

MEMO# 12292

July 18, 2000

MASSACHUSETTS DEPARTMENT OF REVENUE RELEASES GUIDANCE ON TAX TREATMENT OF PARTNERS' ELECTIVE CONTRIBUTIONS TO 401(K) PLANS

[12292] July 18, 2000 TO: PENSION COMMITTEE No. 50-00 RE: MASSACHUSETTS DEPARTMENT OF REVENUE RELEASES GUIDANCE ON TAX TREATMENT OF PARTNERS' ELECTIVE CONTRIBUTIONS TO 401(K) PLANS The Massachusetts Department of Revenue recently released Directive 00-5, which provides that a partner's elective contributions to a 401(k) plan, including any partnership matching contributions that are treated as elective contributions, are excluded from Massachusetts gross income to the extent they are excluded from federal gross income. The Directive notes that a partnership is allowed to have a 401(k) plan, which includes any arrangement that directly or indirectly allows partners to vary the contributions made on their behalf to the plan. The partnership is treated as the employer of each partner who is an employee. For tax years beginning before January 1, 1998, if the partnership made matching contributions to a partner's elective contributions, the matching contributions were also treated as elective contributions and therefore excluded from gross income. For tax years on or after January 1, 1998, partnership matching contributions are treated as elective contributions only if the partnership elected to have them so treated for purposes of nondiscrimination testing for the 401(k) plan. Directive 00-5 states that although the federal rule for what constitutes a partnership's elective contribution changed in 1998, the result for Massachusetts tax purposes remains the same. If the partnership's contribution is excluded from federal gross income, it will be excluded from Massachusetts gross income. The Directive also states in a footnote that if the partnership does not elect to have the matching contribution treated as an elective contribution, the matching contribution is included in the partner's federal and Massachusetts gross income. For federal tax purposes, the partner's distributive share of contributions made by the partnership on his or her behalf are deductible. A copy of Directive 00-5 is attached. Kathryn A. Ricard Associate Counsel Attachment Attachment (in .pdf format)