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Small Business Jobs Act of 2010
New Roth Conversions within 401(k) Plans

The Small Business Jobs Act of 2010 (the "Jobs Act") was signed into law on Monday. It allows 401(k) plans to permit participants to convert certain portions of their before-tax accounts into Roth accounts without taking distributions from the plan. This provision of the Jobs Act is effective September 27, 2010.

Mechanics of Conversion. Under the Jobs Act, a Roth conversion within a 401(k) plan is technically a distribution from the plan and an immediate rollover back into a designated Roth account under the same plan. Previously, Roth conversions could be accomplished only by means of an actual distribution and rollover into a Roth IRA.

Limitations. Because a Roth conversion is technically a rollover, it may only be made available to participants who are otherwise eligible to receive distributions from the plan. For example, a 401(k) plan may not permit participant deferrals to be distributed until a participant severs from employment, dies, becomes disabled or attains age 59½. This means that an actively employed participant cannot transfer his or her before-tax contributions into a Roth account until the participant reaches age 59½.

Also, these types of Roth conversions may only be offered by 401(k) plans that allow participants to make Roth 401(k) deferrals. A plan cannot establish Roth accounts only to accommodate conversions.

Taxation. A Roth conversion within a plan is taxed the same way as a rollover to a Roth IRA. The amount of the distribution is currently taxable to the participant, but it is not subject to the early distribution excise tax. In addition, for a conversion that occurs during 2010, the participant may elect to include half of the converted amount in income in 2011 and the other half of the distribution in income in 2012.

Distributions from Roth accounts are tax free if the distribution is made (i) after the 5-year period beginning with the first year the participant made a contribution to the Roth account, and (ii) after the participant attains age 59½, dies or becomes disabled.

Plan Amendment. If you would like to add a Roth conversion feature to your plan, your plan document will need to be amended by the end of the plan year in which conversions are first offered. It is anticipated that the IRS will establish some remedial amendment period to allow later amendments, but it has not yet been announced.

Contact Information. If you have any questions about these new Roth conversions or whether they may be implemented in your plan, please contact David Putnal (404.888.8836), Toby Walls (404.888.8870), Teri King (404.888.8847), Andrew Overway (404.888.8858) or Will Cantrell (404.888.8839).

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