SCHNEIDER DOWNS
Retirement Solutions

# 457(b) Plans

## What You Should Know

### What is a 457(b) Plan?

A 457(b) plan is a retirement/pension plan that provides benefits to government employees, as well as those of tax-exempt organizations. Participants in 457(b) plans are allowed to defer their compensation on a before-tax basis via regular payroll deductions. Money placed in these accounts grows on a federally tax-free basis until withdrawn. Importantly, contribution limits for persons working for employers sponsoring a 401(k) or 403(b) are essentially doubled if they are also eligible for a 457(b) plan. Instead of being confined to a single contribution limit in each of their 401(k), 403(b) and 457(b) plans, employees are allowed to defer the maximum contribution amounts to each plan individually instead of combining each plan into a single limit.

### Nongovernmental 457(b) Plans

Nongovernmental 457(b) plans are limited to a select group of management or highly compensated employees – typically directors or officers of the company. Often this compensation limit is the same as that used for 401(k) participation testing purposes. Because these plans are usually limited to highly compensated employees or a select group of executives, they're sometimes referred to as "top hat" plans.

### 457(b) Plan Restrictions

Plans for nongovernmental entities are much more restrictive than their governmental counterparts. For example, money deferred into the plans cannot be rolled over into any other type of tax-deferred retirement plan – only another nongovernmental 457 plan. In addition, the money placed into these accounts is not held in a trust for the sole benefit of the employee who makes the deferral. Instead, the money remains the property of the employer and therefore is available to creditors.

### Elective Deferrals

Elective deferrals (governmental and tax-exempt) are not subject to income tax withholding in the year of deferral. For purposes of 457(b) plans, the definition of elective deferrals includes nonelective contributions made by the employer.

### Deferral Limits 2024

In 2024, the contribution limit on a 457(b) plan is $23,000. For years 2025 and beyond, the limit on these plans will be indexed for inflation, and applies to both governmental and nongovernmental 457(b) plans.

### Catchup Contributions

Two types of catchup contributions are potentially available under a 457(b) plan, if provided for in the plan document. Governmental 457(b) plans may provide for an age 50 catchup contribution similar to those permitted under 401(k) and 403(b) plans. An eligible participant of a governmental 457(b) plan who is over age 50 by the end of the calendar year could qualify for an additional catchup contribution of $7,500 in 2024.

Both governmental and nonprofit employers may allow for a "special" 457(b) catchup contribution in the three years prior to attainment of normal retirement age as defined in the plan document. This catchup feature can be as high as the normal annual deferral limit ($23,000 for 2024), however these contributions are limited to unused deferral limits from previous years. Participants who previously deferred the maximum amount into a 457(b) plan every year would not be eligible to use this special catchup.

A governmental 457(b) plan can provide for only one of these two types of catchup contributions, not both. A nonprofit 457(b) plan can only provide for special catchup contributions

### Governmental 457(b) Plan Distributions

A distribution from a governmental 457(b) plan that qualifies as an eligible rollover is subject to 20% income tax withholding unless the participant directly rolls over the distribution to another governmental 457(b) plan, IRA, 403(b) plan or qualified plan. If not an eligible distribution (e.g., a periodic distribution), it is subject to 10% withholding unless the participant elects to waive the withholding. The plan administrator (generally, the employer) is responsible for the withholding unless it directs the payor to withhold income taxes on the distribution. The plan administrator reports the distribution on a Form 1099-R in the same manner as a qualified plan. Further, the 457(b) plan reports the withholding annually using the EIN and Form 945 of the person responsible for the withholding (generally, the plan administrator), though the plan may use the EIN of the trust if the trust obtains its own trust EIN. If that's the case, the 457(b) plan uses the trust's EIN to report distributions and withholding on Forms 1099-R and 945.

### Tax-exempt 457 Plan Distributions

Distributions from a 457(b) plan sponsored by a nonprofit employer are taxed as wages in the year paid. Accordingly, the plan administrator needs to withhold income taxes with respect to such distributions in the same manner it would any other wages. Distributions are reported on Form W-2 and the withholding on Form 941. Distributions to a beneficiary are reportable on Form 1099-R and such distributions are not subject to withholding.