COMMENTS CONCERNING CODE SECTION 403(b)
REGULATIONS PROJECT

The following comments (the “Comments”) are the individual views of the members of the Section of Taxation who prepared them and do not represent the position of the American Bar Association or the Section of Taxation.

These Comments were prepared by individual members of the Committee on Employee Benefits of the Section of Taxation of the American Bar Association (the “Section”). Principal responsibility was exercised by Robert Abramowitz. Substantive contributions were made by Kurt Lawson, Amy Null, Kristi Cook, James Kemper, Mark Dray, David Powell, David Raish and David Pratt. These comments were reviewed by David Mustone, Taina Edlund and Thomas R. Hoecker of the Section’s Employee Benefits Committee, T. David Cowart of the Section’s Committee on Government Submissions and Thomas A. Jorgensen, Council Director for the Employee Benefits Committee.

Although members of the Section who participated in preparing these Comments have clients who would be affected by the federal tax law principles addressed by these Comments, or have advised clients on the application of such principles, no such member (or the firm or organization to which such member belongs) has been engaged by a client to make a government submission with respect to, or otherwise influenced the development or outcome of, the specific subject matter of these comments.

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COMMENTS

EXECUTIVE SUMMARY

These Comments offer suggestions regarding several areas under section 403(b) of the Internal Revenue Code (the “Code”) where we believe that guidance is needed. Over the years, section 403(b) of the Code has changed significantly due to amendments by several statutes, including the Tax Reform Act of 1986 and the Economic Growth and Tax Relief Reconciliation Act of 2001. Thus, existing guidance has, in certain instances, become obsolete. In other instances, more definitive guidance simply is needed.

Thus, we offer the following comments and recommendations which we hope will aid in the development of any additional guidance that is promulgated:

1. Any proposed regulations should allow for the termination of 403(b) plans in a manner similar to that permitted under the final regulations under section 457 of the Code.

2. Any proposed regulations should consider retention of the safe harbors under Notice 89-23, 1989-1 CB 654. Retention of the safe harbors would be especially beneficial for small charities.

3. In applying the nondiscrimination rules, imputation of permitted disparity should generally be permitted. Aggregation of 403(b) plans should be permissive, not mandatory. Both approaches are consistent with the rules applicable to qualified plans.

4. Because of the difficulties inherent in determining whether a controlled or affiliated service group exists in the not-for-profit and governmental environments, any proposed regulations should consider applying the universal availability requirement imposed by section 403(b)(12)(A)(ii) only to the common law employer rather than the controlled or affiliated service group.

5. The definition of excludable employees in Notice 89-23 should be retained and, in certain limited circumstances, expanded. The expanded definition generally conforms to the rules applicable to qualified plans, while recognizing the various statutory exclusions applicable to 403(b) plans.
The following are suggested topics for guidance under regulations addressing section 403(b) of the Internal Revenue Code (the “Code”). In some sections, recommendations are made as to what the guidance should be.

I. Termination of 403(b) Plans

Background:

Tax-sheltered annuity plans under section 403(b) of the Code are subject to early distribution restrictions similar to 401(k) plans. Unlike 401(k) plans, however, the termination of a 403(b) plan is not a statutory distribution event. Custodial 403(b) accounts may not be distributed until “the employee dies, attains age 59½, has a severance from employment, becomes disabled or in the case of contributions made pursuant to a salary reduction agreement encounters financial hardship.” Code § 403(b)(7)(A)(ii). The same restrictions apply to non-custodial annuity contracts, but only with respect to distributions attributable to employee deferrals. Code § 403(b)(11). Even if plan termination were a distribution event, it is still not clear, as discussed below, that a sponsor could force distributions in excess of $5,000 without participant consent.

Thus, an employer can freeze a 403(b) plan but often cannot, as a practical matter, terminate the plan even, perhaps, if all participants have experienced distribution events. This is not a significant problem for non-ERISA 403(b) plans, since the employer’s involvement is minimal and there is no Form 5500 filing requirement. For example, section 403(b) plans with minimal employer involvement may be exempt from Title I of ERISA pursuant to DOL Regulation § 2510.3-2(f). At the same time, government plans and non-electing church plans are exempt under section 4(b) of ERISA. All that would be required here is that the accounts or contracts continue to be held by participants or by the provider, which is typically happy to do so.

However, for 403(b) plans subject to ERISA, the employer must continue to comply with all new law changes and file Forms 5500, even though participants may have ceased to accrue benefits under the plan and/or the employer has gone or is going out of existence. This can be quite common today—for example, as a result of the acquisition of a tax-exempt hospital by a for-profit hospital. In such cases, plan contributions are often no longer being made as the successor employer may not be eligible to maintain a successor 403(b) plan, but the plan must be continued until all participants experience a distribution event. Even then, until the individual attains age 62 or, if later, the plan’s normal retirement age, distributions in excess of $5,000 may not be forced. Where the tax-exempt entity continues in existence as a charitable foundation and the new employer will not assume the plan, the foundation is burdened by having to maintain a frozen plan indefinitely.

The restrictions on 403(b) terminations are understandable from an historical perspective, since many 403(b) arrangements were not employer-sponsored (and therefore not subject to ERISA), and tax-exempt entities were involved in fewer “merger and acquisition” transactions than they now are. In addition, there were not as many tax-deferred rollover options as there are now.

It is submitted that with the loosening of the rollover rules and the recently proposed changes in the regulations under section 457 of the Code, there is no longer a public-policy reason for restricting 403(b) terminations. So long as participants’ deferrals can be protected—i.e., an
annuity purchase option would be provided where a plan provides for annuities—and essential ERISA rights are protected, employers should not be forced to maintain frozen 403(b) plans indefinitely. In short, there no longer seems to be any legitimate reason to permit plan sponsors to terminate other common types of employer-sponsored tax qualified arrangements, but not a 403(b) plan.

Recommendations:

1. The proposed regulations should permit 403(b) terminations along the lines permitted under the recently finalized regulations under section 457 of the Code.

2. In the alternative, the Service should develop guidance in coordination with the Department of Labor on whether and how a plan sponsor could cause a plan to cease to be subject to Title I of ERISA.

Discussion:

1. A blueprint for this approach is found in the recent regulations under section 457 of the Code, which provide for termination of 457(b) plans, even though section 457, like section 403(b) of the Code, does not include plan termination as a distribution event. Treasury regulation section 1.457-10(a), Miscellaneous provisions, provides in relevant part as follows:

   “(a) Plan terminations and frozen plans.

      (i) In general. An eligible employer may amend its plan to eliminate future deferrals for existing participants or to limit participation to existing participants and employees. An eligible plan may also contain provisions that permit plan termination and permit amounts deferred to be distributed on termination. In order for a plan to be considered terminated, amounts deferred under an eligible plan must be distributed to all plan participants and beneficiaries as soon as administratively practicable after termination of the eligible plan. The mere provision for, and making of, distributions to participants or beneficiaries upon a plan termination will not cause an eligible plan to cease to satisfy the requirements of section 457(b) or the regulations.

      (ii) Plan termination. As an alternative to determining the tax consequences to the plan and participants under paragraph (a)(2)(i) of this section, the employer may terminate the plan and distribute the amounts deferred (and all plan assets) to all plan participants as soon as administratively practicable in accordance with paragraph (a)(1) of this section. Such distribution may include eligible rollover distributions in the case of a plan that was an eligible governmental plan. In addition, if the employer is a state, another alternative to determining the tax consequences under paragraph (a)(2)(i) of this section is to transfer the assets of the eligible governmental plan to an eligible governmental plan of another eligible employer within the
same state under the plan-to-plan transfer rules of paragraph (b) of this section."

The Service should consider formulating a regulation providing for the termination of 403(b) plans that are subject to Title I under rules similar to the above and those under Treasury regulation section 1.411(a)-11(e)(1). As was the case under section 457 of the Code, section 403(b) does not provide a statutory termination mechanism. Yet, because compelling circumstances may exist when an employer wishes to terminate a plan, an approach was developed under the regulations under section 457 of the Code to recognize an employer’s need for limited flexibility. We would suggest that this approach may also be applied to 403(b) plans.

2. In the alternative, if the Service is unable to provide by regulation for distribution of 403(b) accounts or contracts upon plan termination, it is recommended that the Service coordinate with the Department of Labor to provide further guidance on whether and how a plan sponsor could cause a plan to cease to be subject to Title I of ERISA, and thereby release the employer of the ongoing burden of administering a frozen 403(b) plan. Support for this position is found in Revenue Ruling 90-24, 1990-1 CB 97, which provides that “[t]here is no actual distribution within the meaning of section 403(b)(1) of the Code where funds are transferred from one section 403(b) investment to another section 403(b) investment if the transferred funds continue after the transfer to be subject to any distribution restrictions imposed on them prior to the transfer by section 403(b)(11) or section 403(b)(7)(A)(ii).” For example, it might be possible to transfer an annuity to an approved custodian (or the participant) so that the rights of participants and their spouses would be preserved, but the annuity would cease to be part of an ERISA-covered program.

II. Nondiscrimination Rules

Background:

Section 403(b)(1)(D) of the Code imposes a nondiscrimination requirement on 403(b) plans other than church plans. Section 403(b)(12)(A)(i), added by the Tax Reform Act of 1986, provides that the nondiscrimination requirements are satisfied if, in the case of contributions other than salary reduction contributions, a 403(b) plan satisfies the nondiscrimination requirements of sections 401(a)(4), (5), (17) and (26), 401(m) and 410(b) of the Code in the same manner as plans described by section 401(a) of the Code. Under section 403(b)(12)(A)(ii) a plan providing for salary reduction contributions must permit all employees of the organization to make salary reduction contributions of more than $200. These requirements, other than those of section 401(a)(17) of the Code, do not apply to governmental plans.

Notice 89-23, 1989-1, C.B. 654, currently provides limited guidance regarding the application of the nondiscrimination requirements applicable to 403(b) plans. Notice 89-23 provides a series of safe harbors for the satisfaction of the nondiscrimination rules. Three safe harbors apply for satisfaction of the section 403(b)(12)(A)(i) nondiscrimination rules applicable to contributions other than salary reduction contributions and matching or employee contributions subject to the
requirements of section 401(m) of the Code. These safe harbors are applied on an aggregated basis, including all 403(b) programs of the employer to which the employer makes contributions and, if the employer desires, any one or more of its plans described by section 401(a), 403(a), 414(d) or 414(e) of the Code. Permitted disparity may not be imputed under the safe harbors. In addition, for purposes of the 403(b)(12)(A)(i) safe harbors, the employer under the controlled group rules of sections 414(b), (c), (m) and (o) is deemed to be the entity contributing to or maintaining the 403(b) plan and each entity in the group may contribute to or maintain a 403(b) plan. Notice 89-23 modifies these controlled group rules by providing special rules based on the direct or indirect control of an entity due to overlapping membership of its governing body by a contributing employer or receipt of at least 80% of its operating funds. However, with respect to the universal availability requirement of section 403(b)(12)(A)(ii), these controlled group rules do not apply.

In applying the safe harbors, Notice 89-23 provides that certain employees, in addition to those excluded under section 403(b)(12), may be excluded from consideration in applying the safe harbors.

Recommendations:

1. We recommend retention of the safe harbors under Notice 89-23. Retention of the safe harbors would ease the administrative costs of the many 403(b) plans of small charities that cannot afford actuaries or attorneys to conduct necessary coverage and nondiscrimination testing.

2. There is no need to prohibit imputation of permitted disparity since the only employees not covered by social security are state and local government employees, and plans maintained by those employers are exempt from the nondiscrimination requirements for nonelective contributions under section 403(b)(12)(A)(i) of the Code.

3. We recommend that, consistent with the qualified plan rules, aggregation of 403(b) plans should be permissive.

4. We recommend that the universal availability requirement under section 403(b)(12)(A)(ii) of the Code be applied only to the common law employer or distinct operating units of the employer, and not to any controlled or affiliated service group, due to the difficulties inherent in determining the members of such group and operational difficulties. Many tax-exempt employers have maintained separate benefit structures, separate benefit programs, and separate payrolls for distinct operations (e.g., separate campuses of a single university), and it would be a hardship to extend this requirement to all employers in the controlled or affiliated service group or to all operating units. These distinctions were recognized in Part III of Notice 89-23 and should be continued. Section 403(b) is not listed in sections 414(b), (c), (m), or (t), which is further support for this position.

5. In addition to the extension of the exclusions set forth in Notice 89-23, it would be helpful to have additional guidance on the exclusion under section 403(b)(12)(A)(ii) of
the Code, which authorizes an exclusion for employees who normally work less than 20 hours per week (Notice 89-23 extended this exclusion to any of the safe harbors contained in the Notice).

i. One possible approach would be to permit an employer to use a “look-back” for some prior period (such as six or twelve months) to determine whether this standard is met.

ii. Alternatively, the regulations might provide that a “regular” schedule could be relied upon.

iii. Similarly, plan sponsors should be permitted to continue to allow salary reduction contributions, for a brief period of time, by employees whose work schedules change to less than 20 hours per week. Such relief is necessary since plan sponsors have difficulty in contemporaneously identifying changes that would lead to excludability. A similar approach can be adopted for other categories of exclusion, if such categories are recognized by the proposed regulations.

iv. Another approach would be for the proposed regulations to permit determinations of whether the minimum service requirement is met to be made using the ERISA “year of service” eligibility rules.

v. In addition to retaining the separate testing alternative of Notice 89-23, separate testing of other classes of excludable employees for purposes of both 403(b)(12)(A)(i) and (ii) (besides those not meeting the plan’s minimum age and service requirements) would be helpful in that it would encourage employers to include employees in their plans.

6. Because of the way that the exemption for church plans is worded, some church 403(b) plans will be exempt from ERISA, including the ERISA vesting requirements, but still be subject to section 403(b)(12) of the Code. Ironically, though, some of the requirements that do not apply to church plans under section 401(a) would apply to them indirectly via section 403(b). If a section 401(a) plan is taken into account in testing a church 403(b) plan, there could be a significant difference in the vesting schedules that apply to benefits under the two plans, which would be taken into account in determining whether they provide comparable benefits.

Discussion:

1. In general

We would urge the retention of safe harbors similar to those contained in Notice 89-23. Retention of such safe harbors would especially encourage smaller charitable organizations to continue providing benefits for their employees by limiting the administrative costs of nondiscrimination testing. Many of these charities have historically adopted plans with age-
based or service-based contribution rates or other provisions that make the safe harbors under section 401(a)(4) of the Code unavailable. Streamlined nondiscrimination testing by retaining the Notice 89-23 safe harbors would help preserve longstanding benefit delivery mechanisms.

However, regardless of whether safe harbors are retained, we would suggest that the mandatory aggregation of 403(b) annuity programs should not be required in testing nondiscrimination under section 403(b)(12)(A)(i) of the Code.

Likewise, we would suggest that any proposed nondiscrimination rules permit the imputation of permitted disparity. Notice 89-23 provides that, in determining whether an aggregated 403(b) annuity program satisfies the available safe harbors, an employer may not take into account (i) social security benefits or contributions that may otherwise be taken into account under sections 401(a)(4) and 401(a)(5) of the Code, or (ii) permitted disparity under section 401(l) of the Code. While, as noted by the legislative history of section 403(b)(12) of the Code, imputation of permitted disparity is prohibited with respect to employees not covered by Social Security, there is no reason to prohibit the imputation in the case of other employees. Other than employees of state and local governments, employees of employers maintaining 403(b) plans are covered by social security. Thus, in keeping with the rules applicable to qualified plans, imputing disparity should be permitted.

2. Universal availability

We believe that any proposed regulations should recognize the difficulties inherent in determining the identity of controlled group members based on the principles of section 414 of the Code and apply the universal availability requirement solely to the employees of the common law employer. It is more difficult for 403(b) plan sponsors to determine what entities are included in their controlled groups than it is for for-profit employers, since governmental and section 501(c)(3) entities typically have no stock and control is difficult to determine in the absence of stock. In many circumstances, nominal board-level control by one tax-exempt entity of another does not mean that the entities are truly integrated or are under common control. For example, the minority members may exercise certain veto powers, and there may be no mechanism (as there typically would be in the for-profit arena) to remove the minority board members. Unlike section 403(b)(12)(A)(i), section 403(b)(12)(A)(ii) of the Code does not explicitly apply the qualified plan nondiscrimination rules to salary reduction contributions under a 403(b) plan. Moreover, since section 403(b) is not listed in, and hence, not directly subject to, sections 414(b), (c), (m) or (t) of the Code, there is legal support for the position that controlled and affiliated service group rules need not apply. Therefore it would be helpful to retain the position set forth in Notice 89-23 and clarify that the universal availability requirement need only be applied to common law employees of the employer.

Likewise, it would be helpful to have better understanding of what an employer’s obligations are regarding universal availability - for example, must the employer give written notice to employees who may contribute, or would it be sufficient if the employer simply permitted an employee to request to make a deferral without the employer adopting an on-going communication policy for all employees?
3. Excludable employees

We believe that the statute excludes too few categories of employees. Application of the nondiscrimination requirements of section 403(b)(12) of the Code would be further simplified if the expanded definition of excludable employees contained in Notice 89-23 were retained. Many of the additional categories of excludable employee that were set forth in Notice 89-23 are needed to make the rules parallel the rules for section 401(a) plans or to reflect the nature of 501(c)(3) organizations.

Moreover, in applying the exclusion for employees who normally work less than 20 hours a week in determining whether the universal availability requirement is satisfied, in order to lessen the burdens of plan administration, limited flexibility regarding the application of exclusion to employees who normally work less than 20 hours would greatly simplify the determinations regarding excludable employees. The ability of an employer to adopt a “look-back” approach, akin to the ability of an employer to look to prior year compensation under section 414(q) of the Code, or, alternatively, adopt a “regularly scheduled to work” approach or an averaging approach would alleviate the burdensome nature of close monitoring of hours without harming employees. Allowing flexibility with respect to employees whose hours drop below 20 hours per week from time to time would also serve to alleviate inadvertent eligibility errors without harming plan participants.

Likewise, in determining hours of service for purposes of the minimum age and service exclusion, we would suggest that 403(b) plans be allowed to elect to apply the same ERISA hour of service rules that apply for qualified plans. Since the minimum age and service exclusion is to be applied in accordance with the standards set forth under section 410(a)(1) of the Code, utilization of these rules would be appropriate.

Further, we would urge the retention and expansion of the separate testing alternative to the age and service rules set forth in Notice 89-23. Expansion of the separate testing alternative would serve to encourage employers to provide benefits by balancing the need to provide benefits to a broad spectrum of employees with the administrative complexities created by providing such opportunities to limited service employees.

III. Post-Employment Employer Contributions

Background:

Prior to EGTRRA, the IRS, in two private letter rulings, permitted two employers to make post-employment contributions into 403(b) accounts of retirees as part of early retirement incentive programs. The rulings set forth the conditions necessary to qualify such contributions under section 403(b) of the Code in effect at the time. Because of the interplay between the definition of includible compensation under section 403(b)(3) of the Code and the special rules for 403(b) plans under section 415(c)(4)(B) of the Code, the employers could make contributions not to exceed $15,000 per year for former employees who were eligible to use the “B” election under

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1 PLR 9625043 and PLR 9233030
section 415(c)(4)(B). In addition, the PLRs permitted the contributions to be made for a period not to exceed five years.

EGTRRA effectively codified these two PLRs by modifying section 403(b)(3). The new section 403(b)(3) extended the definition of “includible compensation” for a five (5) year period following an individual’s severance from service with the employer. From a practical perspective, employees were deemed to have “includible compensation” over that five-year period in an amount equal to the includible compensation earned during the final period of service that counts as a year of service under section 403(b)(4). Thus, in each of the five years following severance from service with their employer, each terminated employee would be deemed to have a contribution limit under section 415(c)(1) equal to the lesser of $40,000 or their final year’s includible compensation. Accordingly, section 403(b)(3) now permits all eligible employers to make post-employment contributions for former employees for a five-year period following the employees’ severance from service.

There are also more recent PLRs, primarily issued to governmental employers, that permit employers to make post-employment contributions into 403(b) plans (as well as 401(a), 457(b) and 414(h) plans) based on the value of each employee’s accumulated per diem benefits, such as sick days, personal leave days and vacation days. The guidance focused on the requirements necessary to avoid “constructive receipt” of the employer contributions, thus “converting” previously taxable benefits into tax-deferred nonelective employer contributions.

However, aside from these PLRs, there is a little guidance for employers and practitioners to support the new post-employment contribution opportunities.

**Recommendations:**

It would be helpful if future guidance could address some of the following issues:

1. **Nondiscrimination Testing Issues.** Since there are no exclusions from the nondiscrimination requirements of section 403(b)(12)(A), must contributions from employers (other than governmental organizations and churches under section 3121(w)(3)(A)) satisfy the nondiscrimination requirements of section 403(b)(12)(A)(i)? Is this considered to be a separate plan for retirees only? How is the “retiree” plan tested for nondiscrimination purposes? Will the plan satisfy the nondiscrimination requirements if it is available on equal terms to all retirees, or will it be tested with the 403(b) program that is available to active employees? Is each retiring group in each year a separate program for testing purposes? If a disproportionate number of highly compensated employees retire in the same year, will the retiree program fail to satisfy the nondiscrimination tests? Would the result be different if the benefit were negotiated subject to a collective bargaining agreement?

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2 PLR 9827040 and PLR 200311043 (401(a) plan), PLR 200301032 403(b) and 457(b) plan, PLR 200302032 (401(a) or 403(b) plan), PLR 200302032 (for a 501(c)(3) organization) and PLR 200252095 (414(h)(2) pick up plan)
2. **Contribution Issues.** Can other types of payments be converted into nonelective employer 403(b) contributions? Since the early PLRs permitted post-employment contributions designed to encourage retirement of senior faculty members, can post-employment 403(b) plans be structured to support early retirement incentive programs? Can they be used to facilitate employee retention programs, an issue of particular interest for local public school districts trying to retain teachers enticed into retirement by state level early retirement programs? Can traditional severance pay programs or early retirement incentive programs for a public school system be redesigned to provide nonelective employer contributions for employees who agree to retire? Are there any types of benefits that could not be replaced by nonelective employer contributions into 403(b) plans?

3. **Constructive Receipt Issues.** Individually negotiated agreements that provide for employer 403(b) contributions may be considered to be “elective deferrals” for purposes of the Section 402(g) elective deferral limits. Can employee groups negotiate post-employment 403(b) contributions in their employment contracts in lieu of other benefits without violating constructive receipt principles? Can individuals, such as school superintendents who are not part of a larger group, include nonelective employer 403(b) contributions as part of their employment contracts? Would it matter if the school district made nonelective 403(b) contributions for other employees? Assuming that state law permits modification of existing contracts, can employees modify current (not expiring) contracts to incorporate post-employment contributions and forfeit or reduce other benefits, such as retiree healthcare or supplemental life insurance? Can classifications be created to provide different contribution levels for different members so long as no individual choice was permitted? For example, could an employer make nonelective employer contributions equal to the value of employees’ accumulated sick days if the value of such days exceeds $2,000 and make cash payments if the value of the sick days was less than $2,000. This distinction would accommodate potential problems with vendors who maybe unwilling to establish 403(b) accounts for small contributions.

4. **Establishment Issues.** ERISA requires a written plan document. Therefore, it seems that 403(b) plans that are subject to ERISA should describe the post-employment contribution feature of the 403(b) plan in the plan document. However, there is no Code requirement for a written plan document for 403(b) plans. Since the Code does not require written plan documents for 403(b) programs, how is a post-employment employer contributory program established? Is any type of documentation necessary to create a post-employment 403(b) program? For plans that are not subject to ERISA, is a resolution by a school board or a church board sufficient? Is a collective bargaining agreement sufficient?

5. **Loan Issues.** Since the employment relationship has ended, there is no payroll deduction option for retirees who have previously defaulted on a loan from their 403(b) account. Vendors will not, as a rule, accept physical collateral on 403(b) loans. Given that employers will not have a continuing relationship with the retiree and will not know whether new loans are made, what liability will the employer have for loans made to retirees from post-employment contributions? How can the employer prevent vendors from continuing to make loans?
from making such loans since the employee is the owner of 403(b)(7) custodial accounts and individually issued annuities? The final loan regulations permit reliance on employee certification that no previous loan defaults occurred, but who is protected by such certifications? The vendors are not “liable” for loan violations, but they are the parties that authorize the loan and get the employee certification. What is the employer’s risk if the vendor fails to get a certification for an employee with a previous default? Since violations of the loan regulations may occur broadly based on each vendor’s actions, do violations of the loan regulations put the employer’s entire 403(b) program at risk? Are only employees with “bad” loans at risk or is the post-employment program considered to be a separate 403(b) plan with (potentially) significant violations of the loan regulations?

While the final loan regulations make it clear that there is no exception for 403(b) plans from the requirement that employees with prior defaulted loans may not have a subsequent loan unless separate collateral is provided or the employer accepts payroll deductions, for 403(b) plans, and more particularly, 403(b) plans with post-employment contributions as the source of loan proceeds, compliance is extremely difficult. Employers do not have an ongoing relationship with retirees that would sustain payroll deductions, have little control over the compliance efforts of the vendor and generally have no control over the vendors’ efforts to comply with the loan regulations. This is particularly true for public school employers and other non-ERISA 403(b) plans where the employers’ relationships with the vendors are severely limited.

6. **Definition of Includible Income.** Many practitioners would appreciate additional guidance relating to the definition of “includible compensation” and the effect of the five-year look-back, which permits employer contributions under a 403(b) arrangement for up to five years after termination of employment, subject to any nondiscrimination rules.

7. **Post-Death Contributions.** It would be helpful if the guidance addressed the death of the participant during the five-year look-back period, particularly in situations where the employer is contractually obligated to make contributions during this period.

IV. **Rev. Rul. 90-24**

*Background:*

In general, Rev. Rul. 90-24 allows transfers among section 403(b) funding vehicles. There is, however, a practical issue in that transfers from a 403(b) custodial account to a 403(b) tax-sheltered annuity would require the annuity to continue any distribution restrictions that apply to a custodial account. If, as seems common, the annuity vendor fails to monitor this limitation, the employer/plan sponsor is at risk, as is the participant.

*Recommendations:*

Ideally, the distribution rules should be made parallel to avoid traps for the unwary and to accommodate transfers of investment vehicles.
V. 401(a)(17) Limit

In general, the limit under section 401(a)(17) of the Code is tied to the plan year. Many exempt organizations operate on a fiscal year, and the plan year is the fiscal year. The 403(b) limits, however, are often applied on a calendar year basis.

Recommendations:

It would be helpful if it were clarified that an employer sponsoring a 403(b) arrangement could apply the 401(a)(17) limit on a calendar year basis if the plan year is not a calendar year. Many tax-exempt organizations are on a fiscal year, but the 402(g) and 415 limits are required to be applied to 403(b) plans on a calendar year basis. Allowing the 402(g), 415, and 401(a)(17) limits to be applied consistently would assist in compliance.

VI. Church Plans - Commingled Investments

Background:

Numerous private letter rulings have authorized church plans to make commingled investments of retirement income assets with assets of 401(a) plans and with other church funds, consistent with the legislative history of the Retirement Equity Act of 1984, which added section 403(b)(9).

Recommendations:

It would be helpful if the regulations could consolidate the guidance that has been published in the private letter rulings. Doing so would make the guidance more readily available, and would enable church plan sponsors to rely on the published guidance without the need to obtain a private letter ruling. Likewise, the regulations could clarify that retirement income accounts under section 403(b)(9) may be invested in any type of investment.

VII. Timing of Contributions

For tax-qualified plans under section 401(a), employer contributions can generally be made until the due date, with extensions, for the employer’s tax year in which falls the last day of the calendar year. It is unclear what the timing rule is for employer contributions under a section 403(b) arrangement.

Recommendations:

It would be helpful if the guidance indicated when employer contributions under a section 403(b) arrangement need to be made. It is suggested that the due date for contributions should be tied to the due date, with extensions, for any applicable tax return for the sponsoring organization (which would typically be Form 990), as is done under the Code section 415 regulations. See Treas. Reg. §1.415-6(b)(7)(ii). For those organizations which do not file a tax return, the due
date might be a specified period following the end of the sponsor’s fiscal year, such as the six-month period specified in the regulations under section 415 of the Code for such organizations.

VIII. **Tacking Rules under Section 402(g)(7)**

**Background:**

Certain catch-up contributions under section 403(b) arrangements are tied to the participant’s years of service. Questions can arise as to whether service with a predecessor employer counts as service for this purpose with a successor.

**Recommendations:**

It would be helpful to have guidance on the rules for tacking service under section 402(g)(7).