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SEPTEMBER NEWSLETTER



Operating Your 403(b) Plan in 2009 and Beyond

Last year, BCG completed the restatement of all 403(b) Plans on behalf of its clients to comply with the new 403(b) regulations issued in 2007 and made effective January 1, 2009. In early 2009, the IRS provided a one-year delay for adopting a compliant plan document. However, the date for complying with the remainder of the regulations was not delayed. Instead, plan sponsors must operate their plans in good faith compliance with the new regulations. Specifically, the following two conditions must be satisfied: (1) During 2009, the plan must operate in accordance with a reasonable interpretation of the statute, taking the new regulations into account; and (2) before the end of 2009; the employer must make its "best efforts" to correct any operational failure. This means, of course, that the employer must first take steps to identify any operational failures by reviewing plan operation, using the final regulations as a checklist. We suggest you examine the following items at a minimum.

Does the employer really make deferral opportunity universally available?

Eligible employers with 403(b) plans (including governmental public schools) have long been required to make the opportunity to defer compensation "universally available" to all employees from day one of their employment. The new regulations expand this by eliminating many of the exceptions that formerly applied. The only exceptions now left are for employees covered under another 403(b) arrangement or a 401(k) plan, nonresident aliens, students whose wages from the school are exempt from employment taxes, and employees who normally work fewer than 20 hours per week -- and the last two exceptions are subject to further limiting conditions. (Generally, the employee must work less than 1,000 in the prior year to take advantage of the 20-hour part time exception.)

The regulations emphasize that universal availability must exist in practice, not just on paper. IRS compliance questionnaires ask employers how the right to make elective deferrals is communicated to employees (for instance, through hiring packages or other communications). Employees should check their employee communication materials, since this will likely be a prime area for IRS investigation in future audits.

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dwhite@bcgbenefits.com, or
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Is the exempt organization now in a broader "controlled group?"

For benefit plan purposes, all employees of a controlled group of entities are treated as employed by one employer. The existing rules were based only on stock ownership or profits or capital interests, so tax-exempt organizations were rarely included in a controlled group except with their direct stock or for-profit subsidiaries.

The new regulations retain those rules but also added a new form of controlled group based on interlocking board (or trustee) relationships. A controlled group exists if 80 percent of the board (or trustees) of one tax-exempt organization are representatives of, or controlled by (through the power to elect or appoint), another organization. (Exempt organizations that have a common benefit plan for employees and regularly coordinate their activities may elect to be treated as a controlled group.)

The new controlled group rules mean the nondiscrimination tests for employer contributions must be performed taking all employees within the controlled group into consideration. They will also be used to determine when one employer is responsible for another employer's pension plan funding shortfall. Tax exempt organizations should review their governance structure and determine whether they are now in a controlled group with other entities and evaluate the consequences of that determination.

Note that the universal availability requirement is applied separately with respect to each controlled group member that has a 403(b) plan.

Who is responsible for the plan?

It is up to the employer to ensure that the 403(b) plan is tax compliant. The employer must see that applicable contribution limits and nondiscrimination rules (including universal availability) are satisfied. Other matters of particular concern to the IRS include ensuring that distributions permitted only on termination of employment occur only upon termination of employment, that hardship distributions occur only upon hardship, and that limitations on contract loans are properly applied taking into account all outstanding loans to the employee under all of the employer's benefit plans (including any 401(k) plan and all annuity contracts under any 403(b) plan). BCG can provide optional services where we assist the employer in satisfying these responsibilities.

Is an information sharing arrangement in place with vendors where required?

Administrative coordination becomes even more of a problem when employees have kept contracts or custodial accounts with vendors that are no longer receiving employee or employer contributions (or with vendors that never received contributions from the employer but to which the employee transferred his or her contract). The regulations require that these contracts must be treated as part of the plan for purposes of complying with the section 403(b) requirements. This means that loans and hardship withdrawals under these contracts must be taken into account in determining whether loans and hardship withdrawals from other contracts under the plan comply with the section 403(b) requirements.

The IRS provided some guidance on contracts held by former vendors. In general, contracts or accounts issued after December 31, 2004 by

Did You Know?

Form 5500 Deadline

Just a reminder that Form 5500 must be filed by October 15, 2009, if your plan year ended 12/31/2008.

Form 5500 must generally be filed by the last day of the seventh month following the end of the plan year, unless an extension has been filed. For calendar year plans, the deadline is normally July 31. Form 5500 or 5500-EZ must be filed with the Employee Benefits Security Administration (EBSA), not the IRS.

Form 5500 Filing Calendar

Plan Year End	Due Date
12/31/08	7/31/09
6/30/09	1/31/10

With Extension

Plan Year End	Due Date
12/31/08	10/15/09
6/30/09	4/15/10

By the way, your Plan Account Manager will cover this requirement during your annual plan account review.

For more information, please contact your Plan Account Manager at 800-524-401k, option 5.



vendors no longer receiving contributions under the plan will be treated as covered by the plan, even though the vendor is not currently "in" the plan, if the employer makes a reasonable, good faith effort to enter into an information-sharing arrangement with the vendor. Information that the employer must provide its former vendors includes notice of severance and hardship (or other distribution events), outstanding loans, information about the employees' other contracts needed for that coordination, and most importantly, who at the employer is the contact person for providing that information. The employer in return should ensure that these former vendors advise it about the individual's loans and distributions. No information sharing arrangement is required for contracts or accounts issued before January 1, 2005.

Information sharing about contracts or accounts of former employees is required only to the extent that if the individual requests a loan, the vendor must try to determine from the employer whether other loans to that individual are outstanding from other employer plans.

Is the plan an ERISA plan?

Governmental plans (including most public schools), and most church plans, are exempt from ERISA. Section 403(b) plans of nongovernmental employers that have employer contributions are subject to ERISA. Department of Labor "safe harbor" regulations exempt 403(b) plans that only allow employee deferrals, as long as employee participation is voluntary, only the employee has rights under the annuity contract or custodial agreement, the employer receives no compensation (consideration from the investment vendor) other than reimbursement of expenses, and the involvement of the employer is limited to certain specified activities.

According to the Department of Labor, it is possible for an employer to adopt a bare-bones plan incorporating the annuity contracts and providing for coordination among different investment vendors, without necessarily creating an ERISA plan -- provided the document correctly describes the employer's limited role and does not permit the employer to make any discretionary determinations.

Tax-exempt employers with elective-deferral-only 403(b) arrangements can, therefore, choose whether to live within the Department of Labor guidance and avoid ERISA (which may as a practical matter be difficult to do), or to accept regulation under ERISA. If the plan will be an ERISA plan, it can be structured to reduce the fiduciary liability exposures and other negative consequences of ERISA, while taking advantage of several of ERISA's favorable (for the employer) aspects, such as preemption of state law and deferential standard of judicial review. Employers must make it clear, however, from the face of the plan document, whether the plan is intended to be an ERISA plan or exempt from ERISA. Having an ERISA plan and not knowing it (and not having planned for it) can put the employer in a very difficult position.

Does the employer have the information needed for Form 5500?

Until this year, 403(b) plans that were ERISA plans nevertheless had only minimal financial reporting obligations on Form 5500. New Department of Labor regulations (independent of the new 403(b) tax regulations) effective for 2009 now impose on ERISA 403(b) plans the same reporting



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requirements applicable to 401(k) and other qualified plans. Notably, 403(b) plans with more than 100 participants must supply an audited financial statement as part of their filing. Form 5500 schedules themselves have been expanded to collect new and detailed information about plan arrangements with insurance companies and other service providers. These schedules may need to include information relating to annuity contracts held by former employees. ***Affected employers must engage an accountant for the plan, and ensure they have systems in place to obtain, track and report the required information.*** BCG recommends that clients engage an accountant well before the end of 2009 to assure that the required information will be available in a timely fashion.

Fortunately, the DOL recently provided relief with respect to assets held by vendors to whom contributions are not made after 2008. As long as the employee is fully vested in the account or contract and may enforce his or her rights in the account or contract without the employer's involvement, these assets need not be taken into account for purposes of the 5500 or accountant's opinion issued in connection with the audit. Moreover, if these are the only assets of an employee or former employee in the plan, he or she need not be counted as a plan participant, which may eliminate the need for an audit altogether.

Operating the Plan After 2009.

The good faith correction procedure for 2009 described above does not apply after December 31, 2009. However, the IRS operates an Employee Plans Compliance Resolution System that allows 403(b) plans (as well as qualified plans) to correct operational errors and receive an IRS letter of compliance with the payment of a modest fee.

BCG is available to help clients perform a self-audit of their plan or correct operational errors in compliance with IRS procedures. Contact your Plan Account Manager for assistance.