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IRS Blesses an Employer's Proposal to Link Plan Contributions to Student Loan Repayments

In a Private Letter Ruling, the IRS blessed an employer's proposed student loan program through which an employee's student loan debt repayment would be matched by the employer in its 401(k) plan. However, the structure of the program is very specific and may be difficult, if not impossible, for certain plans and employers to implement.

Background

In recent years, there has been greater awareness among employers that employees' financial wellbeing can directly impact their physical wellbeing — which in turn may affect productivity at work, absenteeism, and the usage/cost of employer-provided healthcare. With student loan debt increasing significantly over the past decade, many employers have looked for ways to help alleviate this burden. The focus of employer-provided loan repayment assistance has generally been on addressing employees' overall financial wellbeing rather than retirement readiness — or lack thereof. Employees that spend a large portion of their paycheck servicing student loan debt are unlikely to contribute to the employer's 401(k) plan, often missing out on an employer match and leaving money on the table.

Concern about violating the "contingent benefit" rule under Code section 401(k)(4)(A) and Treas. Reg. Section 1.401(k)-1(e)(6) has previously deterred employers from linking student loan repayments with 401(k) plan benefits. This rule prohibits a qualified plan from conditioning payment of another benefit on an employee's electing to make, or not make, elective contributions under the plan. The allowance for employer matching contributions is an exception to this rule.

IRS OKs An Employer's Proposed Plan Contributions Linked to Student Debt Repayment

On August 17, 2018, IRS released PLR 201833012 in response to an employer's request for a ruling on its proposed amendment to its 401(k) plan to offer a voluntary student loan benefit program. In a ruling directly applicable only to the employer involved but potentially with more far-reaching implications, IRS concluded that the proposed plan design will not violate the contingent benefit rule.

Specifically, under the program as proposed, the employer would make a nonelective contribution to the 401(k) plan at the end of the year — in lieu of the existing payroll period match on elective deferrals — conditioned on the participant making a student loan repayment. If the participant makes a loan repayment and a contribution to the plan in a pay period, the participant would be eligible to receive the nonelective contributions at the end of the year — if the participant does not make a loan repayment but does make a contribution to the plan in a pay period, the participant would be eligible to receive a "true-up matching contribution" at the end of the year. Both contributions — nonelective and true-up matching — would be subject to the participant being employed on the last day of the plan year (except in the case of death or disability). The nonelective contributions would be subject to applicable plan qualification requirements — including eligibility, vesting, and distribution rules, contribution limits, and coverage and nondiscrimination testing. They would not be considered matching contributions for nondiscrimination testing purposes. All employees eligible to participate in the plan would be eligible to participate in this program. A participant can opt out of enrollment on a prospective basis, and thereby resume eligibility for matching contributions.

Student Loan Benefit Program Does Not Violate the Contingency Prohibition

In the PLR, the IRS ruled that since the nonelective contributions under the student loan program are conditioned on repayment of the student loan and not on the participants making elective contributions under the plan, there is no violation of the contingent benefit prohibition. The IRS further reasoned that because the employee can make elective contributions in addition to student loan repayments, the nonelective contribution is not directly or indirectly conditioned on the employee choosing to make or not make elective contributions.

Nondiscrimination Testing May Be A Roadblock

In the PLR, the IRS was careful to describe the contribution to the 401(k) plan as a nonelective contribution and made it clear that a participant could not receive a regular match at the same time as a nonelective contribution. For these reasons, the structure of the program in the PLR precludes its use in safe harbor plans because the participants in the loan program are not simultaneously eligible for the safe-harbor match if they make elective contributions. Assuming these are the only nonelective contributions in the plan and that the benefiting group with student loan debt is generally comprised of nonhighly compensated employees, the nonelective contributions should pass the general 401(a)(4) nondiscrimination test easily. Conversely, reduced elective deferrals and matching contributions by these participants may make passing the Actual Deferral Percentage (ADP) and Actual Contribution Percentage (ACP) tests difficult. Employers should consider these demographic issues before adopting a similar student loan repayment program.

> **Note:** Administratively, employers might find it challenging to manage their payroll data to trigger matching contributions when an employee stops making student loan payments but continues or starts elective contributions.

What About Employees Who Do Not Have Student Loan Debt?

Employer-provided loan repayment assistance is helpful to some employees, but what about the bulk of the population who do not have student loans? How can an employer help employees towards their retirement, as well as other financial goals? Many employers offer tools to foster financial well-being, but many have been concerned

that the contingent benefit prohibition precludes making nonelective contributions to a 401(k) plan dependent upon an action by participants (for example, completion of a tutorial on balancing a budget). This PLR could serve as an impetus for rethinking how employers can more effectively incentivize good financial behavior through contributions to a qualified plan.

In Closing

Although the PLR can only be relied on by the employer that requested it and does not address potential nondiscrimination testing issues or plans that may be structured differently, it may nevertheless serve as a template for employers wishing to help employees achieve financial wellness goals. They may see the framework of the PLR as a “win-win” — an attractive recruitment and benefit tool that helps employees address their student loan debt and enhance retirement preparedness, while not costing the employer more than the maximum amount of matching contributions already promised under the plan.

Authors
Joanne Jacobson, JD, LLM
Julia Zuckerman, JD

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