

LETTER TO CREDIT UNIONS
NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA 22314

DATE: February 20, 1998

LETTER NO.: 98-CU-5

TO: ALL FEDERALLY INSURED CREDIT UNIONS

SUBJECT: NEW FEDERALLY-INSURED CREDIT UNION ACCOUNTS

This letter is intended to inform you of several new member accounts eligible to be insured by the National Credit Union Share Insurance Fund (NCUSIF). These accounts include Education and Roth IRAs, Medical Savings Accounts (MSAs), and Savings Incentive Match Plan for Employees (SIMPLE) accounts. As of January 1, 1998, federally-insured credit unions are permitted to establish and maintain these accounts; however, credit unions are not required to offer them. To date, the Internal Revenue Service (IRS) has not issued comprehensive implementing rules or guidance on all of these accounts. Therefore, credit unions should contact the IRS and/or their own legal counsel or tax advisor if more information is needed.

Education and Roth IRAs

Two new IRA options are Education IRAs and Roth IRAs. The objective of the Education IRA is to provide a means for parents to save for the future costs of their children's higher education through nondeductible, after-tax contributions. The objective of the Roth IRA is to provide an IRA funded with nondeductible, after-tax contributions that permits tax-free withdrawals of interest and principal under certain conditions.

NCUA considers both Education and Roth IRAs to be insured member accounts. For insurance purposes, Education IRAs are insured as irrevocable trust accounts under 12 C.F.R. §745.9-1 and will be added to other irrevocable trust accounts for insurance purposes. Roth IRAs are insured as traditional IRAs under 12 C.F.R. §745.9-2. A Roth IRA and a traditional IRA of a member will be added together for insurance purposes.

Savings Incentive Match Plan for Employees

A SIMPLE plan is a retirement plan for small employers. It can be offered as a SIMPLE Retirement Account (SRA) or a SIMPLE 401(k) plan without having to comply with all of the current IRS rules for qualified plans. SIMPLE plans will be available to most employers that do not simultaneously maintain a qualified retirement plan or Simplified Employee Pension Plan, and that employ 100 or fewer employees who earn \$5,000 or more per year. To be eligible, an employee must earn at least \$5,000 per year for the two prior years and the current year.

NCUA considers member accounts established as either SRAs or SIMPLE 401(k)s to be insured member accounts. For insurance purposes, SRAs will be added to other traditional IRAs and insured under 12 C.F.R. §745.9-2. SIMPLE 401(k)s will be added to other deferred compensation accounts and insured under 12 C.F.R. §745.9-3.

Medical Savings Accounts

Federal MSAs are tax-exempt trust or custodial accounts into which either employers or employees of small companies and the self-employed, but not both, may deposit funds to pay for non-catastrophic health care. Instead of using traditional health insurance, a person with an MSA must purchase a catastrophic health insurance policy with a high deductible and pay for routine medical care out of the MSA non-catastrophic health care account. MSA contributions by an eligible individual are deductible in computing adjusted gross income. Unused MSA funds can be carried over to cover future medical expenses. Distributions from an MSA are excludable from gross income if used for medical expenses. Other kinds of MSA withdrawals are generally taxable and subject to an early withdrawal penalty. However, MSA distributions made after the account holder turns age 65, becomes disabled, or dies are not subject to the penalty.

Initially, MSAs are a pilot program made available to a limited population of 750,000 taxpayers over 4 years (1997-2000). This trial population includes self-employed workers and workers at companies with 50 or fewer employees. NCUA is aware that sixteen states have legislation authorizing state MSAs: Arizona, Colorado, Idaho, Illinois, Indiana, Louisiana, Michigan, Mississippi, Missouri, Montana, New Mexico, Oklahoma, Utah, Virginia, Washington and West Virginia.

NCUA considers federal and state MSAs to be insured member accounts. The particular account classification for an MSA will depend upon the circumstances of how it is established and maintained. An individual MSA may be insured as either a Single Ownership Account under 12 C.F.R. §745.3 or Deferred Compensation Account under 12 C.F.R. §745.9-3. A family or joint MSAs may be insured either as Joint Accounts under 12 C.F.R. §745.8 or Deferred Compensation Accounts under 12 C.F.R. §745.9-3. Depending on the account classification, the funds in an MSA will be added to other similarly classified accounts for insurance purposes.

Currently, a FCU can not act as a trustee or custodian of an Education or Roth IRA, an SRA or SIMPLE 401(k), or either a federal or state MSA.

If you have any questions on interpretations of the laws affecting Roth and Education IRAs, SIMPLE accounts, or Medical Savings accounts, please contact the IRS or your tax or legal advisor. If you have any questions regarding FCU trust powers or the NCUSIF insurability of credit union member accounts, please call your regional office.

For the National Credit Union Administration Board,

/S/

Norman E. D'Amours
Chairman

