

is operated in accordance with a reasonable, good faith interpretation of section 457(b). Whether a plan is operated in accordance with a reasonable, good faith interpretation of section 457(b) will generally be determined based on all of the relevant facts and circumstances, including the extent to which the employer has resolved unclear issues in its favor. The regulations state that a plan will be deemed to be operated in accordance with a reasonable, good faith interpretation of section 457(b) if it is operated in accordance with the terms of these regulations. The IRS will also deem a plan to be operated in accordance with a reasonable, good faith interpretation of section 457(b) if it is operated in accordance with the terms of the 1982 regulations as in effect for taxable years beginning before January 1, 2002 (to the extent those 1982 regulations are consistent with subsequent changes in law, including EGTRRA) or in accordance with the terms of the 2001 proposed regulations. However, a plan will be deemed not to be operated in accordance with a reasonable, good faith interpretation of section 457(b) if it is operated in a manner that is inconsistent with the terms of the 1982 regulations as in effect for taxable years beginning before January 1, 2002 (to the extent those 1982 regulations are consistent with subsequent changes in law, including EGTRRA) except to the extent permitted under either these final regulations or the 2001 proposed regulations.

Further, there is a special delayed effective date for the rule under which an eligible governmental plan cannot distribute rollover account benefits to a participant who is not yet eligible for a distribution. Thus, this rule is not applicable until years beginning after December 31, 2003, since this issue is expected to be resolved before that date.

The regulations also retain the rule in the proposed regulations under which the regulations do not apply with respect to an option that lacked a readily ascertainable fair market value (within the meaning of section 83(e)(3)) at grant that was granted on or before May 8, 2002. Thus, the status of such an option under section 457(f) would be determined without regard to these regulations.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure

Act (5 U.S.C. chapter 5) does not apply to these regulations. It is hereby certified that the collection of information in these regulations will not have a significant economic impact on a substantial number of small entities. The collection of information in the regulations is in section 1.457-8(a)(3)(ii)(B) and consists of the requirement that a custodian of a custodial account may be a person other than a bank only if the person demonstrates to the satisfaction of the Commissioner that the manner in which the person will administer the custodial account will be consistent with the requirement of section 457(g)(1) and (3) of the Code. This certification is based on the fact that the cost of submitting this information is small, even for small entities. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 602

Reporting and recordkeeping requirements.

Amendments to the Regulations

■ Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

■ **Paragraph 1.** The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *.

■ **Par. 2.** Sections 1.457-1, 1.457-2, 1.457-3 and 1.457-4 are revised to read as follows:

§ 1.457-1 General overviews of section 457.

Section 457 provides rules for nonqualified deferred compensation plans established by eligible employers as defined under § 1.457-2(d). Eligible employers can establish either deferred compensation plans that are eligible plans and that meet the requirements of section 457(b) and §§ 1.457-3 through 1.457-10, or deferred compensation plans or arrangements that do not meet the requirements of section 457(b) and §§ 1.457-3 through 1.457-10 and that

are subject to tax treatment under section 457(f) and § 1.457-11.

§ 1.457-2 Definitions.

This section sets forth the definitions that are used under §§ 1.457-1 through 1.457-11.

(a) *Amount(s) deferred. Amount(s) deferred* means the total annual deferrals under an eligible plan in the current and prior years, adjusted for gain or loss. Except as provided at §§ 1.457-4(c)(1)(iii) and 1.457-6(a), amount(s) deferred includes any rollover amount held by an eligible plan as provided under § 1.457-10(e).

(b) *Annual deferral(s)*—(1) *Annual deferral(s)* means, with respect to a taxable year, the amount of compensation deferred under an eligible plan, whether by salary reduction or by nonelective employer contribution. The amount of compensation deferred under an eligible plan is taken into account as an annual deferral in the taxable year of the participant in which deferred, or, if later, the year in which the amount of compensation deferred is no longer subject to a substantial risk of forfeiture.

(2) If the amount of compensation deferred under the plan during a taxable year is not subject to a substantial risk of forfeiture, the amount taken into account as an annual deferral is not adjusted to reflect gain or loss allocable to the compensation deferred. If, however, the amount of compensation deferred under the plan during the taxable year is subject to a substantial risk of forfeiture, the amount of compensation deferred that is taken into account as an annual deferral in the taxable year in which the substantial risk of forfeiture lapses must be adjusted to reflect gain or loss allocable to the compensation deferred until the substantial risk of forfeiture lapses.

(3) If the eligible plan is a defined benefit plan within the meaning of section 414(j), the annual deferral for a taxable year is the present value of the increase during the taxable year of the participant's accrued benefit that is not subject to a substantial risk of forfeiture (disregarding any such increase attributable to prior annual deferrals). For this purpose, present value must be determined using actuarial assumptions and methods that are reasonable (both individually and in the aggregate), as determined by the Commissioner.

(4) For purposes solely of applying § 1.457-4 to determine the maximum amount of the annual deferral for a participant for a taxable year under an eligible plan, the maximum amount is reduced by the amount of any deferral for the participant under a plan described at paragraph (k)(4)(i) of this