David W. Powell
(202) 861-6600
dpowell@groom.com

June 4, 2009

CC:PA:LPD:PR (Announcement 2009-34)
Room 5203
Internal Revenue Service
POB 7604
Ben Franklin Station
Washington, D.C. 20044

Re: Comments on IRS Announcement 2009-34

This letter is to provide comments on the proposed Revenue Procedure set out in Announcement 2009-34. We appreciate the work that has gone into this proposed procedure and the related draft List of Required Modifications (LRMs) for 403(b) plans. We believe that this proposal represents an effective way for the Service to ensure better compliance with the new rules in this area without unduly burdening employers, many of whom are nonprofit organizations and schools without extensive financial resources. On behalf of Diversified Investment Advisors, we would like to address several areas in which we believe the proposed prototype process could be made better both for the Service and many employers.

In Announcement 2009-34, the Service indicates that one of its goals in establishing the § 403(b) prototype plan program is to ensure that § 403(b) prototype plans will be broadly suitable for the majority of eligible employers. And, appropriately, the Service does not intend that prototype plans be suitable for every eligible employer or every circumstance.

To that end, however, the Service has stated that, because it believes most eligible employers do not include vesting schedules or require provisions applicable only to churches and organizations described in § 3121(w)(3):

1. All 403(b) prototype plans must provide for full and immediate vesting of all contributions under the plan; and

2. Opinion letters will not be issued for plans that include provisions applicable only to churches or qualified church-controlled organizations as described in § 3121(w)(3), church-related organizations described in § 1.403(b)-2(b)(6), or ministers described in § 414(e)(5)(A); or plans that fail to satisfy requirements that apply to organizations other than churches and qualified church-controlled organizations as described in § 3121(w)(3), such as universal availability for elective deferrals or the

limitation of § 401(a)(17) (notwithstanding that nonelecting church plans can otherwise use a prototype).

We agree with the Service that it generally would not be a good use of resources to attempt to accommodate every type of 403(b) plan in the upcoming prototype program. However, we would strongly urge the Service to consider opening the program to include (1) plans with vesting schedules, and (2) *some* of the provisions relating to defined contribution church plans. We and, we believe, many other providers and plan sponsors in the 403(b) community are concerned that without at least these two modifications, there will be a substantial number of common 403(b) plans that will not be able to use the prototype program. Those plans would be forced into the individual determination letter program, even though many of those would be using, as they do now, specimen documents almost identical to the prototypes the Service will approve, but at the additional expense to the Service of having to review, and the employers submit, each one individually. Allowing these two changes, we submit, should be relatively simple to accommodate and significantly decrease the number of individual plans and the work for both the employers and the Service.

We would also recommend that the Service consider other comments to the language of the related draft List of Required Modifications: (1) a recognition that the language of LRM 62 regarding the "Contribution Formula" should not preclude prototype plans having more flexible options for allocating employer contributions, subject to nondiscrimination requirements where applicable and the 415 limits; (2) more flexibility in the cashout limit addressed in LRM 33 for plans not subject to such limitations (i.e., nonelecting church and governmental plans); (3) allow the use of non-safe harbor definitions of hardship in LRM 41; and (4) in LRM 7, to allow the use of the Social Security Act definition of disability.

Vesting

As we understand it, the principal reason for the Service excluding plans with vesting schedules for employer contributions from the prototype program is the belief that there are not many such plans. Secondary considerations are that many 403(b) plans are exempt from ERISA and thus may have different vesting rules, such as for service-counting, that may be difficult to accommodate, and that the vesting rules are somewhat different under 403(b) than for 401(a) plans due to the nonforfeitability rule of 403(b)(1)(C).

In our experience, while a substantial segment of the 403(b) market – particularly public school district plans – often does not have vesting schedules, a not insignificant segment - ERISA-covered plans, as well as many non-ERISA church plans - do. Although we are not aware of any hard data in this area, we are aware that many major 403(b) providers allow vesting under their current specimen documents and many employers currently take advantage of that feature. Not only would excluding vesting

from prototype plans result in those plans being submitted as individual plans, but the Service would wind up reviewing the same specimen documents - similar to ones already approved by it without vesting - as individual plans with vesting, over and over again.

We believe the concern that non-ERISA plans (governmental or nonelecting church plans, since DOL safe harbor plans cannot have employer contributions and thus are always vested) might have unusual vesting rules that are not easily accommodated, is more theoretical than real. In our experience, non-ERISA plans that apply vesting schedules by and large use ERISA service counting rules, for example, hours of service rules (by counting hours or determining hour equivalencies) or elapsed time rules for counting years of service, and break in service rules (and in most cases, apply ERISA vesting standards, such as 2 to 6 year graded or 3 year cliff vesting), as they are well-established and familiar to many plan administrators and participants. Accordingly, if the Service believes that the introduction of quirky non-ERISA vesting or service rules would introduce problems into the prototype review process, we would suggest that the Service consider allowing vesting schedules in the prototype process only if compliant with the ERISA rules (which are consistent with the Code rules under 411, of course, and so would be familiar to the Service). If a non-ERISA plan wishes to have some different vesting rule, then perhaps it would be appropriate for such a plan to seek an individual determination letter.

With respect to concerns that the nonforfeitability requirement of 403(b)(1)(C) may complicate the drafting of vesting provisions, we note that Treas. Reg. section 1.403(b)-3(d)(2) explains how vesting rules and the nonforfeitability rule work in combination, and we think that a prototype plan could essentially follow the language of the regulation.

Selected Church Plan Rules

A church defined benefit 403(b)(9) plan in existence on August 13, 1982 is a unique thing, and fairly *sui generis*. It would seem entirely reasonable to exclude those from the prototype program.

However, a number of defined contribution church plans use documents, including specimen documents from 403(b) providers, which are very similar to the documents used by ERISA-covered 403(b) plans, and use for investment the same annuity contracts and custodial accounts holding registered investment company shares available from the provider for other 403(b) plans. Such church employers may include local churches independent of large denominations, church schools, church colleges and universities, or church hospitals. The differences from an ERISA 403(b) plan in plan language are often, we believe, minimal and easily accommodated by drafting a handful of discrete provisions applicable only if the plan is a church plan (and which is currently a feature in a number of fairly generic specimen 403(b) plans). These include:

1. Allowing participation by ministers who may not be common law employees. Ministers may be self-employed or chaplains employed by another employer (and are permitted to contribute to 403(b)(9)s and deduct the contribution up to the 402(g) limit under 404(a)(10)). See Code section 414(e)(3)(B).

2. The special $10,000/$40,000 rule of Code section 415(c)(7)(A).

3. The special rule of Code section 415(c)(7)(C) allowing an annual addition of $3000 for foreign missionaries whose AGI does not exceed $17,000.

4. The special rule treating certain contributions for foreign missionaries to be treated as investment in the contract under Code section 72(f) (though it may not be necessary for that to be in the plan to be effective, it is often referenced).

5. Special church service-counting rule for the 15-year catch-up election under Code section 415(c)(7)(B) and 402(g)(7). This rule essentially permits service within a convention or association of churches (commonly a denomination) to be tacked-on for eligibility to make this special catch-up contribution for qualified organizations.

6. Nondiscrimination rules. 403(b) plans of churches as defined under Code section 3121(2)(3)(A) (which includes certain church elementary and secondary schools) and qualified church-controlled 501(c)(3) organizations described in Code section 3121(w)(3)(B) are exempt from nondiscrimination testing, while 403(b) plans of church-controlled 501(c)(3) organizations which do not meet the internal support test of Code section 3121(w)(3)(B) (referred to as "non-QCCOs"), such as church hospitals, colleges, universities and nursing homes, are subject to those rules. The prototype plan could state that the nondiscrimination rules of the referenced sections do not apply to a church plan unless the employer is a non-QCCO within that definition.

7. Designation of a 403(b) benefit as housing allowance pursuant to Rev. Ruls. 62-117 or 75-22. We recognize that the treatment of retirement plan distributions as housing allowance is a no-ruling area (see Rev. Proc. 2009-3). It is also possible that, to the extent this applies, it need not be in the plan so long it is properly designated by the appropriate authority, but it is common to reference it and a reference to the treatment as parsonage allowance should not be the basis for excluding consideration of a prototype plan.

We do not think that these provisions would add much complexity to a prototype document, and flexibility in these areas would allow a number of church plans –

particularly those of independent churches and church schools, hospitals, colleges and universities, with plans very similar to non-church 403(b) plans - to avoid the expense of individual determination letters. We could also provide sample language in some of these areas if that would be of assistance.

Comments on the LRMs

As noted above, we also have some comments on specific provisions of the LRMs:

1. Employer Contributions – LRM 62. The LRMs contemplate that discretionary and nondiscretionary contributions may be made to a nonstandardized plan. However, the only contributions referred to require at least 500 hours of service, or are based on a percentage of compensation or are in proportion to compensation. We recognize that this language is based on the Defined Contribution LRMs for 401(a) plans, just as the matching contribution language of the 403(b) LRMs is based on the Cash or Deferred Arrangement LRMs. In practice, though, in our experience, such contributions may be a flat dollar amount, or a matching percentage of salary reduction contributions which may not satisfy 401(m) if 401(m) does not apply, or may be capped at a dollar amount or percentage of compensation, or age or service weighted, or with different formulas for different classes, or a combination of those. Even for plans subject to the nondiscrimination requirements, these often pass nondiscrimination testing due to the non-highly compensated nature of much nonprofit employment. We would request that the Service not decline to issue opinion letters to prototype plans with such flexible employer contribution provisions, so long as they are subject to nondiscrimination requirements to the extent applicable, and the 415 limits.

2. Cashout Limit – LRM 33. This LRM states that "[i]f elected in the Adoption Agreement, distributions may be made in the form of a lump-sum payment, without the consent of the Participant or Beneficiary, but no such payment may be made without the consent of the Participant or Beneficiary unless the Account Balance does not exceed $5,000 (determined without regard to any separate account that holds rollover contributions)". This reflects the cashout limit of Section 203(e) of ERISA (since the similar Code provision, 411(a)(11)(A), does not apply to 403(b) plans). However, though not common, nonelecting church and governmental plans which are not subject to ERISA sometimes set higher cashout limits, such as $10,000, where the expenses of maintaining the account are believed to not justify having many small accounts. Such plans should be allowed to set a different cashout limit, and we request that the language of the LRM be modified to so indicate. (The Service has also previously issued guidance on how such higher limits in non-ERISA plans operates in conjunction with the default IRA rollover rule of Code section 401(a)(31)(B); see Notice 2005-5.)

3. Hardship Distributions – LRM 41. The hardship distribution provisions of LRM 41 reflect only the "safe harbor" rules of Treas. Reg. § 1.401(k)-1(d)(3) under

which a hardship request may be "deemed" to be on account of an immediate and heavy financial need of the employee. Again, we recognize that this is similar to the Cash or Deferred Arrangement LRMs. However some 403(b) plans elect to not use the safe harbor hardship provision and apply the general rules of Treas. Reg. § 1.401(k)-1(d)(3). We would request that the Service not decline to issue opinion letters to prototype plans that allow use of the general hardship distribution rules of the regulation and not the safe harbor.

4. Disability Definition – LRM 7. We recognize that this definition is the same language as used in the Defined Contribution LRMs for qualified plans. The Code and regulations refer to the definition of disability in Code section 72(m)(7), and the regulation under that provision is that on which this language is based. However, some plans apply the requirement that a person demonstrate that they have been determined to be "disabled" for purposes of Section 223(d)(1) of the Social Security Act, which should be a slightly stricter and more objective definition. We request that the Service not decline to issue opinion letters to prototype plans that permit the option of using a determination of disability under the Social Security Act as the trigger to permit a distribution on disability (of course, normally, a disability meeting any of these requirements will be accompanied by a severance from employment permitting a distribution in any event).

* * * * *

Again, we thank the Service for its work on the proposed 403(b) prototype procedure, and recommend that, with the changes and clarifications described above, a large number of substantially similar plans could effectively use prototypes and not be forced to use the individual determination letter program. Please let us know if you have any questions.

Yours sincerely,

David W. Powell