking tax questions.* Call the IRS with your tax questions at **1–800–829–1040.**
- *TTY/TDD equipment.* If you have access to TTY/TDD equipment, call **1–800–829–4059** to ask tax questions or to order forms and publications.
- *TeleTax topics.* Call **1–800–829–4477** to listen to pre-recorded messages covering various tax topics.

Evaluating the quality of our telephone services. To ensure that IRS representatives give accurate, courteous, and professional answers, we evaluate the quality of our telephone services in several ways.

- A second IRS representative sometimes monitors live telephone calls. That person only evaluates the IRS assistor and does not keep a record of any taxpayer's name or tax identification number.
- We sometimes record telephone calls to evaluate IRS assistors objectively. We hold these recordings no longer than one week and use them only to measure the quality of assistance.
- We value our customers' opinions. Throughout this year, we will be surveying our customers for their opinions on our service.

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- An extensive collection of products available to print from a CD-ROM or photocopy from reproducible proofs.
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IRS Publication 3207, *The Business Resource Guide,* is an interactive CD-ROM that contains information important to small businesses. It is available in mid-February. You can get one free copy by calling **1–800–829–3676.**

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