Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE

LOAN PROVISION
January 30, 2013

Requirements

- IRC 457(b) allows loan programs for participants and beneficiaries, but it is not a plan requirement
- Maximum amount - the lesser of:
  - 50% of the account balance or
  - $50,000, reduced by any outstanding loan
- Repayment
  - General Purpose Loan: Repaid within five years in amortized periodic installments
  - Residential Loan: Must be used to acquire a principal residence and loan repayment period may be for up to 30 years
  - Reasonable interest rates – usually Prime plus 1%

Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE

Avoiding Taxation

- If the loan and interest are repaid according to the terms of the agreement, it is not a taxable event
- If the participant defaults on loan payments, the loan and outstanding interest payments become a “deemed” distribution subject to taxation
- IRC Section 72(p) does not prohibit a participant from borrowing from a plan more than once per year, but loans from all plans must be aggregated to avoid exceeding maximum

Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE

Defaults

- Loan considered in default if the participant:
  - Fails to make scheduled repayments
  - Obtains a loan that exceeds IRC maximum amount
- Automatic default occurs at the end of the quarter following the quarter the last payment was received; outstanding loan balance then “deemed” to be a taxable distribution
- No further follow-up by staff on defaults – recordkeeper will notify participant and issue 1099 for unpaid balance
- If terminated participants are not allowed to continue repaying, the loan is considered an “offset” and becomes a taxable distribution either when a distribution is taken or when the default grace period has expired

Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE

Hardship Withdrawal or Loan?

- Participant may be required to take out loan before obtaining unforeseen emergency withdrawal
  - A best practice, but not a requirement
  - Based on ERISA rules to explore all avenues before taking a taxable event
  - Would be addressed in Plan Document
- According to a recent survey by NAGDCA, of 76 respondents, 39 or 51% offered loans

Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE

Hardship Withdrawal or Loan?

- Responding plans from NAGDCA survey require participants to exhaust the following options before authorizing a hardship withdrawal:
  - Stop deferrals – 43%
  - Take a plan loan – 24%
  - No requirements – 20%
  - Not applicable (no hardship withdrawal offered) – 19%
  - Other – 17% (exhaust financial reserves, personal loan, sale of non-essential assets, loans from other plans)
- 68% of responding plans allow participants to temporarily suspend loan payments while on an unpaid or partially paid leave of absence

Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE

Considerations

- Eligibility is based on employment status, not participant status
- Default monitoring – NDC staff to oversee loans from all plans
- Loan Authorization – who is responsible for authorizing disbursements – logically NDC staff who will be able to review loan applications from both plans
- Must have a legally enforceable loan document (each plan has their own loan forms)
- Determine minimum loan term (usually 12 months)
- Set amount of loan origination fee, if any (currently $100-ING)
- Establish minimum loan amount ($1,000 is common)

Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE

Further Considerations

- Set maximum number of plan loans a participant may take at one time
  - Example: One loan with each provider would be considered two plan loans
- Loans not available for retirees
- It is the most complicated of all plan services provided
  - Military leaves of absence must be considered
  - Extended leaves of absence
  - Separation from service

Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE

What's Next

- Program must meet lending provisions similar to those required of a bank
- Amend provider contracts and agreements
- Update plan documents and develop custom internal forms, if required, to properly administer loans between providers
- Develop and implement workflows and policies
- Delineate responsibilities of providers and NDC office; approval/denial process
- Decide who is responsible for determining interest rates
- Communicate policy to participants
- Set up ACH payment process with participant's bank

Nevada Deferred Compensation
YOUR PLAN...YOUR FUTURE