

2002 for eligible governmental plans provide participants affected by these types of events the ability to retain their retirement savings in a funded, tax-deferred savings vehicle by rollover to an IRA, qualified plan, or section 403(b) contract. The regulations provide a outline for the different plan termination and plan-to-plan transfer alternatives available to sponsors of eligible governmental plans in these situations.

a. Plan Terminations

The regulations allow a plan to have provisions permitting plan termination whereupon amounts can be distributed without violating the distribution requirements of section 457. Under the regulations, an eligible plan is terminated only if all amounts deferred under the plan are paid to participants as soon as administratively practicable. If the amounts deferred under the plan are not distributed, the plan is treated as a frozen plan and must continue to comply with all of the applicable statutory requirements necessary for plan eligibility.

b. Plan-to-Plan Transfers Among Eligible Governmental Plans and Purchase of Permissive Service Credit by Plan-to-Plan Transfer

The proposed regulations would have allowed plan-to-plan transfers between eligible governmental plans under new circumstances, as well as the purchase of permissive service credits by transfer from an eligible governmental plan to a governmental defined benefit plan, but only if the transfers were made by plans within the same State. Commentators objected to the requirement under the new transfer rules that the transfers be to plans within the same State.

Upon consideration of the comments received, the regulations allow transfers among eligible governmental plans in three situations. In each case, the transferor plan must provide for transfers, the receiving plan must provide for the receipt of transfers, and the participant or beneficiary whose amounts deferred are being transferred must be entitled to an amount deferred immediately after the transfer that is at least equal to the amount deferred with respect to that participant or beneficiary immediately before the transfer. Transfers are permitted among eligible governmental plans in the following three cases:

- A person-by-person transfer is permitted for any beneficiary and for any participant who has had a severance from employment with the transferring employer and is performing services for the entity maintaining the receiving

plan (whether or not the other plan is within the same State).

- No severance from employment is required if the entire plan's assets for all participants and beneficiaries are transferred to another eligible governmental plan within the same State.

- No severance from employment is required for a transfer from one eligible governmental plan of an employer to another eligible governmental plan of the same employer.

The final regulations also allow a plan-to-plan transfer from an eligible governmental plan to a governmental defined benefit plan for permissive service credit, without regard to whether the defined benefit plan is maintained by a governmental entity that is in the same State. In addition, language that was in an example which implied that section 415(n) (which addresses the application of maximum benefit limitations with respect to certain contributions) might apply to such a transfer has been eliminated because Treasury and the IRS have concluded that section 415(n) does not apply to such a transfer in any case in which the actuarial value of the benefit increase that results from the transfer does not exceed the amount transferred.

c. Plan-to-Plan Transfers Among Eligible Plans of Tax-Exempt Entities

The regulations retain the rule from the 1982 regulations allowing a plan-to-plan transfer after a participant has had a severance from employment.

d. Rollovers

The proposed regulations specified the treatment of amounts rolled into or out of an eligible governmental plan and stated that amounts rolled into the plan are treated as amounts deferred under the plan for purposes of the regulations. Some commentators requested that consideration be given to allowing eligible governmental plans to have the same flexibility that they claimed was permitted for qualified plans with respect to the timing of distributions of rolled-in assets. Specifically, these commentators requested the ability for an eligible governmental plan to allow a participant to receive a distribution of rolled-in assets even though the participant may not yet be eligible for a distribution of other assets held under the plan.

Commentators pointed out that, since section 402(c)(10) allows an eligible governmental plan to accept a rollover contribution only if the rolled-in assets from other plan types are separately accounted for (in order to apply the section 72(t) early withdrawal income

tax for distributions from these assets), this ability should not cause administrative problems for plan sponsors. Commentators also asserted that the flexibility to design an eligible governmental plan to permit such distributions would be beneficial to its participants.

These regulations do not permit an eligible governmental plan to distribute rolled-in assets to a participant who is not yet eligible for a distribution until future guidance of general applicability is published that addresses this issue. Treasury and the IRS intend to issue, in the near future, guidance of general applicability resolving this issue in coordination with the applicable rules for qualified plans and section 403(b) contracts.

Commentators also requested clarification on the order of accounts for partial distributions to participants who have rolled-in assets that are subject to the early withdrawal income tax. They requested that consideration be given in final regulations to clarifying that the participant may be treated as receiving a partial distribution first from other plan assets to minimize the early withdrawal income tax that would otherwise apply. These regulations clarify that, if a rollover is received by an eligible governmental plan from an IRA, qualified plan, or section 403(b) contract, then distributions from the eligible governmental plan are subject to the early withdrawal income tax in accordance with the plan's method of accounting, *i.e.*, for purposes of applying the section 72(t) early withdrawal income tax, a distribution is treated as made from an eligible governmental plan's separate account for rollovers from an IRA, qualified plan, or section 403(b) contract only if the plan accounts for the distribution as a distribution from that account. Thus, for example, an eligible governmental plan may provide that any unforeseeable emergency withdrawal is made from other accounts to the extent possible, in which event the early withdrawal tax will not apply assuming that the plan only debits such other accounts to reflect the distribution.

The proposed regulations had requested comments on the issue of separate accounting for rolled-in amounts and asked if there are any special characteristics that would be lost if multiple types of separate accounts were not maintained. Commentators asked for the regulations to permit maintenance of a single rollover account for all amounts that are rolled into the eligible governmental plan. These regulations require separate accounting only to the extent mandated by section