

## Questions and Answers from the March 20, 2009 ftwilliam.com 403(b) webinar

### **Q 1: What if you have a plan year 7/1/08-06/30/09-what is the effective date?**

A 1: The effective date and adoption date deadlines under the final regulations / Notice 2009-3 do not depend on the plan year of the 403(b) plan. For most 403(b) plans, the plan document should be effective 1/1/09 (and should be adopted by 12/31/09).

### **Q 2: Is it true that if you have both the 403(b) catch up and the Age 50 catch up in the plan, if a participant is over 50, the special 403(b) catch up must be taken first and only one catch up is allowed within the plan year?.**

A 2: This is not quite right. If a plan allows both types of catch ups (and a participant is eligible for both), the special 403(b) catch up is taken and calculated first and then the age 50 catch up may be taken. Both can be used in one year.

### **Q 3: Does Ft William have a Universal Availability notice for 403b plan?**

A 3: ftwilliam.com does not currently have a universal availability notice. There are no content or form requirements for notifying participants of the ability to make elective deferrals -- although there is a requirement that participants be notified. A salary deferral agreement should be sufficient notice of the right to make elective deferrals.

A customer recently provided a sample universal availability notice and we think this would be valuable to other customers – so we plan to add this to our system. It should be available within the next few months (we will send out an email once it is available to let all retirement document customers know).

### **Q 4: Is it not more cost effective for a client to maintain one plan with 2 sources of contribution, rather than 2 separate plans.. is there really any advantage to having 2 separate 403(b) plans?**

A 4: I referenced in the presentation that it is possible to set up 2 mutually exclusive 403(b) plans under one employer and still meet universal availability....

I agree that it is simpler to maintain one plan and one document - and our system should be flexible enough to get all that you need into the checklist. However, I have talked with customers that have unique situations and need to maintain two separate documents.

In addition, many commentators have suggested one reason to have two separate, mutually exclusive 403(b) plans would be to avoid the 5500 audit requirements for large plans.

### **Q 5: Does the adp test apply to a nonprofit 403b plan or just the acp test?**

A 5: The ADP test will never apply to a 403(b) plan. 403(b) plans must meet universal availability instead. (Slide 10 notes that nonprofits must meet "all" nondiscrimination rules. This means nonprofits - that are not governmental and nor FICA Churches - must meet all nondiscrimination rules that apply to 403(b) plans: Universal Availability; 401(a)(17) (comp limits); 401(a)(4), (5), (17); 401(m) (ACP); and 410(b).)

**Comment 6: When I saw your slide last Friday listing 401(a)(26) the first thing I thought was "That's wrong". Then I dug around a little and found that although the code section is applicable to 403(b) plans, it would never come into operation because they're DC plans.**

Response 6: This comment came in over email after the webinar and I thought it was worth pointing out to webinar participants. 401(a)(26) deals with participation requirements for defined benefit plans. In general, 403(b) plans may not be defined benefit plans – with a limited exception for "TEFRA church" DB plans (see 1.403(b)-10(f)(2)). [Because the reference is likely to just be confusing (and there is not enough space to deal with it in detail), I have removed the reference from the nondiscrimination slide.]

**Q 7: Slide 13 indicates that distributions can be taken from deferrals if there is a severance of employment, death, disability or age 59 1/2. Are hardships from deferrals permissible? Your slide doesn't list hardship or inservice distributions for 403b plans. Are these permitted? Is there a difference between limited and full scope plans?**

A 7: Apologies. My slide should have addressed hardships. The slide has been updated to indicate that hardships may be taken from most accounts under the plan (elective deferrals and annuities – although there are some restrictions on the use of some accounts for hardships: may not be taken from custodial accounts that are not made up of elective deferrals and certain accounts if the plan utilizes a safe harbor contribution, for example).

Inservice distributions are allowed for 403(b) plans, although the type may be restricted dependant on the type of accounts the distributions are made from (elective deferral accounts may have inservice distributions after age 59-1/2 but not at an earlier stated age, for example).

There are some differences between the full scope and limited scope plans in how inservice distributions are handled. Both plans have options to allow hardship withdrawals and distributions from rollover accounts at any time. However, because the limited scope plans will only have elective deferrals, there are fewer options in the limited scope plan for inservice withdrawals. The general rule for distributions is set in the basic plan document, Sections 7.01 and 7.03 (pasted below) and checklist item **E.1** ("Does the Plan impose any limitations or conditions on distributions in addition to those specified in Section 7.01 and 7.03?") will allow you to modify the general rule if necessary.

Limited Scope Plan Section 7.01 and 7.03:

### **Section 7.01 Benefit Distributions**

At Severance from Employment or Other Distribution Event. Except as permitted under Section 5.06 (relating to excess Elective Deferrals), Section 8.02 (relating to withdrawals of amounts rolled over into the Plan), Section 8.01 (relating to hardship), or Section 10.02 (relating to termination of the Plan), distributions from a Participant's Account may not be made earlier than the earliest of the date on which the Participant has a Severance from Employment, dies, becomes Disabled, or attains age 59 1/2. Distributions shall otherwise be made in accordance with the terms of the Individual Agreements.

### **Section 7.03 Minimum Distributions**

Each Individual Agreement shall comply with the minimum distribution requirements of Treas. Reg. 1.403(b)-6.

**Q 8: Where in the document do we indicate the type of Funding Vehicle that will be used?**

A 8: We don't believe you need to specifically state which types of funding vehicles the plan will use in the Adoption Agreement. For both the full and limited scope documents, the Funds or Funding Vehicles under the plan are defined as "... Annuity Contracts, Custodial Accounts and Retirement Income Accounts specifically approved by Employer for use under the Plan." However, if you wish to specifically state this somewhere in the document, you may use a custom language appendix.

**Q 9: How does the 415 limit work for an employer that has a 401(k) plan and a 403(b) plan? Are the limits combined?**

A 9: PLEASE NOTE: there was a typo on Slide 15 that I did not catch during the presentation. Slide 15 has been updated. In general, a 403(b) plan and 401(k) plan provided by one employer will **not** have combined 415 limits. This is because, under 415, a 403(b) contract is deemed to be maintained by the participant (not the employer) (Treas. Reg. section 1.415(f)-1(f)(2)).

There is an exception to this rule if the participant "is in control" of the employer. A participant will be in control of the employer if they make up more than 50% of the directors or trustees of the organization or have the power to remove or designate more than 50% of the directors or trustees of the organization. (See Treas. Reg. sections 1.415(f)-1(f)(2), 1.415(a)-1(f) and 1.414(c)-5.) This may mean that for a typical nonprofit, the director will have a combined 415 limit with a 401(k) plan while other employees of the nonprofit will have a separate 415 limit for each plan.

**Q 10: If an employer maintains a 403b plan and wants to end it and replace it with a 401k plan, how is that accomplished.**

A 10: The employer has a number of options...

- 1) Terminate the 403(b) plan and concurrently start a 401(k) (employees could then rollover to the 401(k) if they choose);
- 2) Freeze the 403(b) plan and start a 401(k) plan; or
- 3) Maintain both a 403(b) and a 401(k) plan concurrently (employees could be eligible for just one or the other or both – assuming nondiscrimination testing can be met in both plans).

The problem with terminating the 403(b) plan (option 1) is that all assets in the 403(b) plan must be distributed upon termination. This is typically problematic for 403(b) contracts since the funding contracts may not permit the Plan Sponsor to determine when the contract is terminated and permit distribution of the assets. Under these circumstances, plan termination may not be possible and freezing the plan may be the only option.

Under options 2 and 3 the employees and/or the employer cannot move assets from the 403(b) to the 401(k). A transfer is not permitted from a 403(b) to a 401(k) (see Treas. Reg. section 1.403(b)-10(b)(1)(i)) and there is no distributable event for a rollover.

**Q 11: So 403b cannot terminate and offer the employees the option to roll in to the new plan?**

A 11: This is not accurate. If a 403(b) terminates, the assets must be distributed and employees may rollover their distributed accounts to a 401(k) (or they may keep it and pay tax on the distribution).

**Q 12: If a company sponsors a 403(b) and would like to terminate, they are going to freeze the plan and try to pay people out. If they start a 401(k) at the same time and employees roll money from the 403(b) to the 401(k), what happens if the 403(b) Plan cannot pay out all assets, meaning it can't really terminate? Have we then allowed employees to rollover funds from the 403(b) to the 401(k) Plan without a distributable event? What are the consequences of this?**

A 12: If the 403(b) attempts to terminate but has assets remaining that cannot be distributed, it is not terminated -- and if it is not terminated, then there is no distributable event for the employees' rollovers. This means an operational failure of the plan and a violation of the 403(b) distribution restrictions.

In general, the distributions must be returned to the 403(b) plan. See the EPCRS Rev. Proc. 2008-50 for more information. It would more prudent for a terminating 403(b) plan to hold the liquidation proceeds from annuities in a capital preservation mutual fund under a custodial account until all contracts are liquidated before paying out any money.