



## Employee Benefits Practice Group

### IRS Announces Compliance Check for 457(b) "Top Hat" Plans of Tax-Exempt Employers

Syracuse, New York

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On **June 3, 2013**, the IRS's Employee Plans Compliance Unit ("EPCU") announced a "compliance check" project (see [http://www.irs.gov/Retirement-Plans/Employee-Plans-Compliance-Unit-\(EPCU\)--Non-Governmental-457\(b\)-Plans-Project](http://www.irs.gov/Retirement-Plans/Employee-Plans-Compliance-Unit-(EPCU)--Non-Governmental-457(b)-Plans-Project)) for tax-exempt sponsors of non-governmental 457(b) plans (often referred to as "Top Hat" plans). Project goals include learning more about the operation of non-governmental 457(b) plans, verifying compliance with the Internal Revenue Code ("Code") requirements, identifying noncompliance issues, and recommending ways to remove barriers to compliance.

***Focus of the Compliance Check.*** According to the announcement, the compliance check project will focus on the following issues: (1) verification that deferrals reported on Forms W-2 represent a 457(b) plan; (2) the plan sponsor's eligibility to maintain a 457(b) plan; (3) verification that participation in the 457(b) plan is limited to a select group of highly compensated employees, managers, directors or officers; (4) verification that the 457(b) plan contains only permissible features (e.g., the plan cannot provide for loans, age-50 catch provisions, or contributions placed in a trust for the exclusive benefit of participants); and (5) determination of whether unforeseeable emergency distributions have been made.

***How Plans are Selected.*** Under the program, EPCU will select 200 plans in IRS fiscal year 2013 (ending 9/30/2013) and an additional 200 plans for the 2014 IRS fiscal year (ending 9/30/2014). It appears 457(b) plan sponsors will be randomly selected for the compliance project based on information reported on Forms 990 and Forms W-2 (i.e., which show contributions to a non-governmental 457(b) plan).

***Noncompliance.*** According to the EPCU announcement, if a compliance check reveals that a plan is not established or operated in accordance with Code section 457(b), the plan may be subject to audit, or corrected under the IRS's Voluntary Correction Program. (It is unclear how this will work, however, since 457(b) plans were specifically excluded from the IRS's recent update to the Employee Plans Compliance Resolution System ("EPCRS").)

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**Audit Risk.** The compliance check project is not equivalent to an audit or investigation – i.e., the IRS will not inspect books and records to determine tax liabilities for prior years. However, the IRS conducted a similar compliance check project for 401(k) plans for which a final report was issued in March 2013 (*available at [http://www.irs.gov/pub/irs-tege/401k\\_final\\_report.pdf](http://www.irs.gov/pub/irs-tege/401k_final_report.pdf)*). The final report states that the IRS received responses from 98% of selected plan sponsors, and conducted full-scope examinations of 401(k) plans of ***all*** sponsors failing to respond to the questionnaire. In other words, if the 401(k) program is any indication of how the IRS will conduct the 457(b) compliance check project, non-responding plan sponsors can expect an IRS examination of their 457(b) plans.

**Action required by Plan Sponsors.** Sponsors of 457(b) plans that receive a compliance check letter from the IRS should consult with benefits counsel for assistance in completing the questionnaire. Additionally, plan sponsors not receiving questionnaires should still consider consulting with benefits counsel to ensure compliance with Code section 457(b) and to address any current compliance issues. This will prepare plan sponsors for the potential receipt of a compliance check letter in the 2014 IRS fiscal year, and/or any potential future examination or investigation by the IRS.

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### **Bousquet Holstein PLLC**

The Bousquet Holstein Employee Benefits Practice Group is fully versed in the complex set of rules that regulate the employee benefits area as set forth under ERISA (Employee Retirement Income Security Act of 1974, as amended) and the Internal Revenue Code. We routinely advise clients with regard to the design, implementation, and administration of employee retirement, welfare, and fringe benefit plans. Our expertise covers all aspects of retirement plans, including qualified and non-qualified pension and profit-sharing plans such as 401(k) plans, ESOPs, and "age weighted" plans; cafeteria and "flex" plans; welfare benefit plans; and "Top Hat" and other executive compensation plans. We guide our clients with regard to regulatory compliance and assist those clients facing compliance issues, often employing the government-provided correction programs, EPCRS (IRS's correction program) and VFC (the Department of Labor's correction program). We have represented clients before the IRS, DOL and PBGC in audits involving qualified plans, welfare benefit plans and other compliance issues. We have extensive experience advising clients, at both the employer level and the participant level, with regard to the drafting and approval of Qualified Domestic Relations Orders (QDROs).