



## THE NEW 403(B) REGULATIONS: FINDING THE RIGHT FIX FOR YOUR PLAN

THE NEW 403(B) REGULATIONS HAVE CHANGED THE PLAYING FIELD AND MADE MANY PLAN SPONSORS TAKE A FRESH LOOK AT THEIR CURRENT 403(B) SERVICE ARRANGEMENTS. MANY 403(B) PLANS ARE CURRENTLY ON THE MOVE AS A RESULT OF THE ADDITIONAL SCRUTINY. COST, FUND SELECTION, AND THE DESIRE TO REDUCE THE NUMBER OF VENDORS ARE THE TOP 3 REASONS GIVEN TO EXPLAIN THE DECISION TO MOVE. WHILE THE DECISION TO CHANGE PROVIDERS OR CONSOLIDATE THE NUMBER OF PROVIDERS MAY BE AN EASY ONE, GETTING THERE CAN BE A CHALLENGE. KNOWING THE RIGHT QUESTIONS TO ASK AND UNDERSTANDING THE TRANSITION RULES RECENTLY PUBLISHED BY THE IRS WILL MAKE YOUR JOB MUCH EASIER.

### **The Single-Provider Solution:** Three reasons to consolidate to a single-source provider:

1. **Administrative Ease:** The new 403(b) regulations were designed to increase plan compliance with the Internal Revenue Code through increased employer responsibility. Compliance failures affect your organization and your employees. Dealing with multiple vendors makes your job harder. It will be your responsibility to ensure that each vendor arrangement is accounted for in your plan document and that the separate vendor contracts do not contradict your governing plan document. You will also need to facilitate continuing information sharing among vendors to ensure compliance with distribution, loan, and contribution regulations.
2. **Accountability:** Which provider will ultimately be responsible for filing Form 5500 and aggregating your plan assets for the new financial reporting requirements? Which provider will verify that employer contributions are compliant and appropriately allocated? A single-provider solution provides clarity and prevents passing the buck.
3. **Cost:** For most vendors, pricing varies depending on the assets under management. If you split your employees' assets among multiple vendors, you reduce your bargaining leverage and are unable to negotiate better rates based on the plan's size. Plans served by multiple providers may also require an independent Third Party Administrator to help coordinate among the vendors and provide the ultimate accountability. The more difficult the coordination, the more expensive this additional service will be.

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## One Size Does Not Fit All

HOW YOU GO ABOUT CHANGING PROVIDERS WILL DEPEND VERY MUCH ON YOUR EXISTING SITUATION. ADAPTING TO THE NEW ENVIRONMENT MAY BE A CHALLENGE. BUT ULTIMATELY, YOU'LL BE GLAD YOU TOOK THE TRIP. WITH THE RIGHT PLAN AND THE RIGHT PROVIDER, YOUR PLAN CAN BE A REAL BENEFIT TO YOUR EMPLOYEES WITHOUT BEING A HEADACHE FOR YOU.

### Case 1: Group Contract without Surrender Charges

If this is you, celebrate! Unlike individual contracts, a group contract is between you and the provider. This means that you, as the group contract holder, control the assets and have the ability to transfer the plan in total from one provider to another. While the exact process to go about transferring your assets to a new provider will depend on your new provider's policies, the process will likely follow these simple steps:

- ✦ Choose a new provider and execute a services agreement. Be sure you understand their fees, service offerings, and investment options.
- ✦ Execute a plan document that conforms to the new 403(b) regulations if you have not already done so. A full-service provider should be able to prepare the documents for you in a manner that matches your plan.
- ✦ Provide a Notice of Termination to your current provider.
- ✦ Choose your re-investment strategy. Once the plan assets have transferred to your new provider, they can re-invest according to each participant's investment elections and default into the Plan's default fund any participant that has not specified their investment elections. Alternatively, you may choose to map account holdings from a given fund in your prior investment menu to a comparable fund in your new investment menu. If you choose to map participant holdings, be sure to provide your participants with a Mapping Notice to alert plan participants of the fund changes.
- ✦ Notify plan participants regarding the vendor change. Hold educational meetings to inform participants about the new investment menu and service offerings.
- ✦ Provide a Blackout Notice to each account holder at least 30 days prior to the beginning of the blackout period. During the blackout period, participants will be unable to access their funds while the prior provider readies the funds for transfer and the new provider makes the initial purchases.
- ✦ Monitor the plan liquidation and re-investment.
- ✦ Inform participants as soon as the Blackout Period is over.



## Case 2: Group Contract with Surrender Charges

As the group contract holder, you control the assets and can transfer the plan in total from one provider to another. Many group contracts, however, are subject to surrender charges and you may find that changing providers will be expensive. If you are in this boat, knowledge is power. Be sure that you fully understand your existing contract before making a move.

- Obtain a complete copy of your contract and any amendments. Your current provider should be able to provide a copy if you do not have one readily available.
- Read the contract thoroughly to determine the conditions under which the surrender charges apply. If possible, consult with your attorney to make sure that you fully understand the terms of the contract. Surrender charges come in many forms. In some cases they are a function of the number of years that have passed since the contract was first executed. In other cases, the surrender charge is a rolling charge with an associated schedule for all new deposits. This means that at any time, some of your plan assets may be free of surrender charges while more recent deposits may still be subject to surrender charges.
- Ask your current provider for a detailed surrender quote. If applicable, ask for detail on a per participant level so that you fully understand the nature of the charges and how they will be assessed. Discuss payment options with your provider. Will the charges be assessed against participant accounts or can the employer pay these expenses on behalf of the participant?
- Identify any other charges that may be assessed at the time of plan transfer. Many stable value funds within group contracts are subject to a Market Value Adjustment (MVA) upon transfer. Be sure you understand the conditions under which this adjustment is imposed. In some cases, charges can be avoided if transfers from this sub-account are restricted to a portion (typically 10%) of the balance amount each year. In other instances, if participants transfer from the stable value sub-account to another sub-account prior to the plan transfer, they can avoid the MVA.

**Finding that your plan is subject to surrender charges isn't fatal. Many plans are better off paying the surrender charges to reap the benefits of a better solution that provides better investments, better services, and better pricing.** Even if the surrender charges are prohibitive, you still have options.

1. Stop sending contributions to your old provider and remit all new contributions to your new preferred provider. As plan assets become free of surrender charges, transfer that portion to the new provider. While this is not ideal, you will at least have broken the surrender charge cycle. Over time, you will have accomplished your objective to consolidate your assets with the new provider.
2. Consider terminating the 403(b) plan and establishing a 401(k) plan with the new provider. For many organizations, a 401(k) plan will serve their interests as well as would a 403(b) plan. Plan terminations qualify as a distributable event for plan participants. Plan assets could then be rolled into your new 401(k) plan on an employee by employee basis. Significantly, many group contracts did not envision the possibility of a plan termination when originally drafted because 403(b) plan terminations were only recently allowed. As a result, it is possible that surrender charges would not be applied in this event as employees rolled their funds into your new plan. Be sure to discuss your specific contract provisions with your provider and with your attorney.
3. Stay where you are for now, but negotiate with your vendor for different contract provisions. In many instances, the surrender terms of your contract are linked to the manner in which brokers are paid. If your broker receives large, up-front commissions on new deposits and a smaller "trail" on plan holdings, your vendor may charge surrender charges to reimburse themselves for these up-front payments if the plan leaves early. By negotiating a different arrangement with your broker, you may be able to alter the terms of your contract so that over time you will have the ability to change vendors without penalty.



### Case 3: Individual Contracts

If your current 403(b) is invested in individual contracts with a single or multiple vendors, then there is a separate contract between the vendor and each employee for each employee account. Because you are not a party to these contracts, you do not have the ability to transfer the plan in aggregate to your new provider. Instead, each employee has the choice whether or not to transfer their holdings on an individual basis to your new provider. This can present some unique challenges as you attempt to simplify administration and consolidate the number of vendors servicing your plan. Here are some helpful guidelines to keep in mind.

- Choose your new provider and execute a service agreement. Be sure you understand their fees, service offerings, and investment options.
- Prior to January 1, 2009, execute a plan document and specify only the new provider as eligible to receive new contributions on a going forward basis. Making this decision and identifying your new provider as the sole provider in your plan document prior to January 1, 2009 is extremely important. While the final regulations arguably fail to cover all of the possible scenarios, it is logical to conclude that plan sponsors will have to maintain some type of contractual relationship with every provider that receives contributions after January 1, 2009 so long as any plan account remains open with such provider.
- Notify your employees of the change. In coordination with your new provider, hold educational meetings and explain the process to transfer their accounts from the current providers to your new provider. Work with your new provider to encourage these transfers by providing pre-completed paperwork or explicit instructions. Your new pricing is likely based in part on the size of your plan. The more money that transfers over, the better your pricing will likely be. Further, your ongoing administration is easier if your plan assets are all in one place.
- In many cases, your employees will not be able to transfer all of their holdings at one time. For example, money held in the provider's stable value investment may be subject to transfer restrictions. Work with your employees so that the maximum amount is transferred each year automatically until all of their assets are consolidated with your new provider.
- For remaining plan contracts issued by former providers between January 1, 2005 and December 31, 2008\*, make a "reasonable, good faith effort" to collect available information about these contracts and issuers, and then notify such issuers of the name and contact information of the person in charge of administering your plan for the purpose of coordinating information exchange. Demonstrating this good faith effort ensures that all such contracts do not lose their 403(b) status due to their failure to be encompassed within the new written plan.

\* Automatic relief applies to a discontinued contract issued before January 1, 2005 if the vendor ceased to provide investment products to the plan prior to January 1, 2005. Neither the employer nor the vendor needs to take any action regarding such a contract.

