February 2019

Retirement Times

NEWS AND UPDATES FOR RETIREMENT PLAN SPONSORS AND FIDUCIARIES

Repay Student Loans or Save in a Retirement Plan? Why Not Both?

Many employees feel squeezed to both pay off their debt and save for their future. A recent Private Letter Ruling (PLR) opens the door for employers to help them.

The average student graduating in 2016 has $37,172 in student loan debt.[1] According to the New York Federal Reserve, more than two million student loan borrowers have student loan debt greater than $100,000, with approximately 415,000 of them carrying student loan debt in excess of $200,000.

What do these numbers mean for you? They mean that debt repayment is typically an employee's foremost priority. It's not just the newly minted graduates, either – typically, student loan repayment is stretched over 10 years with close to an 11 percent default rate.

In this climate, don't be surprised when a desired prospective or current employee inquires how you can help them with their priority - debt reduction. Nor should you be surprised when you find that your debt-burdened employees are not using the savings opportunity of their retirement plan. Many employees feel too squeezed to both pay off their debt and save for their future. Those employees are frustrated not only by their lack of opportunity to save early, as is

prudent, but also because they frequently miss out on employer matching contributions in their retirement plans.

Some employers are attempting to solve these issues. On Aug. 17, 2018, the IRS issued PLR 201833012. The PLR addressed an individual plan sponsor's desire to amend its retirement plan to include a program for employees making student loan repayments. The form of this benefit would be an employer non-elective contribution (a student loan repayment contribution, or "SLR contribution").

The design of the plan in the PLR would provide matching contributions made available to participants equal to 5 percent of compensation for 2 percent of compensation deferred, it includes a true-up. Alternatively, employees could receive up to 5 percent of compensation in an SLR contribution in the retirement plan for every 2 percent of student loan repayments they made during the year. The SLR contribution would be calculated at year-end. The PLR states that the program would allow a participant to both defer into the retirement plan and make a student loan repayment at the same time, but they would only receive either the match or the SLR contribution and not both for the same pay period. Employees who enroll in the student loan repayment program and later opt out without hitting the 2 percent threshold necessary for an SLR contribution would be eligible for matching contributions for the period in which they opted out and made deferrals into the plan.

The PLR asked the IRS to rule that such design would not violate the "contingent benefit" prohibition under the Tax Code. The Code and regulations essentially state that a cash or deferred arrangement does not violate the contingent benefit prohibition if no other benefit is conditioned upon the employee's election to make elective contributions under the arrangement. The IRS ruled that the proposed design does not violate the contingent benefit prohibition.

All that said, it is important to note that a PLR is directed to a specific taxpayer requesting the ruling, and is applicable only to the specific taxpayer requesting the ruling, and only to the specific set of facts and circumstances included in the request. That means others cannot rely on the PLR as precedent. It is neither a regulation nor even formal guidance. However, it does provide insight into how the IRS views certain arrangements. Thus, other plan sponsors that wish to replicate the design of the facts and circumstances contained in the PLR can do so with some confidence that they will not run afoul of the contingent benefit prohibition.

Companies are increasingly aware of the heavy student debt carried by their employees, and are exploring a myriad of programs they can offer to alleviate this burden. This particular design is meant to allow employees who cannot afford to both repay their student loans and defer into the retirement plan at the same time the ability to avoid missing out on the "free money" being offered by their employer in the retirement plan (by essentially replacing the match they miss by not deferring with the SLR contribution they receive for participating in the student loan repayment program). This design is not meant to help employees accelerate their debt payoff. If that's your goal, you would have to do so directly into the student loan repayment program – there is no conduit to do so through the retirement plan.

While the IRS ruled in regard to the contingent benefit prohibition, the PLR states definitively that all other qualification rules (testing, coverage, etc.) would remain operative. Thus, if you wish to pursue adding such provisions to your retirement plan, you must take care as you undertake the design.

The facts provided in the PLR were very basic, and the plan design is very basic in that it requires deferral/student loan repayment equal to 2 percent for a 5 percent employer contribution (either match or SLR contribution) with no gradations. This is important because gradations could create separate testing populations for each increment of the SLR contribution plan, since it is a non-elective contribution, not a matching contribution. This could become a nightmare scenario for non-discrimination testing and administration.

Alternatively, to avoid the potential nondiscrimination testing issues, the benefit could be designed to exclude highly compensated employees. However, that still doesn't alleviate the potential administrative burden placed on your payroll and human resources teams. Most of the debt repayment programs are not yet integrated with retirement plan recordkeepers. That means that administering some of the interrelated elements of the two plans would have to be undertaken in-house.

There are more than a few consequential elements that you should be wary of while exploring opportunities to assist your employees and employment targets. In all cases it is recommended that you involve your retirement plan's recordkeeper, advisor and even – in some sophisticated design scenarios – outside counsel to make certain they: (1) don't inadvertently create qualification issues, (2) understand the potential for additional testing and perhaps additional financial considerations of the design; and (3) are prepared for any additional administration the program may require.

This month's employee memo gives ideas for eliminating student loan debt. Even if you are not yet offering this benefit, the memo offers other practical ideas to assist your employee population with student loan debt.

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Effective Employee Education

Fiduciary duty requires you to provide your employees and participants with educational opportunities, so they can make informed investment decisions. It's not always easy to know what your participants need, want or will take advantage of. Using a simple framework for your educational program may increase the effectiveness of your program.

1. Provide a consistent, ongoing program using a variety of communication mediums. This can include group meetings, podcasts, online tools, one-on-one meetings or other mediums attractive to your participants.

2. Vary the content of your program to provide broad education. Content should include plan basics, such as Basic Investing/Getting Started, but may also include topics related to a participant's entire financial picture – e.g., Saving for College, Estimating Retirement Income Sources and Needs, Health Care Options – and other topics of consideration to a retiree's financial well-being.

3. Offer online and professional advice tools to help retirees determine how much they need to save and how they will invest their contributions.

4. Fully disclose to participants, in easily understandable terms, information about the fees associated with their different investment options.

5. Offer participants opportunities to discuss their risk tolerance level, and help them understand how much risk they are willing to take when investing for their retirement.

6. Consider allowing employees to take advantage of educational opportunities and/or one-on-one meetings during working hours. This helps send a message to employees that their employer values this important benefit and is interested in helping employees prepare for their future.

7. Survey employees to determine if they find the educational program valuable, are taking advantage of it, what would make it more attractive and other feedback they may have to help continuously improve the program.

Every plan and its participant base is different, and there is no one right structure for an educational program. By starting with the above and being willing to modify your program's offerings according to participant feedback, your educational program will get stronger, you will meet this responsibility and you may even see employee engagement increase!

[1]Forbes. Student Loan Debt Statistics In 2018: A $1.5 Trillion Crisis.

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