The Advisory Committee on Tax Exempt and Government Entities (ACT) proposes Recommendations to IRS for 403(b) Plans

In its report, the Employee Plans (EP) Subcommittee reviewed the current status of the 403(b) community, with specific focus on areas that have resulted in a lower level of compliance with the Code and created excess operational costs. In the EP Subcommittee's recommendations, it attempted to balance the needs of the 403(b) community with the Service's significant lack of resources. The EP Subcommittee's recommendations are intended to provide value to the 403(b) community and be logistically possible for the Service to achieve. The EP Subcommittee recognizes that many of the guidance recommendations made in this Report may go beyond the authority of EP, especially in light of the reorganization within the Service. It is the EP Subcommittee's hope that EP accomplishes what it can through soft guidance, such as web page clarity, and alert Chief Counsel to the recommendations made that go beyond EP's jurisdiction.

After spending significant time interviewing IRS personnel, 403(b) practitioners, and evaluating the comprehensive responses of the 403(b) community survey that the EP Subcommittee published, the following recommendations are presented for consideration by the Service:

Provide additional guidance on universal availability

- The EPCU should publish its findings as soon as possible from the Higher Education Institutions and the K-12 Schools projects in order to provide similarly situated employers with more relevant guidance.
- The Service should work to target its educational outreach to specific sectors of the 403(b) community, with special emphasis on the 403(b) public school community, who might not be aware of its website, the 403(b) Fix-It Guide and newsletters.
- The Service should address in the form of "soft" or other guidance on certain particularly troublesome specific issues such as:

  o In what manner can receipt of other benefits be conditioned on the employee making, or refraining from making, salary reduction contributions, if at all.

o How the 20 hours per week and 1,000 hours per year rules works in "real life," practical operation.

o The negative consequences that can ensue when an employer fails to provide the annual "effective opportunity" communication about a participant's ability to begin or change regular 403(b) and Roth 403(b) elective deferrals.

o The importance of the plan sponsor describing the terms of eligibility to participants.

o Employees in certain categories cannot be excluded if they satisfy the 20 hour per week or 1,000 hours thresholds and are, therefore, eligible to make salary reduction contributions regardless of job titles or classifications.

o What happens when the job classification of a member of an excludable class changes in the middle of a year?

Clarification for orphan contracts

- The Service should provide additional, practical guidance on the impact of operational violations under an individual's orphan contract on other contracts that the individual may have with the same employer.
- Clarify how pre-2009 frozen contracts issued to current employees **before** 2005 should be handled for compliance purposes.

Minimize 403(b) contract leakage

- The Service should consider issuing soft guidance that clarifies that a 403(b) vendor can act as the decision-maker where the employer no longer exists for rollover and other withdrawal/distribution purposes under contracts.
- The Service should issue guidance that requires issuers to provide reasonable advance notice to: (i) contract holders on the MRD requirements, and (ii) if the issuer does not have current contact information, make reasonable efforts to locate the contract holder.

Address current gaps in termination guidance

- Treasury should seek legislation addressing the problems or giving the Service authority to address the problems with 403(b) plan terminations.
- The Service should expand its webpage with information on terminating a 403(b) plan to recognize and address the many practical problems sponsors and practitioners face when they actually try to do a termination.
- The 403(b) Fix-It Guide should be expanded to address appropriate corrections for situations where the termination fails because all assets cannot be distributed.

Enhance EPCRS to accommodate the unique traits of 403(b) Plans

The Service should:

- Expand the SCP portion to include correction for common loan failures.
- Allow plan sponsors to use the DOL online earnings calculator to compute lost earnings.

- Develop additional schedules for the VCP filing to allow for correction of the most common 403(b) operational failures.
- Develop a separate VCP Appendix C, Schedule 1 and Schedule 2 for 403(b) plans.
- Reduce the filing fees for the 403(b) community, if only for a reasonable period of time, to allow compliance errors uncovered in the remedial amendment period to be discovered and corrected
- Implement a document amnesty program for any 403(b) plan sponsor that adopts a pre-approved plan so that no correction of prior documents is required.

The Service has made strides in its outreach activities to the 403(b) community including, but not limited to, webinars on various subjects and creating the 403(b) Fix-It Guide specific to the issues of these plans. Unfortunately, many plan sponsors either are unaware of their duties or are trying to avoid having any employer responsibility so that the plan will not be treated as an ERISA plan (with its resultant fiduciary and reporting requirements). Also, many plan sponsors do not have attorneys who are expert in 403(b) plans or staff dedicated to the plan. As a result, much of the Service's educational outreach may not be reaching the sponsors most in need of education.

It is the EP Subcommittee's opinion that the conflict between the desire for the plan sponsor to avoid ERISA status and the need for a responsible governing entity for the plan operation is a significant barrier to effective tax compliance for 403(b) plans. The EP Subcommittee, therefore, recommends that the Service address this matter in inter-agency discussions with the DOL to foster further research and possible guidance that would better define the rules governing the responsibilities of a plan sponsor of a 403(b) plan to satisfy the tax rules without making the plan an ERISA plan.

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Who We Are

Torrillo & Associates, LLC specializes in employee benefit plan audits including 401k audits, 403b audits, pension plan audits, and other retirement plan audits. We are licensed in 10 states including Pennsylvania, New Jersey, Delaware, New York and Florida. We are also able to practice in additional states that have passed firm mobility.

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- About
- Services
- Careers
- Clients
- Videos
- Blog
- FAQs
- Contact Us
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