

## **You Need To Determine If Your 403(b) Arrangement Is Subject To ERISA, And If It Is – What To Do About It**

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For many 501(c)(3) organizations, the appealing thing about allowing employees to participate in a 403(b) arrangement has been the minimal employer involvement and the fact that the plan can be operated on a "non-ERISA" basis. That is, the 403(b) wasn't treated as an employer-sponsored plan and, therefore, not subject to fiduciary rules and IRS reporting requirements on the employer's part. However, new IRS regulations effective January 1, 2009, combined with economic circumstances and the reluctance of annuity providers to provide certain services, may be pushing some plans under the ERISA umbrella, subjecting them to a number of fiduciary, reporting, and audit requirements. It is critical for employers with 403(b) arrangements to understand exactly where their arrangement stands and where it's going, or they may wake up on January 1 and find they have a tiger by the tail.

A significant aspect of complying with the final regulations involves the establishment of an information sharing agreement (ISA) between the employer and each investment provider. As we shall see, the terms of these ISAs and the way in which employers and providers decide who will be responsible for certain aspects of 403(b) compliance is likely to determine whether many 403(b) arrangements have "crossed over" from being non-ERISA programs to employer-sponsored plans subject to ERISA. And while it is critically important to bring all 403(b) arrangements into compliance with the final regulations, it is equally important to determine whether your 403(b) arrangement is a "plan" subject to ERISA. If so, you may be surprised to learn that you are now subject to a number of old and new compliance challenges – including the Department of Labor's new reporting and independent audit requirements.

### **How Do We Know If Our Arrangement Or Program Is Subject To ERISA?**

Although there are several pieces of regulatory guidance relevant to this determination, we have boiled them down to three questions:

- Have you, the employer, entered into any agreement or ISA with any provider that obligates you to do anything beyond (i) withholding amounts from your employee's compensation, (ii) remitting such amounts to the provider, and (iii) providing certain factual information about the employee or the employee's circumstances to the provider?

If you have, there is a good chance that your 403(b) arrangement is now an employer-sponsored 403(b) plan subject to ERISA.

- Have you, the employer, limited the investment products available to employees to such an extent that your employees no longer have a reasonable choice of investments?

If you have, or you think you may have, there is a good chance that your 403(b) arrangement is now an employer-sponsored 403(b) plan subject to ERISA.

- In order to comply with the final regulations, have you, the employer, agreed to be responsible for discretionary determinations, under the 403(b) program? For example:
  - Interpreting the terms of the 403(b) document;
  - Reviewing and authorizing hardship distributions (under current economic conditions this may be an especially critical decision);
  - Evaluating proposed qualified domestic relations orders;
  - Reviewing and authorizing participant loans;
  - Authorizing plan-to-plan transfers; or
  - Satisfying qualified joint and survivor annuity requirements, if applicable.

To the above, you may have answered: "We're okay. We haven't been doing any of these things!" The problem is, starting January 1, 2009, not only will you have to have a written plan document (or documents) that specify that the various 403(b) rules will be satisfied – you also will have to have in place some mechanism for making sure that the applicable rules are complied with. Here's where the so-called ISAs come in.

### **It's More Than An Information Sharing Agreement**

In order for 403(b) investment providers to receive transfers from other 403(b) providers after 2008, it will be necessary for each to enter into an ISA with the employer maintaining the 403(b) arrangement. At a minimum, an ISA must contain an agreement between the provider and the employer to share information necessary to insure compliance with the various 403(b) rules, such as the annual limit on pre-tax contributions by a single participant. However, the 403(b) regulations permit an employer to allocate responsibility for various aspects of plan administration and compliance to entities other than the employer, such as the providers. Given the fact that it is the investment

providers and not the employer who are benefiting financially from the ongoing operation of the 403(b) arrangement, it only makes sense to many employers to have these providers "earn their keep." As a result, a significant number of 403(b) employers have expanded the terms of their ISAs to allocate to each of the providers responsibility for compliance to the fullest extent possible. Unless a shifting of responsibility occurs, it will fall on the employer to make many of the discretionary determinations mentioned earlier – this would result in the 403(b) arrangement becoming subject to ERISA.

Of course, most investment providers are not going to take on additional responsibility and potential liability without a bit of encouragement. 403(b) employers, fortunately, wield exactly the type of encouragement that is needed. If it is committed to not becoming a 403(b) plan sponsor subject to ERISA, the employer simply can require each of the investment providers to sign an ISA that allocates most, if not all, of the compliance responsibility to the provider. If a provider is not willing to sign such an ISA, the employer can refuse to permit the provider to offer its 403(b) investments to the employer's employees. This type of refusal can be done, up to a point, without subjecting the arrangement to ERISA. It has been our experience that a number of 403(b) providers are willing to take on the added responsibility in exchange for the privilege of offering their investments.

Right now, there are literally dozens and dozens of 403(b) providers approaching 403(b) employers with suggested ISAs. Unfortunately, most of these vendor-provided ISAs do not go far enough from the standpoint of the employer. In fact, we recently reviewed an ISA template prepared by a national organization that purported to represent the interests of employers and providers in the 403(b) marketplace. However, its suggested ISA left responsibility for 403(b) compliance totally ambiguous – presumably the responsibility of the employer!

### **So What's So Bad About Becoming An ERISA Plan?**

Nothing. In fact, we previously have suggested that most 403(b) participants would be far better off if their employers would step up and take ERISA fiduciary responsibility for their 403(b) arrangements. See [\*Managing Your 403\(b\) Plan Is Like Herding Cats\*](#).

We are concerned about employers who think they have been maintaining, and are continuing to maintain, a non-ERISA 403(b) arrangement when they really are maintaining a plan subject to ERISA!

If a not-for-profit's 403(b) arrangement is subject to ERISA, then the employer-sponsor will take on a number of additional responsibilities, including:

- Taking fiduciary responsibility to insure that each of the investment options offered under the plan is appropriate and prudent – in the same way that most 401(k) plans are managed.
- Making sure that no more than a reasonable amount of fees or other expenses are charged to participant's accounts or annuity contracts.
- Complying with ERISA's various disclosure requirements, such as the requirement to provide each employee with a summary plan description.
- Satisfying applicable ERISA reporting requirements, such as the new requirement to file a more complete annual report (Form 5500) and, if applicable, obtain an independent accountant's opinion with respect to the plan's financial statements (See, **[insert title of related CPA's article on reporting and audit requirements]** for more about these rules).

### What Should You Do?

In order to avoid the unenviable shock of riding along in the bus only to learn that you are the driver (or learning that the cat thought you knew is a whole different animal), you need to immediately determine whether your 403(b) arrangement is subject to ERISA. If it is not currently subject to ERISA, you need to decide if you want to keep it that way or change it into an employer-sponsored plan – one that requires you to look out for the interests of participants. If you want to make sure that you do not become subject to ERISA, you need to carefully examine how you will comply with the final 403(b) regulations and whether you will be able to allocate responsibility for compliance to your providers. Do not wait any longer to deal with this determination and these important compliance issues. You may have literally dozens of providers that you must negotiate ISAs with, and there will be a learning curve for you and those who work with your arrangement if you determine that you are, or have been, an ERISA 403(b) plan.