



SMALL BUSINESS & NONPROFIT CLINIC

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**November 11, 2008**  
**403(b) Plans and ERISA Compliance**

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As a result of working with Elsie Publishing, a 503(c)(3) organization, on 403(b) plan issues, I have learned the following points that may be helpful for other clinicians advising on this topic.

Beginning January 1, 2009, all organizations with a 403(b) plan must put the plan in writing. It is the new regulation requiring a written plan that brought Elsie Publishing to the clinic for assistance. For smaller organizations with few employees, this can be achieved easily by gathering together copies of the 403(b) account contracts of each employee and stapling them together with a cover sheet.<sup>1</sup> Those employers with one plan provider may request assistance from the provider in drafting the plan.

A 403(b) plan is a retirement savings plan that can be used by tax-exempt organizations. It operates like a 401(k) plan used by for-profit businesses. A 403(b) plan allows employees of the exempt organization to contribute pre-tax dollars to the retirement savings account, up to a maximum annual contribution amount. These employee contributions are known as "elective deferrals." Employers may opt to contribute to employees' 403(b) accounts in addition to the employees' elective deferrals. Employer contributions are called "nonelective contributions."

For 2008, the Internal Revenue Service ("IRS") allows a maximum amount for contribution of \$15,500. However, employees with 15 years or more of service with a qualified employer are eligible for the "15-Year Rule," which increases the maximum allowed annual contribution by up to \$3,000 (for tax year 2008). Qualified employers include "a public school system, hospital, home health service agency, health and welfare service agency, church, or convention or association of churches (or associated organization)."<sup>2</sup>

Many employee retirement savings plans are subject to the Employee Retirement Income Security Act ("ERISA"), administered by the Department of Labor ("DOL"); however, a tax-exempt organization with a 403(b) plan is not required to comply with ERISA if it meets certain conditions. First, the plan must be available to all employees and include "employees of tax-exempt organizations established under section 501(c)(3) of the Internal Revenue Code, employees of public school systems who are involved in the day-to-day operations of a school, employees of cooperative hospital service organizations, civilian faculty and staff of the Uniformed Services University of the Health Sciences ("USUHS"), employees of public school systems organized by Indian tribal governments, and certain ministers."<sup>3</sup>

Second, the employer may not be involved in administering the plan. In practice, an employer is only allowed to provide employees with sales brochures about the accounts the plan providers offer to its employees. It cannot be involved in advising employees about the various plan providers or accounts, assist in administering any contract terms such as loans from the account, or, most importantly, change any terms of an existing plan provider account. Finally, only two types of accounts may be offered by plan providers for tax-exempt organizations: annuity contracts and custodial accounts invested in mutual funds.

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<sup>1</sup> IRS representative in Employee Plans provided this information by phone.

<sup>2</sup> <http://www.irs.gov/publications/p571/ch04.html#d0e1860>

<sup>3</sup> <http://www.irs.gov/publications/p571/ch01.html#d0e427>

A tax-exempt organization with a 403(b) plan may also offer a Simplified Employee Pension plan (“SEP”) to its employees. However, only a Prototype SEP plan may be combined with a 403(b) offering. Prototype SEPs are a specialized type of SEP not offered by all investment management companies. Banks are the most likely source for a Prototype SEP. The more common type of SEP, a 5305 SEP, cannot be offered by an organization with a 403(b) plan by IRS mandate.<sup>4</sup>

You must contact both the IRS and the DOL when working on legal issues related to employee retirement plans because of the interplay between IRS regulations and ERISA.

Below is some helpful contact information when seeking answers on 403(b) plan issues.

- IRS Business Division: (800) 829-4933
- IRS Employer-side Retirement Plans: (877) 829-5500, or e-mail RetirementPlanQuestions@irs.gov
- Department of Labor – Office of Regulations and Interpretations: (202) 693-8500

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<sup>4</sup> IRS representative in Employee Plans provided this information by phone.