



Agenda

- What is a 457 Plan?
- Why Choose a 457 Plan?
- 457 Overview
- Sections 409A and 457(f)
- Administration & Compliance Issues





What is a 457 Plan?

- A “Nonqualified” deferred compensation plan that is maintained by not-for-profit and governmental organizations.
- It is subject to the rules of Internal Revenue Code Section 457 and its regulations.



Why Choose a 457 Plan?



- To attract and retain employees.
- A method of deferring income and the tax on such income to a specific future date.
- It is designed specifically for a key individual or select group of individuals to provide for deferral of income above and beyond amounts provided under the organization's other retirement plans provided to all employees.
- Not-For-Profit Organizations may only provide nonqualified deferred compensation through 457 plans.





457 Overview

- **There are two types of 457 Plans:**
 - May be Elective or Non-Elective
 1. Eligible Plans – 457(b)
 2. Ineligible Plans – 457(f)



457 Overview



- **Requirements of a 457(b) Plan**

- Plan must be in writing
- Must include requirements for participation, contributions and limits, distributions and form of benefit payment
- Optional provisions, if any, must be included in plan document
- Must comply in form and operation

- **457(b) Characteristics**

- Tax deferred Plans
- Limited to select group of highly compensated and management employees
- Unfunded plan may use a Rabbi trust but assets are subject to employer's creditors
- Treated as Top Hat Plan



457 Overview



- **457(b) Contribution Limit**

- Same limits as 401(k) and 403(b) deferrals (\$16,500)
- Not aggregated with contributions to 401(k) or 403(b) plans
- Reduced only by deferrals to other 457(b) plans
- Age 50+ catch up is not permitted in not-for-profit plans
- All 457(b) plans of employer treated as one plan
- Beware: Employer contributions are treated as elective deferrals and reduce deferral limits





457 Overview

- **Excess Deferrals**

- Distribute by April 15 of year following calendar year of excess
- If April 15 deadline is missed then:
 - 457(b) plan becomes a 457(f) plan
 - Excess deferrals are double taxed in the year of deferral and the year of distribution





457 Overview

- **457(b) Distributions**

- Severance from employment
- Age 70 ½ while still working
- Unforeseeable emergency
- Small account balances
- Distributions usually not subject to 10% early distribution tax



457 Overview



- **457(f) Plans – Ineligible Plans**
 - Contribution above annual 457(b) limits
 - For executives and high paid
 - Contributions must be subject to substantial risk of forfeiture
 - Amounts can be taxable before participation is eligible for distribution
 - Must be in writing
- **457(f) contributions may be taxed when:**
 - Deferred
 - Vested (no substantial risk of forfeiture) or
 - Paid





Sections 409A and 457(f)

- **Applies to Section 457(f) plans**
 - Internal Revenue Code Section 409A requirements in addition to 457(f) requirements
 - Timing of election to defer compensation as well as election of time and form of payout is crucial
 - Must be specified before the beginning of the year in which services related to deferred compensation are to be performed
 - Election for first year of plan may be made within 30 days of initial eligibility
 - Section 409A does not apply to Section 457(b) plans





Administration & Compliance Issues

- Permitting catch up contributions in a 457(b) nongovernmental plan
- Exceeding contribution limits in 457(b) and failing to distribute by April 15
 - Excess contributions subject to income tax in year of deferral and year of distribution
- Rollovers
 - 457(f) and 457(b) nongovernmental plans not eligible for rollover
 - Exception rollover of 457(b) plan to another organization's 457(b) plan
- Negotiating new employment agreements impacting deferred compensation and overlooking 457 plan
- Failing to execute 457 documents or elections



Administration & Compliance Issues



- Results of 457(b) Plan Compliance Issues
 - Plan becomes subject to 457(f)
 - Since a 457(b) plan does not contain a substantial risk of forfeiture, all amounts for **all individuals** covered under the plan becomes immediately taxable in the year of the violation





Administration & Compliance Issues

457(f) Plan Issues

- Invalid Substantial Risks of Forfeiture
 - Non-competes
 - Entitlement must be conditioned on performance of substantial future services or occurrence of a condition that is related to the purpose of the compensation
- Elective salary/bonus deferrals
 - Government Presumptions
 - A rational person would not forego compensation and subject it to a substantial risk of forfeiture
 - Presumed not to have a valid substantial risk of forfeiture



Administration & Compliance Issues



- Severance benefits paid upon voluntary termination extended over more than 2 ½ months after year end
 - Really deferred compensation
 - Payout is Guaranteed
- Severance arrangements will be bona fide if
 - Payable upon **involuntary** termination
 - Payment does not exceed two times salary capped at \$490,000 for 2011
 - Paid within two years from year of termination





QUESTIONS?

