



What do the 403(b) Regulations Mean for You?

On July 26, 2007, the Internal Revenue Service (IRS) issued final regulations for tax-sheltered annuity arrangements under section 403(b). Given that the first 403(b) regulations were issued by the IRS in 1964, these regulations were over 40 years in the making. As you would expect, these final regulations provide for significant changes in the way 403(b) plans must be maintained and administered.

The following is a summary of the new principal concepts covered in the final regulations, commentary on what those changes mean to 403(b) plan sponsors, and the ways AUL Retirement Services can help you comply. The retirement services division of AUL has been dedicated to the 403(b) marketplace for more than 40 years.

The final regulations are generally effective for plan years beginning on or after January 1, 2009. The intended effect of these regulations are to make the rules governing 403(b) similar to the rules governing other arrangements that include salary reduction contributions, such as 401(k) plans and 457(b) plans.

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Tax qualified retirement plans from American United Life Insurance Company® (AUL) are funded by an AUL group annuity contract. While a participant in an annuity contract may benefit from additional investment and annuity related benefits under the annuity contract, any tax deferral is provided by the plan and not the annuity contract.



NEW REQUIREMENT

Written Plan

All 403(b) arrangements, including those not subject to ERISA, must maintain a written plan.

Excess Contributions

Contributions, other than employee deferrals, that exceed the limits under Internal Revenue Code § 415(c) cannot be returned. They must instead be deposited in a separate account and treated like a 403(c) taxable contribution that is immediately included in the employee's gross income. Excess employee deferrals, however, can be returned.

Participation Rules

An "effective opportunity" must be provided to employees regarding their rights to participate in the plan and they must be given time to elect to make or change the amount of their deferrals.

The "universal availability" rule is still applicable. Generally, this rule provides that all employees of the employer must be permitted to make elective deferrals.

Only the following

employees may be excluded:

- ✓ non-resident aliens
- ✓ employees eligible for 457(b) plans
- ✓ students
- ✓ employees who normally work less than 20 hours per week
- ✓ employees eligible under another 403(b) plan
- ✓ employees eligible to participate in a 401(k) plan

IMPACT ON EMPLOYERS

The employer must maintain documentation that includes all of the material provisions regarding:

- ✓ eligibility
- ✓ benefits
- ✓ applicable contribution limits
- ✓ available contract descriptions
- ✓ loan procedures
- ✓ hardship withdrawals
- ✓ the time and form under which benefit distributions may be made.

Generally, this will require something very similar to a plan document of the type required for other deferral plans.

The employer must:

- ✓ monitor excess deferrals and contributions
- ✓ return excess deferrals on a timely basis
- ✓ establish the proper separate accounting and complete the appropriate tax reporting on any excess contributions

The employer must:

- ✓ ensure that new hires are aware of the plan and the right to make deferrals.
- ✓ monitor who is participating and determine if those who are not have been given proper notice of the right to participate

HOW AUL CAN HELP

AUL can provide a document that includes essential provisions, including:

- ✓ eligible categories of employees
- ✓ deferral limits
- ✓ transfers of benefits
- ✓ available investments
- ✓ loan and hardship provisions
- ✓ time and form of benefit distributions

AUL will assist employers with:

- ✓ monitoring deferrals and contribution amounts
- ✓ returning excess deferrals on a timely basis
- ✓ separate accounting
- ✓ tax reporting

AUL will assist employers by:

- ✓ providing a sample notice that the employer may utilize in notifying employees of their right to participate in the plan and to make elective deferrals



NEW REQUIREMENT

Transfers

A nontaxable transfer of assets is permitted provided that the transfer is:

- ✓ a change of investment within the same plan, or
- ✓ to the plan of another employer

Transfers previously permitted pursuant to Revenue Ruling 90-24 are no longer allowed as of September 24, 2007.

Catch-up Contributions

Two separate catch-up contributions are available to eligible participants and must be coordinated for employees eligible to make both. Any amounts contributed to the plan in excess of the annual deferral limitation (\$15,500 in 2007) are first treated as a 403(b) catch-up contribution available to participants with at least 15 years of service (to the extent permitted) and then as an age 50 catch-up contribution (to the extent the age 50 catch-up amount exceeds the 403(b) catch-up)

Plan Termination

Plan may include language that permits plan termination and distribution of benefits. The distribution of benefits would only be allowable if the employer does not make contributions to another 403(b) plan beginning on the date of the plan termination and ending 12 months after the distribution of all assets from the terminated plan, subject to exceptions.

IMPACT ON EMPLOYERS

The employer must:

- ✓ establish a procedure for the proper sharing of information regarding a participant's employment
- ✓ establish a procedure to determine if transfers should be permitted
- ✓ ensure that the benefit cannot be reduced by the transfer
- ✓ ensure that the same distributions restrictions are applicable to the new plan or investment

The employer must:

- ✓ review current administrative procedures to ensure eligibility and proper coordination

The employer must ensure that:

- ✓ all accumulated benefits are distributed to participants as soon as administratively feasible following termination of the plan
- ✓ no contributions are made to another 403(b) contract beginning on the date of plan termination and ending 12 months after the distribution of all assets from the terminated plan, subject to exceptions.

HOW AUL CAN HELP

AUL will assist employers by:

- ✓ prompting the employer, or the employer's designated representatives to approve any transfer into and out of the plan
- ✓ reviewing document(s), if available, to ensure that benefits will not be reduced and that the same distribution restrictions are applicable
- ✓ providing a sample notice that the employer may use in notifying employees of ineligible transfers

AUL will assist employers with:

- ✓ tracking and properly allocating employee deferrals
- ✓ identifying employees who are eligible for catch-up contributions
- ✓ coordinating the two catch-up limits

AUL will assist employers by providing:

- ✓ sample resolutions
- ✓ sample notices and communications to participants
- ✓ employer-directed distributions to participants



NEW REQUIREMENT

Severance from Employment

Distributions are permitted upon severance from employment. Severance from employment occurs when (1) the employee ceases to be employed by an eligible employer that maintains a section 403(b) plan or (2) the employee works in a capacity that is not employment with an eligible employer.

Controlled Group/ Aggregation Rules

In the case of tax-exempt entities maintaining a 403(b) arrangement, the employer includes not only the organization whose employees participate in the plan, but also any other exempt organization that is under common control (80% or more board control) with such organization. In addition, if two or more exempt organizations regularly coordinate their day-to-day exempt activities, they may elect to treat themselves as being under common control.

Loans

Loans may be treated as a taxable distributions based on certain “facts and circumstances,” which include whether or not:

- ✓ the loan has a fixed repayment schedule
- ✓ the loan bears a reasonable interest rate
- ✓ there are “repayment safeguards to which a prudent lender would adhere.”

IMPACT ON EMPLOYERS

Employees are not required to terminate employment with all employers (in situations where the employer is part of a controlled group) sponsoring the 403(b) plan in order to be eligible for distributions.

As a result, the employer must:

- ✓ monitor terminations to determine if an employee is eligible for a distribution that he or she may not have been previously eligible to receive

Tax-exempt employers must:

- ✓ determine if they are part of a group of organizations under common control
- ✓ ensure that the employees of all members of the group are offered the opportunity to participate in the 403(b) plan

The employer must:

- ✓ ensure that that loans meet the “facts and circumstances” tests to avoid being taxable
- ✓ properly report the employee’s taxable income if the loan fails to meet the requirements

HOW AUL CAN HELP

AUL will assist employers with:

- ✓ employer-approved distributions upon severance from employment

AUL will assist employers by:

- ✓ providing information that will enable them to determine if an entity is part of a controlled group
- ✓ providing divisional recordkeeping and reporting, if necessary, for multiple entities

AUL will assist employers by providing :

- ✓ loan procedures and documents that comply with the terms of the plan and regulations
- ✓ reports regarding requests for loans and information regarding loans



NEW REQUIREMENT

Hardship Distributions

Hardship distributions are permitted provided the distributions meet the hardship distribution rules for 401(k) plans (*i.e.*, they must be for an immediate and heavy financial need, limited to the amount necessary to satisfy the hardship, etc.). In addition, hardship distributions under 403(b) plans are limited to the amount of the participant's elective deferrals, reduced by any other distributions previously made from the plan.

IMPACT ON EMPLOYERS

The employer must determine:

- ✓ if a financial need exists for a hardship distribution
- ✓ the amount of the financial need
- ✓ that the distribution does not exceed the amount of the hardship

Finally, the employer must restrict deferrals by a participant for a period of six months following the hardship distribution.

HOW AUL CAN HELP

AUL will assist the employers by providing them with information necessary to determine:

- ✓ if a financial need exists for a hardship distribution
- ✓ the amount of the financial need
- ✓ that the distribution does not exceed the amount of the hardship

AUL will also provide the employer with provisions and procedures that are safe harbor compliant for the administrative ease of the employer.