



In this Issue:

- Overview
- Public School 403(b) Plans Allow Workers to Save for Retirement
- Application of ERISA to 403(b) Plans
- Consequences of ERISA Not Applying to Public School 403(b) Plans
- State Laws May Impose Additional Requirements
- Conclusion

EXEMPTIONS UNDER ERISA FOR PUBLIC SCHOOL 403(B) PLANS

Overview

The Employee Retirement Income Security Act (ERISA) is a federal law that contains rules for retirement plans, such as 401(k) plans. These rules address a variety of issues that relate to operating a retirement plan, such as when must someone be allowed to participate in the plan, when do contributions have to be deposited into the plan, and who is responsible for the plan's administration.

Retirement plans must also follow rules contained in the Internal Revenue Code. The Code must be satisfied in order for the participants in the plan to qualify for favorable tax treatment, such as being able to contribute from their pay on a pre-tax basis.

Public School 403(b) Plans Allow Workers to Save for Retirement

A 403(b) plan is a type of retirement plan that is similar to a 401(k) plan in that employees can save their own money on a tax favored basis. Employees are also permitted to make independent decisions as to how much they want withheld from each paycheck and contributed to the plan. In most cases, employees are allowed to change their contribution amount during the year to go higher or lower as their needs dictate. Employers can also make non-elective contributions to 403(b) plans on behalf of their workers.

However, there are some important differences between 401(k) and 403(b) plans. For example, participants in 403(b) plans often have individual contracts with the investment provider. Thus, the onus is on the participant to learn about how the plan works, how much to save for retirement, and how to invest his or her money in the plan. As a result, teachers who participate in 403(b) plans often benefit from additional assistance to help in planning for their retirement.

Application of ERISA to 403(b) Plans

ERISA was intended to be a comprehensive law, but not all 403(b) plans are subject to its coverage. ERISA exempts two large categories of 403(b) plans: (1) governmental plans; and (2) voluntary salary deferral only 403(b) plans in which employer involvement is limited.

Governmental plans are plans for employees of the Government of the United States, the government of any State or political subdivision, or any of their agencies or instrumentalities. These plans include 403(b) plans and other retirement plans sponsored by public school districts. Governmental plans are subject to the Internal Revenue Code's requirements, but are exempt from ERISA.

ERISA also has an exemption for certain 403(b) plans offered by tax-exempt 501(c)(3) organizations if certain conditions are satisfied. The exemption applies if the only contributions to the plan are employee deferrals and the employer's involvement in running the plan is very limited. However, this deferral only exception is not relevant for public school district plans since they are already exempt from ERISA as a governmental plan.

While ERISA may apply to 403(b) plans offered by tax-exempt 501(c)(3) organizations depending on the degree of employer involvement, there is nothing a public school district can do to make their 403(b) plan subject to ERISA.

Consequences of ERISA Not Applying to Public School 403(b) Plans

The requirements that apply to some tax-exempt 501(c)(3) organizations' 403(b) plans do not apply to public school 403(b) plans because of the ERISA exemption for governmental plans. For example, the following rules in ERISA do not apply to public school 403(b) plans.

- **Public Schools Are Not Required by ERISA or the Internal Revenue Code to Restrict 403(b) Plan Investments** - Plans that are subject to ERISA are required to prudently select and monitor plan

service providers and the investments in their plans. These rules are not part of the Internal Revenue Code. Since ERISA does not apply to public school district plans, ERISA does not place any restrictions on public schools with respect to the investments that they choose to offer in their 403(b) plans.

- Public Schools Do Not Have to File Form 5500s** - Plans that are subject to ERISA generally have to file an annual report with the federal government known as Form 5500, Annual Returns/Reports of Employee Benefit Plan. Public school 403(b) plans do not have to file this report as ERISA does not apply to them.
- Service Providers Do Not Have the Same Obligations Under ERISA to Public School 403(b) Plans** - ERISA provides plans with the ability to recover losses if service providers fail to act in accordance with ERISA's requirements. Some service providers claim that they are acting in accordance with ERISA when they are providing services to public school 403(b) plans. However, they cannot satisfy ERISA's requirements while performing services for public school plans as ERISA does not impose any requirements for these plans. Additionally, since ERISA does not apply, it does not provide any method for public schools to seek recovery if service providers fail to act in the best interests of the plan.
- Participants in Public School 403(b) Plans Do Not Have the Same Rights to Information Under ERISA** - ERISA requires information about plan investments to be given to participants. These disclosure rules do not apply to public school 403(b) plans. As a result, a task force that includes the National Education Association (NEA), the National Tax Sheltered Accounts Association (NTSAA) and the American Society of Pension Professionals & Actuaries (ASPPA) developed a new tool to facilitate these disclosures to participants in public school 403(b) plans. More information is available at <http://savemy403b.org/403b/new-fee-disclosure-solution-released-by-nea-ntsaa-asppa-joint-403b-taskforce>.

Conclusion

Public school 403(b) plans are very different from 401(k) plans. As a result, it is important for school districts to select service providers and consultants who are knowledgeable about public school 403(b) plans and the rules that apply to them.

State Laws May Impose Additional Requirements

Some states have enacted laws that impose additional requirements on public school 403(b) plans. In some cases, these laws may be similar to the rules in ERISA. As a result, it is important that all who work with and administer governmental 403(b) plans ensure that they are familiar with the state laws that apply to their plan.