Retirement Plan Alternatives for Nonprofits

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Pro Bono Partnership of Atlanta:

To provide free legal assistance to community-based nonprofits that serve low-income or disadvantaged individuals. We match eligible organizations with volunteer lawyers from the leading corporations and law firms in Atlanta who can assist nonprofits with their business law matters.

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- In order to be a client of Pro Bono Partnership of Atlanta, an organization must:
  - ✓ Be a 501(c)(3) nonprofit.
  - ✓ Be located in or serve the greater Atlanta area.
  - ✓ Serve low-income or disadvantaged individuals.
  - ✓ Be unable to afford legal services.

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Legal Information:

✓ This webinar presents general guidelines for Georgia nonprofit organizations and should not be construed as legal advice. Always consult an attorney to address your particular situation.

Retirement plans vary widely in their design & administration:

- ✓ employer eligibility
- ✓ employee eligibility
- ✓ steps to starting and maintaining the plan
- ✓ employer contributions
- ✓ employee contributions
- ✓ tax treatment of distributions
- ✓ nondiscrimination requirements
- ✓ vesting requirements
- ✓ compliance with relevant rules under ERISA and Internal Revenue Code

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Before starting a retirement program, consider:

- ✓ what type of plan
- ✓ how to establish the plan
- ✓ how to operate and maintain the plan
- ✓ how to terminate the plan

Small Employer Retirement Programs

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Small Employer Retirement Plans: Payroll Deduction IRA

Payroll Deduction IRAs

- simplest type of retirement plan for small employers
- employer must set up an IRA for each employee
- employer's involvement is limited to transmitting employee payroll deduction contributions
- employee contributions are limited to $6,000 for 2019
- no employer contributions permitted

Small Employer Retirement Plans: SEP

SEP stands for “Simplified Employee Pension”

- only allows employer contributions
- employers have discretion to make or not make contributions each year
- employer sets up an IRA for each employee and executes a written agreement for a SEP
- employer contributions are limited to the lesser of 25% of employee’s compensation or $56,000 (for 2019)
- all employees must be eligible to participate
- employer must contribute equally to all employees

Small Employer Retirement Plans: SIMPLE IRA

SIMPLE IRAs stands for "savings incentive match plan for employees individual retirement account"

- limited to employers with 100 or fewer employees
- employer sets up a SIMPLE IRA for each eligible employee
- employees can make deferral contributions of up to $13,000 for 2019
- employer must either:
  - ✓ match employee contributions dollar for dollar up to 3% of compensation
  - ✓ make a fixed contribution of 2% of compensation for all eligible employees

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Small Employer Retirement Plans: SIMPLE 401(k)

SIMPLE 401(k) stands for "savings incentive match plan for employees 401(k)"

- limited to employers with 100 or fewer employees
- employer sets up a SIMPLE 401(k) account for each eligible employee
- employees can make deferral contributions of up to $13,000 for 2019
- employer must either:
  - ✓ match employee contributions dollar for dollar up to 3% of compensation
  - ✓ make a fixed contribution of 2% of compensation for all eligible employees

Retirement Plans

Retirement Plans

Retirement plans are governed by the Internal Revenue Code and the Employee Retirement Income Security Act of 1974 (ERISA).

Retirement Plans

- There are ongoing obligations for retirement plans, including:
  - ✓ filing the annual Form 5500
  - ✓ annual nondiscrimination testing and required corrections
  - ✓ timely remittance of employee contributions to the plan's trust
  - ✓ utilizing IRS and DOL correction programs if compliance errors materialize

Retirement Plans: Internal Revenue Code

- Internal Revenue Code
  - ✓ minimum participation requirements
  - ✓ nondiscrimination testing for compensation
  - ✓ nondiscrimination testing for ACP/ADP
  - ✓ maximum contribution limits
  - ✓ top heavy requirements
  - ✓ minimum vesting requirements
  - ✓ consent for distribution requirements
  - ✓ joint and surviving annuity requirements

Retirement Plans: ERISA

- ERISA
  - ✓ fiduciary requirements
  - ✓ vesting requirements
  - ✓ reporting requirements
  - ✓ disclosure requirements
  - ✓ document requirements
  - ✓ funding requirements
  - ✓ ERISA preemption of state laws

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Retirement Plans: Church Plans

- Church Plans are exempt from ERISA, meaning no Form 5500 filing requirement, no disclosures in summary plan descriptions, and no ERISA preemption of state laws.
- A church plan is:
  - ✓ established and maintained for its employees by a church that is exempt from tax under Code Section 501
  - ✓ its principal purpose of function is the administration or funding of a retirement or welfare plan for church employees
  - ✓ it is “controlled by” or “associated with” a church

Retirement Plans: Government Plans

- Government plans are exempt from ERISA, meaning no Form 5500 filing requirement, no disclosures in summary plan descriptions, and no ERISA preemption of state laws.
- A government plan is: …

401(k) Plan

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401(k) Plan

- Most common type of retirement plan
- 401(k) plans are subject to ERISA (unless a church plan)
- employees can contribute up to $19,000 for 2019 and another $6,000 in catch-up contributions if over age 50 for a total of $25,000
- After-tax and Roth contributions are also allowed
- employers can contribute up to a total of $56,000 in 2019 (including employee deferrals in this limit) or $62,000 in 2019 for those age 50 and older
- governments are not eligible to maintain 401(k) plan

401(k) Plan

Setting up a 401(k) plan:

- employer must adopt a written 401(k) plan document
- employer must arrange a trust to hold the plan's assets
- employer must develop a recordkeeping system
- employer must provide plan information to eligible employees
- employer must file an annual Form 5500

401(k) Plan

Nondiscrimination Testing:

- Employer must perform nondiscrimination testing to ensure the plan does not discriminate in favor of highly compensated employees, which can be complicated
- Actual Deferral Percentage Test
- Actual Contribution Percentage Test
- Coverage testing – generally, plan benefits at least 70% of employees that are not highly compensated employees
- Top Heavy testing – key employees may not have more than 60% of all plan assets

401(k) Plans

- As an alternative to nondiscrimination testing, employers can adopt a safe harbor plan in which the employer must:
  - ✓ make 100% matching contributions of up to 3% of compensation plus 50% of the next 2% of compensation
  - ✓ make nonelective contribution of 3% of compensation

401(k) Plan

Timely Remit Employee Contributions to the Plan's Trust

- must be remitted to the trust as soon as possible but not later than the 15th business day of the following month
- practically, must be remitted on the earliest day in which the company can segregate the employee contributions from the general assets of the company
- For plans with less than 100 participants, the time period is 7 business days following the date the employee contributions are withheld from salary

403(b) Plan

403(b) Plan

- A 403(b) plan is a deferred compensation plan for employees of tax-exempt organizations and public schools that offers pre-tax and optional post-tax retirement savings.
- Employees make contributions to annuity contracts or custodial accounts that invest in mutual funds.
- Although many tax rules that apply to 401(k) plans also apply to 403(b) plans, 403(b) plans are not considered to be qualified retirement plans.

403(b) Plan

- Only certain types of employers can adopt 403(b) plans:
  - ✓ public school systems
  - ✓ public charter schools
  - ✓ public colleges and universities
  - ✓ certain hospitals
  - ✓ tax-exempt entitities

403(b) Plan

- Universal Availability Requirement
  - ✓ 403(b) plans (other than church plans) must permit all employees to participate in the 403(b) plans.
  - ✓ The following employee groups can be excluded:
    - employees eligible to participate in another 403(b) plan
    - employees eligible to participate in a government 457(b) plan
    - employees eligible to contribute to a 401(k) plan
    - nonresident aliens
    - certain student employees
    - certain part-time employees working fewer than 20 hours each week

403(b) Plan

Nondiscrimination Testing

- 403(b) plans are generally <u>not</u> subject to the actual deferral percentage testing requirement
- employer contributions and after-tax employee contributions are subject to actual contribution percentage testing requirement

403(b) Plan

- 403(b) plans are not subject to ERISA if certain requirements are met:
  - ✓ voluntary
  - ✓ funded solely by employee contributions
  - ✓ provide annuity contract or custodial rights enforceable solely by the employee
  - ✓ limited employer involvement with plan (i.e., no loans, no employer contributions, no hardship withdrawals, etc.)
- 403(b) plans sponsored by governmental entities are exempt from ERISA

403(b) Plan

Optional special contributions only for 403(b) plans:

- 403(b) plans allow employee catch-up contributions of $6,000 (in 2019) for those age 50 or older AND catch-up contributions for certain employees with at least 15 years of service.
- Employers can make nonelective contributions to terminated employees up to 5 years after separation from service. Allowing

457 Plan

457 Plan

- Two types of sponsors of 457 plans that have difference plan rules:
  - ✓ government employers: may cover all employees, trust requirement
  - ✓ tax-exempt entities employers: may only cover a select group of employees, must be unfunded, Roth and catch-up not permitted
- Two types of 457 plans:
  - ✓ 457(b) plan: defer up to the IRS limits of $19,000 in 2019
  - ✓ 457(f) plan: nonqualified deferred compensation plan allowing deferrals in excess of the IRS limits, must be limited to a select group of managers or highly compensated employees, must contain a substantial risk of forfeiture, and must be unfunded

457(b) Plan

- Taxation when amount is paid or made available
  - ✓ Even if plan assets haven't been distributed, they're includible in a participant's income in the taxable year they're made available to the participant.
  - ✓ It's critical for tax-exempt employers to understand the rules that apply to an eligible 457(b) plan before deciding on this plan for its employees. If a tax-exempt employer wants to sponsor a plan that covers a broad cross section of employees, it may consider adopting other types of plans, such as a 401(k) plan or 403(b) plan. (403(b) plans are limited to an organization that is tax-exempt under IRC 501(c)(3)).

457(b) Plan

- KEY DIFFERENCES FROM 401(k) and 403(b) plans"
- Employee's election to contribute
  - ✓ Employee's election to make contributions is before the first day of the month in which the compensation is paid or made available.
  - ✓ This is different than 401(k) and 403(b) plans that allow the contribution amount to be changed at least annually
- May not roll over to another qualified plan (unless governmental 457(b) plan
- No distribution upon death or disability
- No ability to correct errors under IRS EPCRS

	Tax-exempt 457(b) Plan	Governmental 457(b) Plan
Eligible Employees	Limited to select management or highly compensated employees	All employees and independent contractors
Nondiscrimination testing	None	None
Employee contributions	Allowed	Allowed
Roth contributions	Not allowed	Allowed
Employer contributions	Allowed	Allowed
Total Contribution Limits	Combined employee and employer for $19,000 in 2019	Combined employee and employer for $19,000 in 2019

	Tax-exempt 457(b) Plan	Governmental 457(b) Plan
Increased salary reduction for final 3 years before NRD	Lesser of: -2 x dollar limit ($38,000 in 2019) or -Applicable dollar limit plus sum of unused deferrals in prior years	Lesser of: -2 x dollar limit ($38,000 in 2019) or -Applicable dollar limit plus sum of unused deferrals in prior years (excluding age 50 catch-up contributions)
Age 50 catch up contributions	Not allowed	Allowed, but cannot use in final 3 years before NRD
Trust	No	Required
Loans	Not allowed	Allowed
Hardship distributions	Allowed	Allowed

	Tax-exempt 457(b) Plan	Governmental 457(b) Plan
Automatic Enrollment	Not allowed	Allowed
Distribution Events	Termination Attainment of age 70.5 Unforseeable emergency Plan termination QDRO Small account distribution of $5,000 or less	Termination Attainment of age 70.5 Unforseeable emergency Plan termination QDRO Small account distribution of $5,000 or less
Rollovers to other plans	Not allowed	Allowed
Statutory period to correct plan failures	No	Yes, 1st day of the plan year beginning more than 180 days after notification by the IRS

Comparison of 401(k), 403(b), and 457(b) Plans

Type of Plan Sponsor

401(k) Plan	403(b) Plan	Tax-exempt 457(b) Plan (not governmental)
For profit entities and Tax-exempt entities but governmental entities are not eligible	Tax-exempt entities and governmental entities but for profit entities are not eligible	Tax-exempt entities but not governmental entities (although governmental entities can sponsor a government 457(b) plan)

Type of Plan Sponsor

401(k) Plan	403(b) Plan	Tax-exempt 457(b) Plan (not governmental)
Only employees and must pass coverage testing if employees excluded	All employees must be eligible	Select group of management or highly compensated employees

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Investments Allowed

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
Variety of investments may be offered, including annuity contracts, mutual funds, and individual securities	Limited to mutual funds and annuity contracts	Varity of investments permitted, including mutual funds, annuities, and stable value arrangements

Employee Contributions

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
The limit on employee contributions is $19,000 for 2019	The limit on employee contributions is $19,000 for 2019	The limit on employee contributions is $19,000 for 2019
Limits need to be combined with other 401(k) and 403(b) plans (but not 457 plans)	Limits need to be combined with other 401(k) and 403(b) plans (but not 457 plans)	Limits do not need to be combined with other plans

Employer Contributions

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
Total combined employer and employee contributions may not exceed 100% of employee's compensation or $56,000 (for 2019)	Total combined employer and employee contributions may not exceed 100% of employee's compensation or $56,000 (for 2019)	Single Limit for both employee and employer contributions of $19,000 for 2019
Trust required	Maybe no trust required	No trust allowed

Catch-Up Contributions

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
Age 50 catch-up contributions allowed of $6,000 in 2019	Age 50 catch-up contributions allowed of $6,000 in 2019	Only increased contributions in final 3 years prior to normal retirement date; age 50 catch-up contributions are not allowed

Nondiscrimination Testing

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
Employer can define eligibility subject to nondiscrimination requirements; nondiscrimination testing is required on contribution amounts unless it is designed to be a "safe harbor plan."	Universal availability applies (even to part-time employees).	No nondiscrimination requirements – employer defines eligibility and limits.

Distributions while employed

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
Only on account of hardship or disability if under age 59 ½ and the plan allows; plan terms must permit in-service distribution at age 59 ½ because it is not automatic	Only on account of hardship or disability if under age 59 ½ and the plan allows; plan terms must permit in-service distribution at age 59 ½ because it is not automatic	Only on account of unforeseeable emergency; small sum cash rule for in-service distributions of $5,000.

Participant Loans

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
If plan allows, loan allowed up to 50% of vested account balance up to a maximum of $50,000	If plan allows, loan allowed up to 50% of vested account balance up to a maximum of $50,000	Loans are not allowed from 457(b) plans that are not governmental plans.

Early Withdrawal Penalty

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
Withdrawals before age 59 ½ are subject to 10% federal tax penalty (with some exceptions).	Withdrawals before age 59 ½ are subject to 10% federal tax penalty (with some exceptions).	No withdrawal penalty regardless of age at termination.

Taxation

401(k) Plan	403(b) Plan	Tax exempt 457(b) Plan
Contributions and earnings are taxed when distributed (except Roth and after-tax contributions).	Contributions and earnings are taxed when distributed (except Roth and after-tax contributions).	For nongovernmental plans, funds are taxable when paid or when made available (even if not received).

Nonqualified Plans

Nonqualified Plans

- Nonqualified plans promise compensation in any year after it is earned. These include bonus plans, long-term incentive plans, and other programs that defer compensation until retirement or termination of employment.
- Subject to Section 409A of the Internal Revenue Code.
- These plans have strict restrictions on timing of contributions and payments but are otherwise flexible as to plan terms.

ANY QUESTIONS?

For More Information:

If you would like more information about the services of Pro Bono Partnership of Atlanta, contact us at:

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