

Impact of New 403(b) Regulations on Public School Districts:

Didn't Anyone Tell the IRS We're Kind of Busy?



Presented at CASBO Institute

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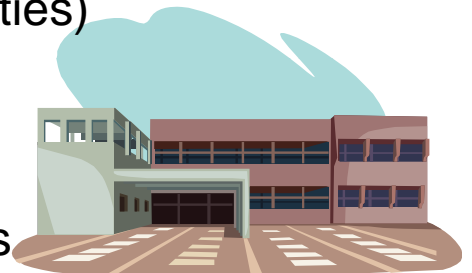
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403(b) Refresher

➤ What is a “403(b)” Plan?

- Internal Revenue Code Section -- allows deferral of income taxation
- Tax-Sheltered Annuities (TSAs), Tax-Deferred Annuities (TDAs), 403(b), 403(b)(7) Custodial Accounts
- Certain tax-exempts (“501(c)(3)s”) and public schools
- Assets may only be held in an annuity contract or a special type of custodial account under 403(b)(7) (in which case the account must be invested exclusively in mutual funds)



403(b) Refresher

➤ Annual Contribution Limits

- Salary Reduction

■ Base salary reduction limit	\$15,500 (2008)
■ Special 15-year catch-up*	up to \$ 3,000 for 5 years
■ Age 50 catch-up	\$ 5,000 (2008)
	<hr/>
	\$23,500 (2008)



* Example of administrative complexity. Employee must have 15 years of service with same “qualified organization”. Special catch-up raises basic limit by \$3,000/year for 5 years (overall \$15,000 maximum); except that catch-up phases out to zero if employee averages \$5,000/year for all years of employment.



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403(b) Refresher

➤ Annual Contribution Limits

- Combined (Employer & Employee) \$46,000 (2008)
 - Age 50 “Catch-up” does not count against limit



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Theme Throughout IRS Regulations

➤ **Non-compliance**  **rules similar to 401(k) plans**

- Final IRS Regulations issued in 2007 replace some regulations dating back to 1964
- Effective January 1, 2009 (Generally)
- 7 Months to:
 - Understand current operation
 - Consider alternatives
 - Discussions with unions, if applicable
 - Make decisions
 - Implement decisions:
 - Providers
 - Plan document
 - Administrative procedures
 - **Information sharing agreements**
 - Employee Communications



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New Requirements under 403(b) Regulations

1. **Plan Document**

- Must state:
 - Eligibility
 - Benefits
 - Limitations
 - Investment products and providers
 - Time and form of distribution
 - Terms of any optional features
 - Loans
 - Hardship withdrawals
 - Contract exchanges
 - Allocate responsibility for administrative functions
- More than one document can be “stapled together” as plan document
- IRS Sample Document – Rev. Proc. 2007-71 (Voluntary Deferral Only Plan)
- Action items
 - Confirm terms of plan
 - Consider any necessary or desired changes



New Requirements under 403(b) Regulations (continued)

2. Universal Eligibility -Elective Deferrals

- Universal Availability
 - If any employee may make 403(b) elective deferrals, all employees must be permitted to do so (\$200 minimum)
 - Effective opportunity – notice
 - Exceptions:
 - (i) employees eligible under another 403(b), 401(k) or 457(b) governmental plans
 - (ii) non-resident aliens
 - (iii) certain students
 - (iv) employees normally work <20 hours/week, and expected to work <1,000 hours/12 months
- No longer permissible to exclude:
 - (i) collectively bargained employees
 - (ii) visiting professors
 - (iii) governmental employees who make one-time elections to participate in another plan
 - (iv) clergy and other religious employees working under vow of poverty
- Delayed effective dates (generally 1/1/10)
- Action Items
 - Confirm universal availability (plan for transition if applicable)
 - Review notices



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New Requirements under 403(b) Regulations (continued)

3. Non-discrimination Testing

- Elective deferrals –
no testing (except for universal availability)
- Employer, and after-tax employee, contributions – testing
(governmental exemption under IRC section 403(b)(12)(C),
except for compliance with 401(a)(17) compensation limit)
- Action Item
 - Decide which Employee Groups to Exclude: student workers



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New Requirements under 403(b) Regulations (continued)

4. Timeliness of Contributions

- **No longer than reasonable for the proper administration of plan.**
Example: Transferring elective deferrals within 15 business days following the month in which \$ would otherwise have been paid
- ERISA plans – **As soon as assets can reasonable be segregated**, but not later than 15 business days following the month in which \$ would otherwise have been paid
(15 days is outside limit, **not** a safe harbor. DOL did propose on February 29, 2008 an ERISA safe harbor, for small plans (fewer than 100 participants), of 7 business days from withholding.) Not technically applicable to governmental plans, but useful guidance nonetheless.
- Action Item
 - Determine length of time to transfer assets



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New Requirements under 403(b) Regulations (continued)

5. Distributions:

- Elective deferrals
Not earlier than:
 - severance from employment;
 - age 59-1/2;
 - disability; or
 - financial hardship(Grandfather rule for pre-1989 deferrals)
- Employer contributions – Custodial Account
Not earlier than:
 - severance from employment;
 - age 59-1/2; or
 - disability
- Employer contributions – Annuity
Not earlier than:
 - severance from employment;
 - age 59-1/2;
 - disability; or
 - stated event – qualified profit sharing plan rules



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New Requirements under 403(b) Regulations (continued)

6. Contract Exchanges –Information Sharing Agreements

- **Participant** replaces existing contract for another with a different provider
(In past, benefit distribution restrictions required to be maintained, but compliance problems)
- **Employer** must enter into an Information Sharing Agreement with the provider receiving the assets
 - Applies to any exchange after September 24, 2007
 - Agreement to share employment and plan benefit information between employer and provider to ensure compliance with plan provisions and legal limitations (e.g. employment status, hardship withdrawal and loan limits)
 - Transition rules regarding non-approved providers and contracts issued before 1/1/2009
- **Action items**
 - Enter into Information Sharing Agreements with providers that have received assets since September 24, 2007
 - Decide whether to permit contract exchanges in the future
 - If permitted, consider limiting the list of providers
 - Consider scope of grandfathering for post 12/24/07 exchanges



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New Requirements under 403(b) Regulations (continued)

7. Plan-to-Plan Transfers



- Between 403(b) plans, if individual is employee or former employee of plan receiving assets, and benefit distribution restrictions maintained
- To governmental defined benefit plan to purchase permissive service credits
- Otherwise, no plan-to-plan transfers to non-403(b) plans (Rollovers permitted)



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New Requirements under 403(b) Regulations (continued)

8. Plan Terminations

- Permitted, subject to successor 403(b) plan restrictions
- Assets distributed, with right to rollover to another eligible retirement plan (i.e. a 403(b), 401(k), 457(b) governmental or IRA)
- Cannot merge or transfer 403(b) assets into a 401(k) or 457(b) plan. Note: Transfer upon plan termination must be at request of the individual through the rollover process



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New Requirements for Form 5500

- **Increased 5500 Financial Information and Plan audits for ERISA 403(b) Plans, starting with 2009 plan year filings**
 - DOL Reg. issued July 16, 2007
 - Good news—5500 report requirement not applicable for 403(b) plans of public school districts



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Bottom Line

1. Increased Employer Involvement/Responsibility

2. Getting Started:

- Understand your 403(b) plan – identify current contracts, custodial agreements, SPDs, forms, collective bargaining agreements
- Review for compliance (now and post-1/1/09)
 - Satisfying universal availability requirements
 - Determine applicable effective dates
- Contact current and prospective providers
- Discuss with unions, if applicable
- Enter into Information Sharing Agreements
- Adopt written plan document

3. IRS information available at:

<http://www.irs.gov/retirement/article/0,,id=172430,00.html>



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