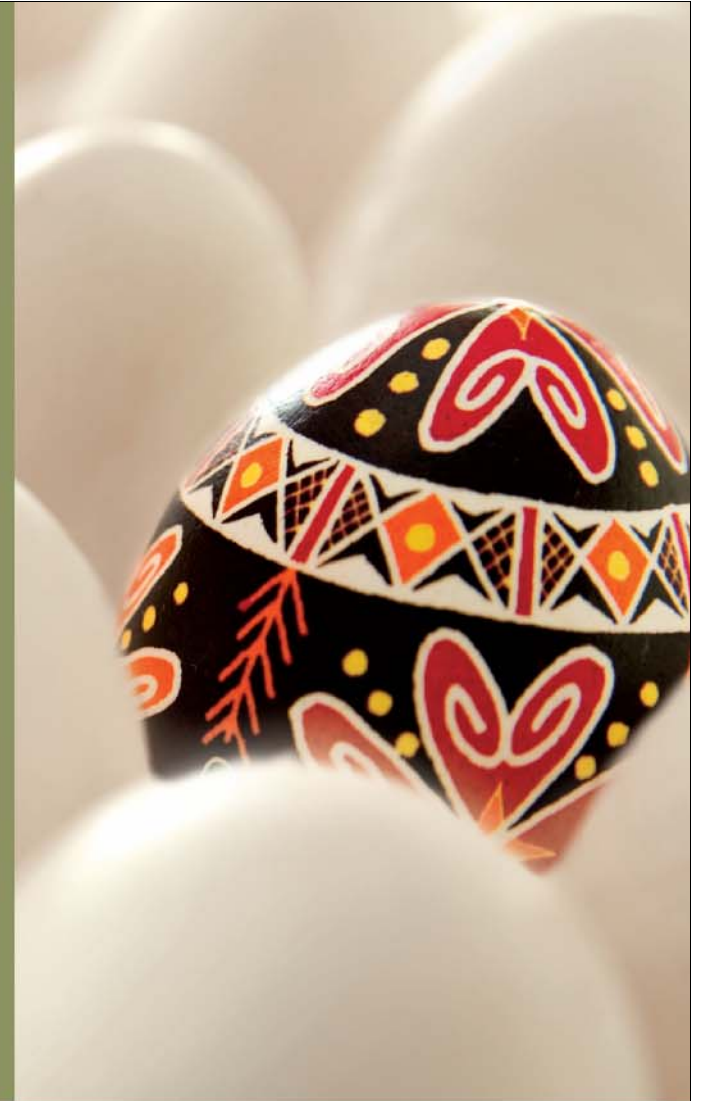


# 403(b) Plan Regulatory Compliance and Reporting

Western Pension & Benefits Conference  
2010 Spring Conference  
Phoenix, AZ

April 22, 2010

Presented By: Kelly Davis



**LarsonAllen**  
LLP  
CPAs, Consultants & Advisors

**NOTICEABLY  
DIFFERENT**

# Learning Objectives

## **To Understand:**

- Regulatory changes
- Compliance with key regulatory requirements
- When an audit is required
- The objective of an audit
- Key audit areas
- Preparation for and facilitation of an audit



# Final 403(b) Regulations - Overview

- **Governing Regulations**

- **Internal Revenue Code (IRS):**

- ◇ Defines 403(b) arrangement
    - ◇ Defines who may establish
    - ◇ Establishes guidance on providing tax deferred arrangement

- Internal Revenue Code rules different from ERISA

- **ERISA (DOL):**

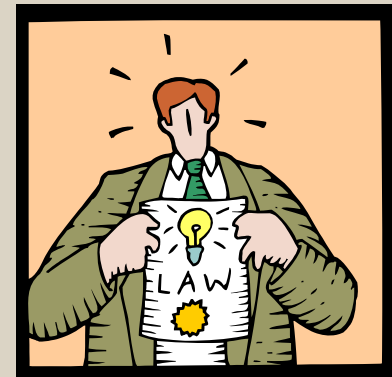
- ◇ Establishes guidance on reporting and disclosure requirements for employer sponsored benefit plans



# Final 403(b) Regulations - Overview

- **IRS Regulations**

- Issued July 26, 2007
- 1<sup>st</sup> comprehensive regulations in 43 years
  - ◇ Proposed 403(b) Regulations - 2004
- Effective for taxable years beginning after 2008
  - ◇ January 1, 2009
- Primary Purpose:
  - ◇ To diminish the extent to which 403(b) plans differ from other salary reduction arrangements
    - 401(k)
    - 457(b)
  - ◇ Increased accountability



# Final 403(b) Regulations - Overview

- **IRS Regulations (cont'd)**

- Key Requirements

- ◇ Written plan document
  - Consolidate vendors
- ◇ Form and operational compliance
- ◇ Funding contract language
- ◇ Vesting
- ◇ 15 year catch-up contributions
- ◇ Salary reduction deferral limit
- ◇ Hardship distributions
- ◇ Nondiscriminatory contributions



# Final 403(b) Regulations - Overview

- **DOL Regulatory Changes**

- Not a part of the IRS final regulations
- Form 5500 filing requirements revised by DOL
  - ◇ November 16, 2007
- Effective for plan years beginning on or after January 1, 2009
  - ◇ Calendar year: July 31, 2010
  - ◇ Fiscal year: January 31, 2011
    - DOL exemption section 2520.104-4(b)(3) being eliminated
    - 403(b) pension plans now subject to Title 1
    - Certain 403(b) plans will be subject to an independent audit, similar to 401(k) plans



# Final 403(b) Regulations - Overview

- **DOL Regulatory Changes**

- FAB 2009-02 (7/20/2009)

- ◇ Transitional relief with respect to annuity contracts and custodial accounts entered into prior to 1/1/2009:

- Beginning with 2009
      - For purposes of annual 5500 requirement, including audit.
      - For 403(b) Plan sponsors to make a good faith effort to transition with 2009 plan year to ERISA's generally applicable annual reporting requirements.



# Final 403(b) Regulations - Overview

- **DOL Regulatory Changes**

- FAB 2009-02:

- ◇ Annuity contracts or custodial accounts do not need to be treated as 403(b) plan assets by Plan Sponsor for ERISA's annual reporting requirement provided:

- Contract or account was issued prior to Jan. 1, 2009 (former or current employees);
      - Employer ceased making contributions to such contact/account prior to Jan. 1, 2009;
      - Contract or account rights and benefits legally enforceable by employee only without any employer involvement; and
      - Employee is fully vested in the contract or account.

- ◇ If above are met:

- Employees excludable as plan participants for annual Form 5500 reporting.
      - DOL will not reject Form 5500 with qualified or adverse opinion.



# Final 403(b) Regulations - Overview

- **DOL Regulatory Changes**

- FAB 2009-02:

- ◇ Except for relief under FAB 2009-02, 403(b) Plan audits must be performed by accountants in accordance with Generally Accepted Auditing Standards (“GAAS”) as required under ERISA by DOL *and* reported in accordance with U.S. Generally Accepted Audit Procedures (“GAAP”).

- The Plan sponsor has a fiduciary responsibility under ERISA and for GAAP purposes to report and include all plan assets that are known or reasonably known.
      - FAB 2009-02 does not extend to or change this requirement.
      - Be wary of industry misinterpretations of FAB 2009-02 and its applicability with ERISA and GAAP.



# Final 403(b) Regulations - Overview

- **DOL Regulatory Changes**

- FAB 2010-01 (Issued 2/17/2010):

- ◇ Issued in response to questions relating to the scope and conditions of FAB 2009-02.
    - ◇ 18 Q&A's clarifying the application of the transitional relief provided under FAB 2009-02.
      - Facts and circumstances



# Impact of Final 403(b) Regulations

- **Internal Revenue Code**

- Plan Document Requirement:

- ◇ Written plan must satisfy the following provisions:

- Must contain all material terms and conditions for eligibility, contributions, and applicable limitations
      - Form and timing of distributions
      - Identify annuity contracts and custodial accounts approved under the plan
        - Incorporate by reference
      - Optional provisions (loans, hardships, etc.)



# Impact of Final 403(b) Regulations

- **Internal Revenue Code**

- Plan Document Requirement (cont'd)

- ◇ Plan is permitted to allocate to employer or other person responsibilities of:

- Performing functions to administer plan
      - Performing functions to comply with regulations
      - Can not be allocated to participants
      - Allocation must identify who's responsible for compliance



# Impact of Final 403(b) Regulations

- **Internal Revenue Code**
  - Plan Document Requirement (cont'd)
    - ◇ Plan funded through multiple contract issuers
      - Employer must adopt a single plan document to coordinate administration rather than adopt a separate document for each issuer



# Impact of Final 403(b) Regulations

- **Internal Revenue Code**

- Salary Elective Deferrals:

- ◇ Elective non-discrimination / universal availability

- All eligible employees must have an effective opportunity to make cash or deferred election to a 403(b) plan
        - No age or service eligibility provisions with 403(b) plans
        - Does not apply to church 403(b) plans
      - Permissive exclusions:
        - employees who contribute < \$200 annually
        - employees participating in a 401(k), 457 or other 403(b)
        - non-resident aliens with no U.S. income
        - students
        - employees normally working < 20 hours per week
        - collectively bargained employees (union)
      - Satisfies nondiscrimination and coverage tests
      - Universal availability applies separately to each common law entity



# Impact of Final 403(b) Regulations

- **Internal Revenue Code**

- Salary Elective Deferrals (cont'd)

- ◇ Elective salary deferral contributions must be transferred to providers within a period no longer than is reasonable for proper plan administration
      - IRS example, transferring elective deferrals within 15 business days following the month in which these amounts would have been paid to the participant
      - ERISA – tighter standards



# Impact of Final 403(b) Regulations

- **Internal Revenue Code**

- Tax-free Transfers

- ◇ Commonly referred to as 90-24 transfers
    - ◇ Ability to move balances to other unrelated institution to employer
    - ◇ Not permitted after September 24, 2007

- Investment Exchanges

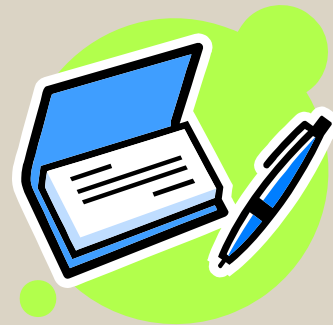
- ◇ Permitted between accounts and contracts
    - ◇ Written agreement between employer and issuer to share information by January 1, 2009
    - ◇ Plan permits
    - ◇ Benefit not diminished
    - ◇ Undiminished distribution restrictions



# Impact of Final 403(b) Regulations

- **Internal Revenue Code**

- Distributable events - can only distribute on severance of employment or “stated event” such as:
  - ◇ Attainment of certain age
  - ◇ Passage of time (years of service)
  - ◇ Disability
- Plan Termination
- QDROs
- Minimum Distributions



# Impact of Final 403(b) Regulations

- **Internal Revenue Code**

- **Nondiscrimination Rules (not new)**

- ◇ All tests apply unless a government plan
    - ◇ ADP vs. Universal Availability (employee elective deferrals)
    - ◇ ACP (employer matching & employee after-tax contributions)
    - ◇ Coverage (employer contributions)



# Impact of Final 403(b) Regulations

- **ERISA Compliance**

- Reporting and Disclosure Requirements

- ◇ Annual reporting (Form 5500) (< or > 100 participants)
    - ◇ Independent audit (generally > 100 participants)
    - ◇ Summary plan description
    - ◇ Summary annual report
    - ◇ Deposit deadlines (salary deferrals)
    - ◇ Joint survivor requirements (document)
    - ◇ Eligibility and vesting requirements



# Impact of Final 403(b) Regulations

- **ERISA Compliance**

- 403(b) plans of tax-exempt 501(c)(3) organizations are subject to ERISA
- ERISA does not apply to:
  - ◇ Any form of Governmental plan
    - Public schools (K-12, universities)
  - ◇ Certain church plans
  - ◇ 403(b) plans *not* considered to constitute the establishment or maintaining of an “*employee pension benefit plan*” defined under ERISA



# Impact of Final 403(b) Regulations

## – ERISA Compliance

### ◇ DOL Safe Harbor Exemption under final 403(b) Regulations

**A deferral-only Plan is not established by employer, as defined by ERISA, if:**

- Employee participation is voluntary
- Employee can enforce vendor contract without employer's assistance (individual contracts)
- Employer receives no unreasonable direct or indirect consideration
- Employer's involvement is limited to:
  - Letting vendors publicize products to employees
  - Requesting information
  - Summarizing or compiling employee information
  - Collecting and remitting deferrals to vendors
  - Maintaining records (e.g. deferral / plan records)
  - Selecting annuity vendors (must be reasonable)



# Impact of Final 403(b) Regulations

## – ERISA Compliance

- ◇ Plans will not meet DOL Safe Harbor Exemption and subject to ERISA, if:
  - One of the safe harbor exemption requirements is not met
  - The Plan provides for employer contributions
  - The employer acts on behalf of participants in facilitating or resolving issues with vendors, e.g. threatens to move employee accounts from vendor
  - The level of employer involvement is, or could be concluded as is, more than what is limited under the exemption requirements



# Impact of Final 403(b) Regulations

- **ERISA Compliance**

- **403(b) Plan Audit Requirement**

- ◇ Plans with more than 100 eligible employees at the beginning of the plan year require an audit
    - ◇ Small plans should be exempt from audit requirement:
      - Qualifying plan investments – 95% rule
      - Bonding for non qualifying plan investments
    - ◇ Governmental and church plans exempt
    - ◇ Possible 5500 Delinquent Filer issues for non filers



# Auditor Selection

- Important to select auditor familiar with plan audits
  - Deficient audit may result in rejection of Form 5500
    - ◇ Becomes Plan Sponsor's issue
- Referral sources
  - Peers
  - Third-party administrator
  - American Institute of Certified Public Accountants Employee Benefit Plan Audit Quality Center (AICPA EBPAQC)



# Audit Objective

- Established by Generally Accepted Auditing Standards (GAAS)
  - Express an opinion on financial statements and supplement schedules
    - ◇ Whether fairly stated in conformity with Generally Accepted Accounting Principals (GAAP)
      - In all material respects
- GAAS audit is NOT designed to ensure compliance with ERISA
- Objectives influenced by Department of Labor (DOL) and Internal Revenue Service (IRS)



# Audit Objective

- Types of Audit Opinions

- Unqualified

- ◊ Accepted by DOL

- Qualified

- ◊ Not accepted by DOL

- ◊ May result in rejection of Form 5500

- Adverse

- ◊ Not accepted by DOL

- ◊ May result in rejection of Form 5500

- Disclaimer

- ◊ Accepted by DOL in the case of limited-scope audits



# What is Audited?

- Limited-scope audit

- Contributions
  - ◇ Plan level
- Benefit Payments
- Participant Data
  - ◇ Eligibility
- Plan Obligations
  - ◇ Participant Accounts
- Other
- Participant Loans?

- Full-scope audit

- Everything in left column
- Investments
  - ◇ Valuation
  - ◇ Income



# Key Audit Areas

- **Internal Controls**
  - Assessment of Plan's control environment
  - Control walk-throughs of significant transaction classes
- **Contributions (Plan level)**
  - Timely remittances of employee contributions
  - Reconciliation between trust, payroll and recordkeeping
- **Benefit Payments**
  - Detail listing matches trust statement
  - Meet eligibility standards to receive benefits
  - Vesting



# Key Audit Areas

- **Participant Data**
  - Integrity of data used to determine eligibility
  - Recalculate eligibility and match to actual
- **Plan Obligations**
  - Reconciliation of activity and balances between trust and recordkeeping
  - Investment Elections
  - Income Allocation



# Key Audit Areas

- Other
  - Expenses
  - Non-discrimination testing
  - Mergers
  - Change in Service Providers
  - Subsequent Events
- Investments (full-scope only)
  - Valuation
    - ◊ Hard to value assets
  - Income



# Role of SAS 70

- Important in electronic environment
- Report on the Processing of Transactions by Service Organizations
  - Auditor audits and assesses internal controls of a service organization
  - Auditor issues a report called the “Service Auditor's Report”
  - Internal controls evaluated are set by service organization



# Role of Third-Party Administrators

- Involvement can vary greatly between third-party administrators
- Source of a significant amount of audit information
  - Audit Package
  - Additional information
- Ultimately responsibility is with Plan Sponsor



# How Do I Effectively Prepare for an Audit?

- Establish a timetable that is mutually agreeable to:
  - You
  - Auditor
  - Other Service Organizations
- Obtain request letter sufficiently in advance
  - Work with auditor to understand exactly what they are requesting
- Pull information prior to auditor site visit
  - Provide information in advance
  - Have ready/organized when they walk in your office



# How Do I Effectively Prepare for an Audit?

- Facilitate auditor on-line access to your Plan if possible
- Prepare reconciliations normally prepared by auditor
  - Investigate variances and irregularities prior to start of audit fieldwork

**BE READY!**



# Initial Audit Issues

- Statement of net assets must be comparative
- Auditable beginning balances (accurate)
- Integrity and accessibility of plan accounting and administrative records (current & historical)



# How Do I Effectively Facilitate an Audit?

- Make audit a priority once it commences
  - Be available to auditors during site visit
  - Respond to additional requests/inquiries timely
- Monitor progress on a periodic basis
  - Weekly updates?
- Obtain support from your financial department
  - Bring Controller/CFO into process



# How Do I Effectively Facilitate an Audit?

- Re-establish timetable if off-course
- Closing Meeting
  - Discuss audit findings
  - Discuss process improvement

**COMMUNICATE!**



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# In conclusion -

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