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Filed Electronically

April 26, 2006

CC:PA:LPD:PR (REG-146459-05)
Room 5203
Internal Revenue Service POB 7604
Ben Franklin Station
Washington, DC 20044

Re: Proposed Regulations Regarding Designated Roth Accounts under Section 402A

Dear Sir or Madam:

The SPARK Institute, Inc. (“SPARK”)¹ appreciates the opportunity to comment on the proposed regulations regarding “Roth Contribution(s).” SPARK members have significant experience with the recordkeeping and administration of retirement plans. Our members are the service providers that will be largely responsible for providing recordkeeping and administrative services for Roth Contributions to a substantial majority of retirement plans. Accordingly, we respectfully request that the Internal Revenue Service (“Service”) consider the following comments.

Our members are concerned that the Roth Contributions regulations as currently written are overly complex and difficult for plan sponsors to understand. Consequently, the adoption of

¹ SPARK represents the interests of a broad-based cross section of retirement plan service providers, including members that are banks, mutual fund companies, insurance companies, third-party administrators and benefits consultants. SPARK members include all of the largest service providers in the retirement plan industry and the combined membership services more than 95% of all defined contribution plan participants.

Roth Contributions has been dramatically less than previously expected.² Among the reasons that Roth Contributions have not been widely adopted are: (1) the perceived administrative complexity among plan sponsors; (2) the perceived complexity in the communication of Roth Contributions and potential participant confusion; and (3) the scheduled sunset of Roth Contributions at the end of 2010.

SPARK requests the following changes to the Roth Contributions regulations in order to simplify their administration and make them less confusing for plan sponsors.

A. Rollover Complexity

SPARK members are concerned that the complexity of the existing rollover provisions in the proposed regulations will unintentionally restrict the portability of Roth accounts. Plan sponsors are reluctant to accept additional reporting requirements. Consequently, plan sponsors are likely to design their plans to prohibit Roth rollovers altogether. SPARK urges the Service to simplify the rules as outlined below.

1. Direct Rollovers between “unlike” plans

The proposed regulations state that a direct rollover, specifically the basis portion of a Roth account from a plan qualified under 401(a), may only be made to another plan qualified under 401(a) that agrees to separately account for the amount not included in income. Likewise, in a 403(b) account with Roth Contributions, the basis portion may only be rolled over to another 403(b) plan via a direct rollover. Pre-tax accounts may be rolled over to any eligible retirement plans, 401(k), 403(b), and governmental 457(b) plans via direct rollover or 60-day rollover. SPARK urges the Service to allow Roth Contributions to be eligible for the same treatment as pre-tax contributions.

2. Reporting requirements for plans receiving indirect rollovers

Under the proposed regulations a plan that receives an indirect (60-day) rollover must report detailed information about the transaction to the Service. Plans that receive direct rollovers of Roth assets or non-Roth rollovers under the current regulatory and reporting environment have no such requirement. Accommodating this new reporting requirement will require costly recordkeeping system modifications; however, distinguishing among these rollovers will be of little value. The Service will be notified of a rollover transaction via Form 1099-R filed by the distributing plan under the current reporting requirements. Additional reporting by the recipient plan appears to be needlessly redundant. In order to avoid these costly changes and reporting requirements it is likely that service providers and plan sponsors will design their plan and administrative practices so that indirect rollovers will not be accepted. This will have the inadvertent and undesirable effect of causing participants to take a distribution instead of a rollover.

² According to an informal survey of SPARK members the adoption of Roth Contributions since January 1, 2006 is less than five percent.

3. Five-year tracking rule – the need for consistency

Under the proposed regulations, a direct rollover will preserve the time in the prior plan for purposes of the five-year rule while an indirect rollover will receive no credit toward the five-year rule. Most service providers will likely supply the required information to the new service providers for direct rollovers (the amount of the investment in the contract and the first year of the five-year period) either in writing or electronically. The service provider will also provide the information to the participant that receives a distribution. SPARK urges the Service to allow an indirect rollover to receive the same treatment as a direct rollover if the participant provides to the recipient plan reasonable proof of the basis amount and the first year of the Roth Contributions (e.g., a copy of a check stub). Treating indirect and direct rollovers similarly for purposes of the five-year tracking rule will simplify plan administration and communications, and preserve savings through more flexible portability options.

4. Tax impact of partial rollovers to an IRA

SPARK requests that the Service clarify its position regarding what appears to be an inadvertent conflict between the preamble of the proposed regulation and the proposed regulation itself with respect to the tax impact of a partial rollover. The introduction to the proposed regulations states that:

“...if only a portion of the distribution is rolled over, the portion that is not rolled over is treated as consisting first of the amount of the distribution that is includible in gross income. These regulations would provide that the income limits for contributions for Roth IRAs do not apply for this purpose.”

This seems to contradict the proposed regulations and the long standing ordering rules providing that the portion of the distribution rolled over is first considered ordinary income and the portion not rolled over is considered the recovery of basis. Section 402(c)(2) is consistent with this rule. Additionally, the Q&As indicate that in the context of partial rollovers, the ordinary income is considered to be the first portion rolled over. SPARK requests that the Service clarify that the ordinary income portion would first be considered rolled over when a partial rollover occurs.

5. Roth rollovers to plans without Roth deferrals

A plan that accepts basis via a direct Roth rollover must be able to separately account for those assets. The proposed regulations do not address whether a plan could accept Roth rollovers if the plan does not also permit Roth deferrals. SPARK requests that the Service clarify that a plan may be designed to accept a Roth rollover without adding a Roth Contribution feature provided that the plan can separately account for Roth rollovers.

B. Hardship complexity

The proposed regulations §1.402A-1, Q-8 require that hardship distributions from a designated Roth account are treated as consisting of basis and a pro rata share of earnings for tax purposes. In a plan that allows distributions of elective deferrals pursuant to Treasury Regulations Section 1.401(k)-1(c)(3), which requires that such distributions not include earnings, the plan must also keep a running total of the amount of elective deferrals available for hardship distributions. Essentially, two separate and distinct accounting functions must exist – one for determining taxation of hardship distributions, and one for determining the amount available for hardship. This is both difficult to administer and confusing to plan sponsors and participants.

SPARK urges the Service to eliminate the need for dual hardship accounting functions by characterizing hardship distributions as a return of elective deferrals only and not a pro rata return of basis and earnings. If the Service does not feel that it has the statutory flexibility to make this change, SPARK requests guidance on determining the amount available for hardship distributions when a plan limits hardships to pre-tax sources (i.e., can both Roth and pre-tax deferrals be included in determining the hardship amount available but satisfy the entire hardship from only the pre tax account?).

C. Other Issues

1. 402(f) notice

SPARK requests that the Service issue a revised sample 402(f) notice that incorporates the final Roth regulations. The complexity and difficulty in explaining and understanding the tax implications of Roth distributions lends itself to standardized model language from the Service.

2. Corrective distributions involving Roth Contributions

SPARK requests that the final regulations allow plan sponsors and document providers to adopt broad language regarding the handling of excess contributions and corrective measures involving Roth Contributions so that amendments are not necessary each year in processing refunds of excess contributions. In the final regulations issued in December of 2005, under Code section 402A. 71 Fed.Reg. 6 (Jan. 3, 2006), Treasury Reg §1.401(k)-2 was amended to state:

“Similarly, a plan may permit an HCE with elective contributions for a year that includes both pre-tax elective contributions and designated Roth contributions to elect whether the excess contributions are to be attributed to pre-tax elective contributions or designated Roth contributions.”

Additionally, the preamble of those regulations states that:

“There is no requirement that the plan provide this option, and a plan may provide for one of the correction methods described in the final regulations without permitting an HCE to make such an election.”

A plan may want to switch its administrative approach from one year to the next. For example, a calendar year plan, in order to meet the March 15th compliance deadline may want to direct that corrective distributions for excess contributions be taken from pre-tax elective pretax deferrals to the extent needed to satisfy the ADP test and then, if necessary, from Roth Contributions. However, for subsequent years, the plan may want to offer affected HCEs a choice between refunds from their pre-tax deferrals or Roth Contributions. SPARK requests that the regulations be modified to allow a plan to change how it addresses these issues without the adoption of a formal amendment every year.

3. Separation from service and the five-year rule

SPARK requests that the Service provide guidance regarding the treatment of a participant who returns to work after a break in service and repays a prior distribution to the plan in order to restore any forfeited company contributions. Specifically, SPARK requests that the Service clarify whether a participant should receive credit for purposes of the five-year rule for the period of time during the break in service.

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SPARK appreciates the opportunity to provide these comments to the Service. In addition, SPARK respectfully requests to supplement this formal submission with further comments that we might receive from our members. Should you have additional questions or need additional information, please do not hesitate to contact us at (860) 658-5058.

Respectfully,

/s/

Robert G. Wuelfing
President

/s/

Larry H. Goldbrum
General Counsel

cc: Tom Schendt (Alston + Bird)