

California Education Code 44041.5

44041.5.(a) For purposes of this section, the following definitions shall apply:

(1) "Annuity contract" means an annuity contract described in Section 403(b) of the Internal Revenue **Code** that is available to employees as described in Section 770.3 of the Insurance **Code**.

(2) "Custodial account" means a custodial account described in Section 403(b)(7) of the Internal Revenue **Code**.

(3) "Deferred compensation plan" means a plan described in Section 457 of the Internal Revenue **Code**.

(4) "Employer" means a school district or county office of **education**.

(5) "Third-party administrator" means a person or entity that provides administrative or compliance services to an employer as described in subdivision (b).

(b) An employer may enter into a written contract with a third-party administrator for services regarding an annuity contract and custodial account or a deferred compensation plan provided by the employer. That contract may include any of the following:

(1) Services to ensure compliance with either Section 403(b) of the Internal Revenue **Code** regarding the annuity contract and custodial account or Section 457 of the Internal Revenue **Code** regarding a deferred compensation plan, including, but not limited to, any of the following:

(A) Administer and maintain written plan documents governing the employer's plan.

(B) Review and authorize hardship withdrawal requests under Section 403(b) of the Internal Revenue **Code**, transfer requests, loan requests, unforeseeable emergency withdrawals under Section 457 of the Internal Revenue **Code** and other disbursements permitted under either Section 403(b) or 457 of the Internal Revenue **Code**.

(C) Review and determine domestic relations orders as qualified domestic relations orders as described in Section 414(p) of the Internal Revenue **Code**.

(D) Provide notice to eligible employees that is consistent with Title 26 of the **Code** of Federal Regulations that those employees may participate in an annuity contract and custodial account.

(E) Administer and maintain specimen salary reduction agreements for the employer and employees of that employer to initiate payroll deferrals.

(F) Monitor, from information provided either directly from the employee, as part of the common remitting services provided pursuant to paragraph (2), through information provided by the employer, or through information provided by vendors authorized by the employer to provide investment products, the maximum contributions allowed by employees participating in either the annuity contract and custodial account as described

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in Sections 402(g), 414(v), and 415 of the Internal Revenue **Code** or the deferred compensation plan as described in Section 414(v) or 457 of the Internal Revenue **Code**.

(G) Calculate and maintain vesting information for contributions made by the employer to the annuity contract and custodial account or deferred compensation plan.

(H) Identify and notify employees that are required to take a minimum distribution of the funds in that employee's annuity contract and custodial account or deferred compensation plan as described in Section 401(a)(9) of the Internal Revenue **Code**.

(I) Coordinate responses to the Internal Revenue Service if there is an Internal Revenue Service audit of the annuity contract and custodial account or deferred compensation plan.

(2) Services to administer the annuity contract and custodial account or a deferred compensation plan that includes, but is not limited to, all of the following:

(A) Common remitting services.

(B) General educational information to employees about the annuity contract and custodial account or the deferred compensation plan that includes, but is not limited to, the enrollment process, program eligibility, and investment options.

(C) Internal reports for the employer to ensure compliance with either Section 403(b) or 457 of the Internal Revenue **Code** and compliance with Title 26 of the **Code** of Federal Regulations.

(D) Consulting services related to the design, operation, and administration of the plan.

(E) Internal audits, on behalf of an employer, of a provider's plan compliance procedures with respect to the provider's annuity contract or custodial account offered under the employer's plan. These audits shall not be conducted more than once per year for any provider's plan unless documented evidence indicates a problem in complying with either Section 403(b) or 457 of the Internal Revenue **Code**.

(c) (1) If an employer elects to contract with a third-party administrator for the administrative or compliance services to employers described in subdivision (b), the employer shall do all of the following:

(A) Require the third-party administrator to provide proof of liability insurance and a fidelity bond in an amount determined by the employer to be sufficient to protect the assets of participants and beneficiaries in the annuity contract and custodial account or deferred compensation plan.

(B) Require the third-party administrator to provide evidence of a safe chain-of-custody of assets process for ensuring fulfillment of fiduciary responsibilities and timely placement of participant investments.

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(C) Require evidence, if the third-party administrator is related to or affiliated with a provider of investment products pursuant to Section 403(b) or 457 of the Internal Revenue **Code**, that data generated from the services provided by the third-party administrator are maintained in a manner that prevents the provider of investment products from accessing that data unless access to the data is required to provide the services in accordance with the contract entered into with the employer pursuant to subdivision (b).

(2) This subdivision shall apply to any administrative or compliance services provided pursuant to a contract for services between an employer and the State Teachers' Retirement System if the system does not contract with a third-party administrator to provide those administrative and compliance services on behalf of the system.

(d) A third-party administrator shall disclose to any employer seeking his or her services any fees, commissions, cost offsets, reimbursements, or marketing or promotional items received by the administrator, a related entity, or a representative or agent of the administrator or related entity from any plan provider selected as a vendor of an annuity contract, custodial account, or deferred compensation plan by the employer. A third-party administrator that is affiliated with or has a contractual relationship with a provider of annuity contracts, custodial accounts, or deferred compensation plans shall disclose the existence of the relationship to each employer and each individual participant in the annuity contract, custodial account or deferred compensation plan.

(e) Any personal information obtained by the third-party administrator in providing services pursuant to this section shall be used by the third-party administrator only to provide those services for the employer in accordance with the contract entered into with the employer pursuant to subdivision (b).

(f) Nothing in this section shall be construed to interfere with either of the following:

(1) The rights of employees or beneficiaries as described in Section 770.3 of the Insurance **Code**.

(2) The ability of the employer to establish nonarbitrary requirements upon providers of an annuity contract that, in the employer's discretion, aid in the administration of its benefit programs and do not unreasonably discriminate against any provider of an annuity contract or interfere with the rights of employees or beneficiaries as described in Section 770.3 of the Insurance **Code**.

(g) This section shall not apply to any services provided by a third-party administrator pursuant to a contract for services between an employer and the State Teachers' Retirement System. Any services provided by a third-party administrator pursuant to a contract for services between an employer and the State Teachers' Retirement System shall be subject to either Section 24953, in the case of an annuity contract or custodial account, or Section 24977, in the case of a deferred compensation plan.



District Business & Advisory Services

Nimrat Johal: Director- DBAS: 408-453-6599

Cathy McKim, Manager-DBAS: 408-453-6588

Bulletin: 11-004

Date: March 10, 2011

To: District Fiscal Directors

From: Cathy McKim

Re: Third Party Administrators (TPA)
Education Code 44041.5 - Why is this important?

Section 44041.5 of the California Education Code authorizes an employer to enter into a written contract with a third-party administrator (TPA) to ensure compliance with employer sponsored plans under either section 403(b) or 457 of the Internal Revenue code. If a district elects to contract with a TPA, the *code requires* that the employer obtain the following from the TPA:

- Proof of liability insurance and a fidelity bond sufficient to protect assets in the plan.
- Provide evidence of a safe chain-of-custody of assets process.
- Disclose any affiliation to a provider of investment products.
- Disclose any fees, commissions, cost offsets, or reimbursements received
- Ensure that any personal information obtained by the TPA shall be used only to provide compliance services.

Many districts elected to work with a TPA without knowledge of this code section. It's advisable to review these points with your TPA to ensure they, and therefore your district, are compliant with this code.

As the IRS has made their intention to conduct audits of 403(b) plans clear; it's in every districts best interest to ensure their plans are compliant not only with this, but with the new IRS regulations as well. Inclusive in the IRS regulations is the requirement that the employer review contributions for compliance purposes. The Common Remitter vendor for the county is tasked with providing every TPA contracted by individual districts with an electronic payroll file. This file is posted on a secure website and is accessible by your authorized TPA only. The purpose of this file is to ensure your TPA has the needed information to conduct a compliance review on a monthly basis. It has been brought to our attention that some TPA's



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are NOT reviewing this file and are not getting the information from the district directly. If the files are not being reviewed, items such as over-contributions and disallowed contributions could be getting missed. This means that the plan could be out of compliance creating potentially severe penalties for the district.

Every district in the county has the right to contract with a TPA of their choice; the point here is to ensure that your TPA is compliant with the code and doing their job for you. Ultimately the responsibility of a plan compliant with IRS regulations falls on the district and not the TPA, Common Remitter, or any other party.

The education code cited in this advisory has been attached for your further review.

Approved:

Nimrat Johal, Director-District Business & Advisory Services