401k v. 403b

EMPLOYEE ELIGIBILITY

401(k) plans allow employers to customize who's eligible for the plan. Most 403(b) plans must make all employees immediately eligible for the plan.

401(k) vs. 403(b)

- Tailor eligibility to meet the realities of the organization (high turnover, large number of part-time workers, etc.), often avoiding costly large-company audits required by the DOL.
- Generally, nonprofits need to make all employees immediately eligible for the 403(b), even part-time workers or workers that aren't expected to stay at the organization all that long.

If you're a nonprofit that has a large workforce and high turnover, then you can very quickly be subject to a large plan audit, which is generally required when a plan has more than 100 eligible employees. The large plan audit applies to plans with over 100 participants and can be very expensive (likely between $15k-$20k).
By setting up a 401(k) with a smarter eligibility period, many nonprofits are able to delay or avoid altogether reaching the 100 eligible employee threshold that can trigger the expensive audit. Employee eligibility periods allow organizations to be strategic with the benefit by only making it available to employees that are committed to staying with the organization — reducing administrative costs and helping you retain your best talent.

COMPLIANCE

ERISA 403(b) plans and ERISA 401(k) plans are subject to essentially the same ERISA requirements.

401(k) vs. 403(b)

- Annual Form 5500 filing
- Large plan audit for organizations with over 100 employees
- Subject to three out of three IRS non-discrimination tests
- Annual Form 5550 filing
- Large plan audit for organizations with over 100 employees
- May only be subject to two out of three IRS non-discrimination tests (not subject to the Top Heavy test)

In rare cases, a 403(b) plan can qualify to be a non-ERISA plan, which reduces compliance work significantly. However, many common elements found in retirement plans — including offering a company match — immediately disqualify a nonprofit from offering a non-ERISA plan.

CONTRIBUTION LIMITS

Both 401(k) and 403(b) plans enjoy the same annual contribution limits.

401(k) vs. 403(b)

- Employee contribution limit in 2016: $18,000
- Age 50+ catch-up contribution limit: $6,000
- Employee contribution limit in 2016: $18,000 – $21,000 (depending on the type of nonprofit, employee contribution history and service with the employer)
- Age 50+ catch-up contribution limit: $6,000

INVESTMENT SELECTION

401(k) plans allow more investment options than 403(b) plans.

401(k) vs. 403(b)

- Mutual funds, individual securities, exchange-traded funds, annuities
- Brokerage windows are allowed
- Assets in a 403(b) plan can be placed in any of the following investment types:
  - an annuity contract provided through an insurance company;
  - a custodial account invested in mutual funds;
  - or a retirement income account set up for church employees.
- No brokerage windows are allowed

The wider range of investment options can help organizations find lower-fee funds that meet the needs of their employees. This is important, as excessive fees can dramatically reduce your employees' retirement savings.

Giving your employees a broader set of lower cost investment options is a compelling reason to consider switching your group away from a 403(b) plan. If nothing else, it is likely worth your time to benchmark your plan's investment options against what is possible with a modern 401(k) plan.

Looking to make a 403(b) change?

If you're looking to offer an employer match at some point, give employees a broader set of investment options, and customize employee eligibility then the 401(k) plan might be the right option for you.