• **457(b) Opportunities for TPA Business Owners**
• This session is geared to 401(k) administrators who want to learn about 457(b) plans and includes a comparison and contrast of 457(b)s and 401(k)s. Learn about the market for 457(b) plans and how they work with your 401(k) clients. Come broaden your plan design and administrative skills.

• Learning objectives:
• Summarize the benefits of the 457(b) plan.
• Discuss the benefits of a 457(b) plan with the plan sponsor.
• Assess if a client is a good prospect for a 457(b) plan.
Both a 401(k) and 457(b) plan are funded through employee payroll deduction contributions. Annual contributions limits are the same for both 401(k) and 457(b) plans ($18,000 for 2015). The age of 50 “catch-up” provision is the same for both plan types. ($6,000 for 2015). A 457(b) plan contribution can qualify for the employee “Saver’s Tax Credit.” A 457 (b) plan can allow Roth contributions.
What is the difference between a 401(k) plan and a 457 plan?

401(k) plans are IRC tax-advantaged qualified retirement savings plans and are subject to the Employee Retirement Income Security Act of 1974 (ERISA).

457(b) plans were originally designed to be “deferred compensation” (non-qualified) plans rather than qualified retirement plans and are not governed by ERISA.

What is the difference between a 401(k) plan and a 457 plan?

A 457 plan is a program in which employees of tax-exempt employers or state and local governmental employers can defer compensation to a later date. In other words, a 457(b) plan is not an elective tax provision. It applies as a matter of law. Any deferred compensation by an eligible employer is done so under section 457 whether the employer intended to offer a plan or not.

In 2001, EGTRRA provisions changed “includible compensation” to have the same meaning used for qualified plans under IRC 457. Today, the market considers and views 457(b) plans as tax-advantaged retirement plans like a 401(k).
What is the difference between a 401(k) plan and a 457 plan?

Employers that can establish 401(k) plans include: private, for-profit employers, some nonprofit employers and some governmental employers where a 401(k) plan existed and was grandfathered upon the creation of the 403(b) plan.

Employers that can establish a 457(b) plan include:
• A state or political subdivision
• An agency or instrumentality of a state or political subdivision
• Any tax-exempt organization that is not a government or a church within the meaning of IRC 3121(w)

What is the difference between a 401(k) plan and a 457 plan?

• 401(k) plans do not allow independent contractors to participate.
• Both governmental and non-profit organizations can allow independent contractors to participate under a 457 plan
• A 457(b) plan cannot cover employees of related taxable entities whereas a 401(k) plan can cover employees of related entities. However, an unfunded deferred compensation plan can be maintained for highly compensated and management employees of taxable affiliates.
What is the difference between a 401(k) plan and a 457 plan?

The IRS does not assess a penalty for premature withdrawals (age 59½) from a 457 account since ERISA rules do not apply. Any withdrawal is still subject to normal income tax.

Early withdrawals (before age 59 ½) from a 401(k) plan are subject to the additional 10% tax penalty.

What is the difference between a 401(k) plan and a 457 plan?

While both plans allow for early withdrawals, the qualifying circumstances for early withdrawal eligibility are different.

Under a 401(k) plan, participants can take early withdrawals using financial “hardship” provisions.

Under a 457 plan, account holders are allowed hardship distributions are allowed under "unforeseeable emergency“ provisions in the plan document.
What is the difference between a 401(k) plan and a 457 plan?

Rules for financial hardship:

457 plans feature a "Double Limit Catch-up" provision that 401(k) plans do not. This provision is designed to allow participants who are nearing retirement to compensate for years in which they did not contribute to the plan but were eligible to do so. Thus, under the right conditions, a 457 plan participant may be able to contribute as much as $35,000 to his plan in one year.

– Historical data sometimes not available
– Calculate individually
– Calculate for all employees to demonstrate plan’s ability to expand savings for tenured employees
Benefits of a 457(b) Plan

- Since 457 plans are nonqualified retirement plans, it is possible to contribute to both a 401(k) and 457 plan at the same time. Many large government employers offer both plans. In such cases, the participant is able to contribute maximum amounts to both.
- Cost savings by combining assets under one product platform - Asset Size Savings if a product provider can support multiple plan products on one platform.
- If the employer has strategic needs for employees to retire before the age of 55 and begin immediate withdrawals, there is no early withdrawal penalty on assets from a 457(b) plan.
- There are no excise taxes on excess contributions in a 457(b) plan. Governmental entities with 401(k) plans are also exempt from the excise tax on excess contributions.

Discuss the benefits of a 457(b) plan with the plan sponsor.

- Employer pitfalls with a 457(b) plan
  - A second benefit plan has additional administration costs
  - You can withdraw funds from a 401(k) for a home purchase or college tuition, but not from a 457 account.
  - **What are other effects of violating limits on total contributions?** In the case of a governmental plan that includes the limits in the plan but violates them administratively, the plan continues to be considered a 457(b) plan until the first day of the first plan year that begins more than 180 days after the date the IRS notifies the employer of the problem and will continue to be a 457(b) plan then if the employer has fixed the problem.
Church Employers (Source p.402)

• A nonelecting church is exempt from I.R.C. § 457(b). Thus, it can maintain an unfunded deferred compensation plan, but is not subject to the I.R.C. § 457(b) requirements. To avoid unfavorable tax consequences, such a plan must not be funded and must meet the requirements of I.R.C. § 409A

Tax-Exempt Employers

• A tax-exempt employer, other than a government or non-electing church, can have a 457(b) plan ONLY for highly compensated and management employees.
• Known as a “Top Hat” Plan
• Ineligible 457 plans vs eligible 457 plans

Assess if a client is a good prospect for a 457(b) plan.

• If they have no plan at all, what are the factors that would lead to starting the employer with a 457(b) plan?
• Severance Pay Plans vs. Deferred Compensation – IRS looks closely at severance pay plans to determine if they are exempt under IRC 457(e). Don’t unintentionally create an ineligible 457(f) plan. Some relief with Announcement 2000-1 and the Job Protection Act of 2004. (The Source p.401)
  – Certain kinds of “separation pay” are considered includible compensation as long as such amounts are paid no later than the end of the tax year following the employee’s final day of employment, or if later, within 2 ½ months of the end of the tax year. (Source p. 403)
• Non-Profit trying to set aside compensation for an executive. If it does not qualify under any of the IRC sections 401, 403(b) or 457, the employee will owe taxes once the money is set aside in a trust or funding vehicle or there is a substantial risk of forfeiture. (Source p.402)
• “Golden Handcuff” option -
Deferral of Sick Leave

• Can an employee defer sick leave cash out under the Organization’s 457(b) Deferred Compensation Plan (“the Plan”) where the amount actually cashed out to the employee is different (more or less) than the dollar amount of sick leave the employee would have received if employment had continued and the leave had been used during employment?

• Proposed Response: No. If the sick leave cash-out is an amount different than that which the employee would received had employment continued, the sick leave that is paid after severance is not includable compensation and cannot be deferred under 457(b).