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Employee Benefit Plan Review

Ask the Experts

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NDT for 403(b) Plans

Q I work for a non-profit company. We currently have a 401(k) plan and are considering setting up a 403(b) plan. I am told that the 401(k) and 401(m) non-discrimination tests do not apply to 403(b) plans. Is that correct?

A That is partially correct. Matching contributions under 403(b) plans need to pass the "actual contribution percentage" ("ACP") test under Section 401(m) of the Internal Revenue Code (the "Code"). This requirement is no different from that of your 401(k) plan.

Unlike your 401(k) plan, however, a 403(b) plan is not required to pass the "actual deferral percentage" ("ADP") test under Section 401(k) of the Code. This is because 403(b) plans are subject to the "universal availability" rule of Section 403(b)(12) of the Code and not the ADP test. Under the universal availability rule, subject to only limited exceptions, all employees of the 403(b) plan sponsor must be permitted to participate in the 403(b) plan by making elective deferrals. As a result, a 403(b) plan cannot impose a one-year waiting period or age 21 requirement for eligibility.

Probably the most important of the limited exceptions to this rule is for employees who "normally" work fewer than 20 hours per week. These employees can be excluded from 403(b) plans without violating the universal availability rule. Treasury regulations set forth rules for determining when an employee "normally" works fewer than 20 hours per week and, therefore, falls within the exception to the universal availability rule.

ERISA Coverage of 403 Plans

Q How do I know if our company's 403(b) plan is exempt from the Employee Retirement Income Security Act of 1974 ("ERISA")?

A ERISA governs "pension plans" (in addition to welfare plans). In order to be a "pension plan," a plan must be "established or maintained" by an employer. Some 403(b) plans have so little involvement by the employer that the plans are not deemed to be established or maintained by the employer and, therefore, are not subject to ERISA and its requirements (such as filing Form 5500s and annual audits). The distinction between minimal involvement by an employer that allows a plan to be ERISA-exempt and sufficient involvement by an employer to cause the application of ERISA is not always clear.

However, because employers wanted some assurances as to the ERISA-exempt status of their 403(b) plans, the U.S. Department of Labor (the "DOL") enacted a safe harbor for 403(b) plans.[1]

To qualify for this safe harbor, the following conditions must be satisfied:

- Participation in the 403(b) plan must be completely voluntary;
- The rights under the annuity contract or custodial account underlying the 403(b) plan must be enforceable only by the participant, his or her beneficiary, or their authorized representative;
- The sole involvement of the employer in the 403(b) plan must be limited to certain acts specifically set forth in the DOL regulation, such as collecting

salary deferrals and forwarding them to the plan's vendors; and
- The employer cannot receive any compensation or other consideration related to the 403(b) plan, other than reimbursement of reasonable expenses incurred.

DOL guidance discussing the safe harbor makes a few things clear.

First, employer involvement in discretionary determinations such as loan, hardship, qualified domestic relations order ("QDRO"), and distribution determinations, will cause the 403(b) plan to be subject to ERISA.

Second, employer involvement to limit the number of vendors available under the plan will not run afoul of the safe harbor as long as there "generally" is more than one vendor available under the plan for participants' investments.

Third, adopting a 403(b) plan document in order to comply with the requirements of Section 403(b) of the Code will not automatically run afoul of the safe harbor.

Fourth, the safe harbor is just that – a safe harbor. Failure to satisfy the safe harbor does not automatically mean that the 403(b) plan is subject to ERISA; that determination is made on a case-by-case basis. Also, note that the safe harbor is available only for 403(b) plans funded solely by employee contributions. A 403(b) plan that allows employer contributions (such as matching contributions) is subject to ERISA.

New Minimum Required Distribution Age

Q Our company sponsors a 401(k) plan for employees. I read that the tax law that was just passed increased the age for taking minimum required distributions from 70½ to 72. When does this change take effect? What happens to plan participants who are age 70½ who have begun receiving minimum required distributions?

A The Setting Every Community Up for Retirement Enhancement Act of 2019 (the "SECURE Act") delayed the age at which individuals must begin taking minimum required distributions from certain retirement arrangements from age 70½ to 72 effective for individuals who attain age 70½ after December 31, 2019.

The Code requires that participants in certain retirement arrangements, including traditional individual retirement arrangements ("IRAs"), simplified employee pensions ("SEPs") IRA, SIMPLE IRAs (*i.e.*, "Savings Incentive Match Plans for Employees"), and 401(k), profit sharing, 403(b), 457(b), and other defined contribution plans, begin receiving minimum required distributions generally after they attain a certain age. The Code imposes a 50 percent excise tax on any minimum required distributions that are not distributed by the required distribution date.

Before the enactment of the SECURE Act, an individual who attained age 70½ generally was required to begin receiving minimum required distributions by April 1 of the calendar year following the calendar year in which the individual attained age 70½. Tax-qualified plans may permit participants (other than participants who own five percent or more of the company sponsoring the plan) to delay receiving minimum required distributions until the later of the minimum required distribution age or retirement. Plan participants who are five percent or more owners of the company sponsoring the plan are required to begin receiving minimum required distributions no later than April 1 of the calendar year following the calendar year in which the minimum required distribution age is attained, even if the individual has not retired.

The SECURE Act delayed the minimum required distribution age from 70½ to 72. This delay in age applies only to individuals who attain age 70½ after December 31, 2019. For purposes of the minimum required distribution rules, an individual attains age 70½ on the date that is six calendar months after the date the individual attains age 70. This means that an individual who attained age 70 on or before June 30, 2019 would be subject to the prior minimum required distribution age. An individual who attained age 70 on or after July 1, 2019 would be subject to the new rules.

Participants who attained age 70½ before January 1, 2020 would continue to receive minimum required distributions in accordance vwith the new minimum required distribution rules and plan terms. Unless your company's plan delays minimum required distributions for participants who are currently employed, participants who attained age 70½ in 2019 who delayed receiving minimum required distributions should begin receiving minimum required distributions on or prior to April 1, 2020.

The minimum required distribution rules are complex. Given the change in minimum required distribution age and certain other changes in the law, it is important to consult with your plan's legal counsel to determine how the changes in law will impact your plan in particular and the timing of plan amendments and participant communications to reflect the change. ❂

Note

1. *See* 29 C.F.R. Section 2510-3.2(f).

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