

Final 403(b) Regulations

Writing the “rule book”
Understanding Revenue Procedure 2007-71

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- Member, Association of School Business Officials International, Legislative Affairs Committee
- Member, American Society of Pension Professionals & Actuaries Tax Exempt/Governmental Plans Committee
- Assisted the Internal Revenue Service as a presenter for their “Partnership for Compliance for 403(b)” program
- Administrator of Qualified and Governmental Retirement Plans since 1985

Background

Let's recap once again....





History

- Proposed regulations issued 11/16/04
- Comment period ended 2/14/05
 - ASBO Int'l submitted comments
- Public hearing held 2/15/05
- Final regulations issued 7/26/07
- IRS responsive to ASBO Int'l comments
 - Model plan language – issued 11/27/07
 - PowerPoint for School Administrators
 - DVD for School Administrators
 - Updated brochures for Districts and Participants

Effective Dates of the Regulations

- The majority of guidance published consists of clarification of current rules...
- Clarification items are effective NOW. Administration should be performed utilizing these rules.
- Will be put into written form in the plan document.
- (Rev. Proc. 2007-71 offers some relief.)



Effective Dates for the Regulations



- Contract Exchanges are effective *September 24, 2007*
- Life insurance changes are effective *September 24, 2007*
- All other non-clarification items *are effective January 1, 2009.*

Clarification Items

How are they translated into our plan document?





Model Plan Language – Rev. Proc. 2007-71

- The model plan language provided has been prepared to take into account the general requirement that a IRC § 403(b) plan include all of the material terms and conditions for the benefits offered under the plan.
- The model plan language provided is intended to be used for a basic plan under which contributions are limited to pre-tax elective deferrals only.



What are the provisions of the plan?

- Eligibility - Universal Availability
- Investment Options - Qualified Funding Vehicles (Annuity/Custodial Mutual Fund Agreements)
- Contributions including types, limitations, and aggregation with other plans
- Plan Rollovers
- Plan Transfers
- Optional plan features such as:
 - Participant loans
 - Hardship withdrawals
 - Roth provision
- Plan distributions



Who is eligible?

Universal Availability Rules

- If the employer offers 403(b) elective deferrals, (including pre-tax and Roth) all employees of the eligible employer must be permitted to have section 403(b) elective deferrals contributed on their behalf. Exceptions are allowed for:
 - Employees who are eligible to participate in a 457(b) eligible governmental plan
 - Employees who are eligible to participate in a 401(k) plan provided by the employer



Universal Availability Rules

- Employees who are non-resident aliens
- Employees who are students providing services described in section 3121(b)(10)
- Employees who normally work fewer than 20 hours per week if and only if:
 - For the 12-month period beginning on DOE, the employer reasonably expects the employee will work less than 1000 hours in such period; and
 - For each plan year following after the close of the initial 12 month period, the employee works less than 1000 hours of service

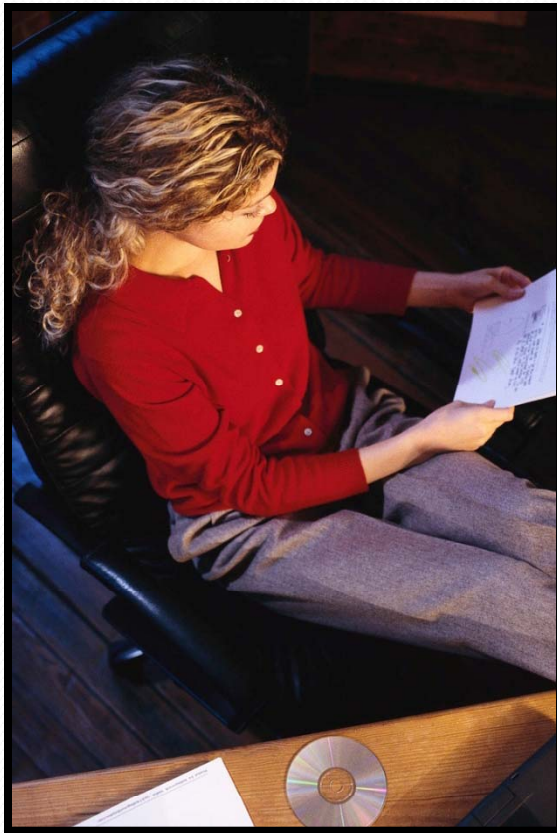


Remember...

Testing is required at least annually...

- You can not exclude employees by class such as substitute teachers and food service.
- You must look at all employees and determine if they have met the eligibility requirements of your plan. (i.e. Did they work 750 hours in a 9 month work year or 1000 hours in a 12 month work year?)
- The plan satisfies the universal availability requirement only if the plan provides an employee with an “effective opportunity” to make (or change) a cash or deferred election at least once during each plan year.

What is an effective opportunity?



- “Effective opportunity” includes:
 - Notice of the availability of the election.
 - Period of time during which the election can be made
 - Other conditions of the election
 - Does not exist if there are any other rights or benefits that are conditioned (directly or indirectly) upon participant making or failing to make an election

Model Plan Document

Eligibility Provision

- **Plan eligibility** –the model plan provides that employees who normally work fewer than 20 hours per week or who are student teachers are not eligible to participate. This language will need to be revised if all employees are eligible to participate in the 403(b) plan or if other permitted exclusions are applied.

Model Plan Document

Automatic Enrollment

- **Automatic enrollment** – the model plan includes an optional provision that provides for any new employee to be automatically enrolled in the 403(b) plan at the time of hire with 5% of pay to be contributed to the plan unless the employee elects otherwise.



Model Plan Document

Allows for Multi-Vendor Annuity and Custodial Mutual Fund Products

- Section 403(b) provides for exclusion from gross income for contributions made by certain employers to specific types of funding arrangements. They include:
 - Annuity contracts issued by an insurance company;
 - Custodial accounts that are invested solely in mutual funds;
 - Retirement Income Accounts which are only permitted for church employees (Only in Church Plans)

Your plan will control your investment providers. Who and What....

- You will identify in your plan document the available investment contracts.
- You are responsible for all transactions to ensure compliance with regulations. Beginning 1/1/09 or even sooner, you will be required to certify eligibility for transactions for any employee employed on 1/1/09 or later.
- Service Agreements should be established with each vendor detailing responsibilities for district coverage purposes.





Rev. Proc. 2007-71 Offers Relief...

- Under these new rules, the contracts held by these vendors will not fail to satisfy § 403(b) merely because the contract is not part of the written 403(b) plan if the employer makes a reasonable, good faith effort to include the contract as part of the employer's plan. A good faith effort includes collecting available information concerning those vendors and notifying those vendors of the name and contact information for the person in charge of administering the plan. **(For this purpose, information is not required to be collected for vendors that ceased to receive contributions prior to January 1, 2005.)**



Rev. Proc. 2007-71 Cont.

- If the participant or beneficiary requests a transaction from the contract, the relief only applies if the vendor makes reasonable efforts to determine the participant's status under the plan from the employer prior to processing. However, if the participant is a former employee of the employer or a beneficiary as of January 1, 2009, the revenue procedure allows the vendor to rely on information from the participant regarding the participant's status as a former employee or beneficiary as of January 1, 2009.
- This special rule applies only with respect to contracts issued prior to January 1, 2009.




Contributions Available Under the plan...

- The final regulations provide guidance on the types of contributions and the calculation of maximum allowable contribution amounts per participant. They include examples on determining contribution limits and maximum amounts.
- All types of contributions are considered part of a single plan such as:
 - Pre-tax employee elective deferrals
 - Roth employee elective deferrals
 - Non-elective Employer contributions (including pre-post retirement)
 - Employer matching contribution



Limitation Testing...

- Contribution limitation testing includes certain ordering rules and aggregation rules.
- Employee contributions to multiple contracts must be aggregated as well as Pre-tax and Roth amounts.
- Employee contributions to other 403(b), 401(k), SIMPLE IRA, and SARSEP plans must be aggregated with amounts in your plan to insure employees do not exceed limits.
- Hardship withdrawals suspend an employee's ability to contribute for six months following the payment; if contributions continue excesses can be created.




Model Plan Language – Contribution limited to Pre-tax Deferrals

- If the employer offers Roth deferrals, employer matching contributions, employer nonelective contributions or post-retirement contributions, the model language will require additional and/or revised provisions which may be necessary or appropriate to comply with the regulations and, if applicable, ERISA.



Distribution Rules

- Plan Document language must be provided for the timing of benefits including early distribution, required minimum distributions, and special rules related to optional features such as hardship withdrawals and participant loans as well as other incidental benefits.
- The general rule is - a distribution may not be paid before the participant has a severance of employment, has a hardship, dies, becomes disabled, or attains age 59 $\frac{1}{2}$.
 - Severance of employment has been defined, for purposes of a public school, as when the employee terminates from the school district and not from the state retirement system.



Model Plan Language – Provides for Benefits Options detailed within contracts plus...

- The model plan language allows for a “paper clip” approach to illustration of plan distribution options by referring to individual contracts.
- The model plan language includes an optional provision that allows for in-service distributions from any amounts held in a rollover accounts.

Your plan will need to allow for Plan Transfers and Rollovers if you wish to offer them...



- Transfers to allow for purchase of permissive service credits in state retirement plans
- Rollovers in and/or out of the plan.
- The model plan includes an optional provision allowing for eligible rollover contributions to the 403(b) plan to the extent permitted by the individual participant contracts.



Contract Exchanges Defined...

- Rev. Proc. 2007-71 defines the differences between a transfer of funds related to a change in the investments among vendors who are permitted to receive contributions to the plan and a contract exchange with vendors who are not permitted to receive plan contributions but who have entered into information sharing agreements with the employer;
- Employees are allowed to make “Contract Exchanges” but it must be detailed within the plan.
- They may move money within your plan using investment providers with whom you have established an agreement to provide data for compliance
- This rule is effective ***September 24, 2007.***
- Prior to that date, employee may exchange contracts to vendors where you have no control. This will create additional administrative burdens in tracking all plan assets and transactional review.

Model Plan – Allows for Contributing and Non-Contributing Vendor Exchanges

- **Exchange to Vendors Who Do Not Receive Regular Participant Contributions** – the model plan includes an optional provision allowing participants to exchange all or a portion of their account balances to vendors who do not regularly receive plan contributions made by participants.

Optional Features in the Model Plan...

- **Hardship Withdrawals**
 - the model plan includes an optional provision allowing for hardship withdrawal payments to the extent permitted by the individual participant contracts and which satisfy 403(b) rules.
- **Loans** – the model plan includes an optional provision that allows for participant loans up to the allowable limits and to the extent permitted by individual participant contracts.



Opportunity for design...

- The written plan document requirement provides a district with the opportunity:
 - To clearly define plan provisions and communicate them to staff
 - Design the plan to meet the needs of employees
 - Evaluate optional features such as:
 - Participant loans
 - Hardship Withdrawals
 - Acceptance of plan rollover
 - Establish Investment Policies and guidelines
 - It is advisable not to use the Model Plan unless all provisions are followed in operation.

Plan Termination an option but must be included in plan language

- The final regulations allow for provisions to be added to the plan document to permit complete plan termination, including distribution of all balances to employees, without disqualification of the plan, provided certain conditions are met.





Plan termination continued...

- In order to terminate a plan, all elective deferrals must be ceased for a least one year prior to the termination and one year following the termination.
- No more than 2% of employees may be covered under another 403(b) within the wait period.
- Employee satisfaction and competition for qualified staff may alter your options – your concern for providing a competitive benefits package may alter your decision in whether to terminate.

District Liabilities

How do you reduce district liability and exposure?



Final Regulations – Employer responsible

- The final regulations state that the employer can not assign responsibilities for the plan to participants. They do allow for assignment to other parties other than the employer for substantial duties necessary to administer the plan. Even if assignments of duties are made, the employer remains ultimately responsible for making sure that all plan duties are performed.



Options for support

- Options are available for support to the district in performing required duties.
- Important to identify what duties you wish to maintain and what duties you wish to assign.
- Common remitters offer support in contribution transaction processing only.
- Transactional support is where the majority of defects occur. (Will vendors talk to other vendors?)
- Complete TPA services may be offered for overall support. (Review Service Agreements.)



Engagement and/or Service Agreement a must...

- In order to completely cover the district, thoroughly review your service provider's service agreement. Free insurance may be no insurance.
- Should be a detailed list of responsibilities being performed by both the district and the service provider.
- Indemnification language should provide language for district "403(b) insurance", your vendor will indemnify you for negligence in their performing the duties under the contract.

Summary

Where do I turn; what does this all mean?



Final Regulations

- The final regulation offer support to plan sponsors but most importantly; plan participants.
- The focus of the regulations are to provide for the security of the retirement plan assets of plan participants and their beneficiaries.
- Although there is additional administration and notice requirements; the intent is to meet the long-term needs of those covered employees under the plan.

Questions?



- We would be happy to address your questions concerning the regulations. Feel free to contact us at:
- tmiddleton@gatekeeperteam.com
- or
- 877-403-4411