

403(b) SERVICES AND SERVICE PROVIDER OPTIONS: REFERENCE GUIDE AND RESPONSIBILITY MATRIX

As a school prepares to comply with the new 403(b) final regulations, one of its first considerations is whether to contract with one or more 403(b) service providers and, if so, what type(s) of service provider to use. The purpose of the school contracting with one or more 403(b) service providers would be to utilize the expertise and resources of the service provider(s) to help the school meet its compliance responsibilities under the final 403(b) rules. For a summary of the school's compliance responsibilities for its 403(b) plan, see the accompanying chart titled *403(b) Responsibility Matrix* (Attachment A).

To assist a school in evaluating whether it will use one or more 403(b) service providers and what type(s) of service provider to use, some basic descriptions of typical types of 403(b) service providers are set out below. Please note that these descriptions are general in nature and no assumption is to be made from these descriptions about the services of any specific provider. Before contracting with any service provider, the school is cautioned to ask questions and carefully review the potential service provider's agreement in order to determine specific services provided under the agreement.

DESCRIPTIONS OF TYPICAL 403(b) SERVICE PROVIDERS

There are a number of different types of 403(b) services and service providers available. Some of the more common types of service providers are the following:

- (1) **Investment provider** – receives contributions from the school's 403(b) plan for investment in a product issued by the investment provider and generally (but not always) provides administrative services for accounts with the new investment provider. Some investment providers also offer third party administration services across investment providers (i.e., 403(b) plan documentation and operational compliance services) for 403(b) plans.
- (2) **Third party administrator (TPA)** – is a company that offers third party administration services (i.e., 403(b) plan documentation and operational compliance services) for 403(b) plans. If the TPA is not affiliated with any provider under the plan and does not have economic arrangements with one or more investment providers and/or other service providers under the plan, the TPA may be referred to as an "independent TPA."
- (3) **Common or volume remitter service** – is a service that might be provided by an investment provider, a TPA or other service provider under which the entity receives the total amount of 403(b) contributions from the

school each payroll period and calculates and forwards the portion of the contributions due to each investment provider in accordance with the allocation instructions that the school has provided. The service provider may or may not offer additional types of third party administration services (i.e., 403(b) plan documentation and operational compliance services).

- (4) **Investment consultant conducting investment review** – is a company that reviews the performance, quality, and cost of investments offered by 403(b) investment providers and recommends investment providers and products to offer under a 403(b) plan. This service provider may or may not offer additional types of third party administration services (i.e., 403(b) plan documentation and operational compliance services). If the investment consultant is not affiliated with any investment provider under the plan and does not have economic arrangements with one or more of the investment service providers and/or the TPAs, it may be referred to as an “independent investment consultant.”
- (5) **Legal counsel** – is an attorney advising a school, a TPA, and/or an investment provider. A school’s legal counsel, or an attorney with employee benefits expertise engaged by the school or the school’s legal counsel, might: (a) provide individually designed 403(b) plan documentation or review standardized 403(b) plan documentation offered by other types of 403(b) service providers; (b) review and negotiate service agreements with 403(b) service providers; (c) advise the school about its 403(b) plan document and operational compliance responsibilities; and (d) advise the school about applicable law requirements that must be satisfied. Legal counsel retained by a TPA or a provider generally might provide assistance, but cannot provide legal advice to a school, at least not without disclosing potential ethical conflicts. Legal counsel that is also an employee of a TPA or investment provider cannot provide legal advice to schools, in accordance with professional rules of legal ethics.

CENTRALIZED vs. DECENTRALIZED 403(b) COMPLIANCE UNDER THE FINAL 403(b) REGULATIONS: WHAT DOES IT MEAN?

A written plan is a new requirement under the final 403(b) regulations. One very important function of the written plan is to describe how plan compliance responsibilities will be allocated among the various parties to the plan, including the school, the participants, the investment providers, and any additional administrators. The regulations make it clear that compliance responsibilities may be allocated in any fashion the school desires, with one critical exception: they may not be allocated to the

participant. This translates into limitations on the extent to which the plan (including the school, the investment providers, and any additional administrators) may rely exclusively on information provided solely by the participant.

A loan request from a 403(b) participant provides an important example of how 403(b) plan administration will work under the new IRS rules. If a participant maintains accounts with more than one provider, under previous guidance each provider could rely on the participant’s representation that he or she did not have loans with other providers that would cause the requested new loan to exceed applicable limitations. Under the final regulations, such reliance would be tantamount to assigning compliance responsibilities to the participant, in much the same way as asking the participant seeking a hardship withdrawal simply to certify “I have a hardship.” As a result, someone on behalf of the plan now must determine whether the loan, when aggregated with other loans under the plan, and loans under other plans of the school, is within applicable limitations. The obvious next question is: what are a school’s options in allocating responsibilities to accomplish this? There are three primary alternatives, each of which can be structured to be consistent with the final regulations and the IRS model plan language:

Alternatives	What is Involved	Considerations
<i>Fully centralized compliance</i>	A single set of investment options under which the administrator (which in many cases may also be the investment provider) will hold all plan records and make all such loan and distribution determinations.	<ul style="list-style-type: none"> • May be attractive to larger employers. • May be unattractive to employees/collective bargaining unit. • May be fairly difficult for a school to utilize this alternative, because the plan will include not only this provider’s investment options, but also many pre-existing contracts and accounts maintained with additional providers that were active in the plan after 2004. As a result, distribution and loan rules would still need to be coordinated across all of these contracts and accounts. This coordination will, in most cases, require something different than fully centralized compliance.
<i>Fully decentralized compliance</i>	<ul style="list-style-type: none"> • Presumes that the 403(b) plan will have multiple providers, and that loans and distributions likely will also be subject to different requirements and limitations under the products of each provider • Each provider would be required to take 	<ul style="list-style-type: none"> • May be most attractive to <ul style="list-style-type: none"> ○ smaller employers, and/or ○ employers with fewer participants maintaining accounts with multiple providers • Providers are likely to be subject to various federal and state privacy restrictions as well as corporate privacy policies.

	<p>into account information about other accounts the participant maintains under the plan, as well as in other plans, in order to confirm the participant’s eligibility for a distribution or a loan, via:</p> <ul style="list-style-type: none"> ○ The school or the participant identifying the providers with which the participant maintains additional accounts, and this information could include information provided by the participant regarding existing loans, etc. ○ The plan provider receiving the loan or distribution request would then confirm with the other provider(s) the specific information relating to the accounts with the other provider(s), as part of the process to determine the participant’s eligibility for the loan or distribution. 	<p>Contract and account language which permits sharing information for plan compliance may be sufficient to address this concern. If not, participant consent to such sharing might be incorporated into appropriate plan forms.</p> <ul style="list-style-type: none"> ● Employers would need to freeze or eliminate providers refusing to share information, or restrict the types of transactions permitted from those contracts and accounts; if they are frozen or eliminated, employees would need to redirect contributions to remaining providers. ● There would potentially be less pressure from employees and collective bargaining units with multiple provider choices.
<i>Hybrid approach</i>	<ul style="list-style-type: none"> ● Combines a centralized plan-level determination with respect to distribution or loan requests, with continued decentralized administration of individual accounts with providers. It can involve collection of information key data: <ul style="list-style-type: none"> ○ in a centralized repository, as with the fully centralized approach, or ○ confirmation of key data for individual transactions, as with the fully decentralized approach. 	<ul style="list-style-type: none"> ● This alternative assumes that someone (generally, either a third party or a plan provider) would perform the initial plan-level determination and then forward to the plan provider where the participant’s account is maintained for processing consistent with the terms of the underlying contract or account. ● If a plan provider is designated to perform this function, the school will likely seek contractual assurances that data from this centralized plan compliance function is not permitted to be used by the plan provider (or affiliate), or any other provider, for marketing purposes.

	<ul style="list-style-type: none"> • May be performed by the school, third party, or plan provider (or an affiliate of a plan provider) to perform plan-level services. 	
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As employers evaluate the range of alternatives, they may be drawn to different alternatives based upon their individual circumstances. A very large school district with a large number of providers may prefer a fully centralized approach but select the hybrid approach because of the practical realities arising out of the final regulations. A small school district with 100 participants, only five of whom maintain accounts with more than one provider under the plan, may choose a fully decentralized structure because it represents the best use of the district's resources. And of course, the employer's selections may be significantly influenced by applicable state laws and restrictions and employee/collective bargaining unit concerns.

403(b) RESPONSIBILITY MATRIX – ATTACHMENT A

<u>Compliance Requirements; Related Resources:</u>	<u>General Summary:</u>
<p>Written Plan</p> <p>>Can use relevant portions of IRS model plan language. (Rev. Proc. 2007-71)</p> <p>>Can obtain specimen language from investment providers or TPAs.</p> <p>>ASBO will post sample plan document first quarter of 2008 with adoption agreement permitting selection of optional features.</p>	<p>The school must adopt and maintain (including subsequent plan design changes and legislative/regulatory updates) a written plan for its 403(b) program by the applicable deadline (generally January 1, 2009). The IRS will expect schools to operate in accordance with the terms of their written plan.</p> <ul style="list-style-type: none"> ○ Schools may meet this requirement by adopting a plan document using: <ul style="list-style-type: none"> ○ the IRS model plan provisions, ○ a plan document provided by its own legal counsel, or ○ a sample plan document provided by a TPA or an investment provider. Documents from all plan service providers should be investment provider-neutral and allow the school to define its plan. ○ If the school offers multiple 403(b) plans (note that this is different than one plan offering multiple investment provider options), generally a single written plan should be adopted for each separate plan, whether it includes one or multiple investment providers. ○ Schools must decide whether to have a single plan document or use the “binder clip” approach, aggregating multiple documents related to the operation of the 403(b) program. However, the IRS has indicated that if the 403(b) program has multiple investment providers, the school should strongly consider adopting a single plan document. ○ Schools must: <ul style="list-style-type: none"> ○ Decide what optional plan provisions (such as loans, hardships, transfers, rollovers in, employer contributions, Roth 403(b) contributions, qualified domestic relations orders) will be part of the written plan. Restrictions on common plan provisions are optional: there is no requirement that the school impose such restrictions. ○ Be aware of underlying investment product provisions to avoid conflicts. Plan may refer to benefits and restrictions in underlying investment products. ○ Identify which employees are eligible to participate, and in so doing create a road map for compliance or noncompliance with applicable nondiscrimination rules and requirements (see universal availability discussion below). ○ Identify, either in the plan document or by reference to a separate list, the specific products and providers available under the plan, and identify whether or not they permit new contributions or transfers/exchanges, if they hold amounts contributed under the 403(b) plan. <i>Recent IRS guidance clarified that, while this would otherwise include any contracts that ever received contributions under the 403(b) plan or program, certain</i>

<p>Written Plan (Cont.)</p>	<p><i>accounts with former providers as of 1/1/09 may be disregarded (e.g., accounts of former employees and beneficiaries and accounts of active employees with providers deselected before 2005). Reasonable good faith efforts must be made to include accounts with providers deselected after 2004, but before 2009. Once under the plan, a contract or account remains under the plan until distributed or transferred, even if that provider is later deselected from receiving new contributions or transfers.</i></p> <ul style="list-style-type: none"> ○ Remember to update your plan to reflect any subsequent operational changes (such as new investment providers, new optional plan features, or changes to existing optional plan features) and legislative/regulatory updates.
<p>“Universal Availability”</p> <p>>Sample employee notices can be obtained from legal counsel, investment providers, or TPAs.</p> <p>>The IRS model plan language permits the exclusion of employees who normally work 20 or fewer hours per week; however, some employers may choose to include all employees to avoid violations.</p>	<p>In general, in order to meet Code requirements that a 403(b) plan is nondiscriminatory, the school must permit any employee to make either pre-tax elective or Roth 403(b) contributions (if Roth 403(b) contributions are offered), or a combination of pre-tax and Roth 403(b) contributions, of at least \$200 per year. However, the school may exclude certain categories of employees (which are optional but must be applied consistently) from making such contributions to the 403(b) plan, including:</p> <ul style="list-style-type: none"> ● Individuals not willing to contribute at least \$200/year; and ● Individuals who “normally” work less than twenty hours per week. For new employees, the new measure will be whether that employee is expected to work at least 1,000 hours in their first year. For existing employees, the measure is whether that employee actually did work 1,000 hours in the previous year. <p>Eligible employees (regardless of whether they participate in the 403(b) plan or not) must be provided an annual notice of their eligibility to participate and to start, stop, or change their deferrals. The notice should be distributed in a manner designed to reach all employees.</p> <ul style="list-style-type: none"> ○ Schools may obtain actual or sample employee notices from available IRS guidance (if any), from its own counsel, or from a TPA or an investment provider. ○ The notice may be distributed by the school, either separately or along with other benefits materials or other school communications. A TPA or an investment provider may offer services to assist with the distribution to new or existing employees or both.

<p>Contributions, and Contribution Limitations</p> <p>>In 2008, salary reduction contributions are limited to \$15,500, plus, \$5,000 for employees age 50+ and a potential \$3,000 more for certain employees with 15 or more years of service.</p> <p>>TPAs and many of the investment providers can provide calculation support and monitor the limits among multiple providers.</p>	<p>The school determines the type(s) of contributions (including pre-tax deferrals, Roth contributions, school matching contributions, other school contributions, after-tax employee contributions) which can be made to the plan (see “Written Plan” above), and the procedures and timelines for enrollment and subsequent contribution changes (whether in hard copy or online).</p> <ul style="list-style-type: none"> ○ Actual or sample salary reduction agreements, as well as services for assisting with the enrollment and subsequent changes (either in hard copy or online) may be provided by a TPA or an investment provider. ○ Employees must be given at least one opportunity each year to stop, start, or change their deferrals; however, employees can be given more frequent opportunities to change their deferral elections (and have historically received more frequent opportunities to make changes). ○ Contributions must be forwarded to the underlying investment provider by the 15th of the month following the month they are withheld from the employee’s pay. If the TPA or an investment provider serves on the school’s behalf as a common remitter, receiving the total of contributions from the school and sending the appropriate contributions to each provider, the contributions still must be received by the investment providers by this deadline. ○ Many investment providers will monitor contribution limits with respect to accounts with that investment provider. Many TPAs and investment providers can also assist a school with monitoring contribution limitations across multiple investment providers under the plan.
<p>Loans</p> <p>>IRS model plan language provides optional language for inclusion of loans.</p> <p>>Investment providers can be required to confirm loan balances with other investment providers, or services to monitor loan limits across multiple vendors and multiple plans can be available from a TPA or an investment provider.</p>	<p>The school must decide whether loans will be allowed in the plan and prepare the written plan accordingly. See “Written Plan.” Loans are subject to specific requirements governing the amount which may be borrowed (looking at both the employee’s vested account balance across all investment providers that the school offers and in all plans sponsored by the school and whether that employee has any outstanding loans from any of those providers or in other plans) and the requirements for repayment frequency and timing.</p> <ul style="list-style-type: none"> ○ Many investment providers will monitor loan limitations with respect to accounts with that investment provider. Many TPAs and investment providers can also assist a school with monitoring loan limitations across multiple investment providers under the plan. In addition, one model for decentralized compliance would require each provider to confirm loan balances with other investment providers in the plan before approving a loan under the provider’s contract or account.

<p>Distributions</p> <p>>School can require that the investment providers verify employment information before permitting a distribution.</p> <p>>Many investment providers and TPAs can monitor withdrawals and distributions among multiple providers.</p> <p>>Providers can be required to notify the school following a hardship withdrawal for the suspension of deferrals to all plans.</p>	<p>According to the Code, distributions of employee deferrals (including Roth 403(b) deferrals) are only available upon satisfying one of the following: attaining age 59 ½, severance from employment, death, disability, or financial hardship. Different restrictions may apply to school contributions or nonelective employee contributions. Additional distribution restrictions may be imposed by the plan.</p> <ul style="list-style-type: none"> ○ Many investment providers will monitor distributions from accounts with the investment provider for compliance with these restrictions. Many TPAs and investment providers can also assist a school with monitoring for these restrictions across multiple investment providers under the plan. ○ Under the final regulations, hardship withdrawals will require documentation of the hardship and a provider cannot rely solely on the employee’s representation of the existence of a specific qualifying event. ○ Schools who elect one of the alternatives under the IRS 401(k) hardship safe harbor rules are not required to confirm that there are no other assets available to meet the hardship need; however, deferrals to all salary reduction plans must be suspended. Thus, many plans will require a cessation of deferrals to plans of the school for 6 months after that employee takes a hardship withdrawal from the 403(b) plan.
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Transfers and Exchanges

>The school can review and authorize exchanges or delegate that responsibility to the investment providers or a TPA.

>To be allowed, plan-to-plan transfers must be permitted in both the transferring plan and the receiving plan document.

Transfers within the plan (or to investment providers under an information sharing agreement) are called “exchanges.” Transfers to another plan are called “transfers.”

If exchanges are permitted under the written plan, then exchanges may be made to investment products who are receiving contributions under the plan or, subject to a requirement for an information sharing agreement, to a provider outside of the plan. Information sharing agreements are required to be between the school and the investment provider. If a school wants to permit a third party to enter into such agreements with the investment provider on the school’s behalf, the school will need to provide proper authorization to the third party to enter into the agreement. The plan may impose limitations, such as only permitting exchanges among investment providers who are receiving contributions under the plan. A school may rely on one or more of its investment providers under the plan or a third party to administer restrictions on exchanges or it may choose to review and approve each exchange request.

- Contracts or accounts established with a prior exchange, on or before September 24, 2007, will be considered “grandfathered” contracts and accounts and not made part of the plan; however, if a new contribution or a subsequent exchange is made into the contract, the referenced grandfathering would cease.
- Many investment providers will monitor exchanges and transfers into and out of that investment provider’s products.
- Many TPAs and a number of investment providers will agree to monitor such exchanges and transfers across providers under the plan.
- Improper exchanges made between September 25, 2007 and January 1, 2009 can be corrected through a “re-exchange” to an investment provider included in the school’s plan (either through an information sharing agreement or because ongoing contributions are being received) provided the re-exchange is completed on or before June 30, 2009.

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