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Answers to Questions About 403(b) Plans

By TARA SIEGEL BERNARDOCT. 21, 2016

What are they, and who uses them?

The so-called 403(b) plans are tax-deferred workplace retirement investment accounts, which are similar in many ways to their more widely used counterparts, 401(k) plans.

They are typically offered to employees of public school systems, religious organizations, private schools and universities, as well as nonprofit organizations, including charities and hospitals.

Corporations that want to offer retirement plans must generally offer 401(k)'s. The rules are different for public schools, which generally must offer 403(b)'s, consultants say. Nonprofits and religious groups have some flexibility, but offering 403(b)'s often can be simpler for them as employers.

Why do they exist?

These accounts predate 401(k) plans. When Congress introduced 403(b) plans in 1958, they were viewed as supplemental pensions for teachers, and the only permissible investments were annuities, according to tax experts and consultants. The plans themselves, named for a section of the tax code, were called "tax-sheltered annuity arrangements." Mutual funds weren't available until 1974.

Who regulates them?

That depends. First, some background: 401(k) retirement plans are covered by the Employee Retirement Income Security Act of 1974, overseen by the Labor Department. The law outlines minimum guidelines and protections for workers and requires employers or plan overseers to act in the best interests of participants.

Here is where it gets more complicated. Governmental 403(b) plans — including public schools — are always exempt from Erisa (and it would take an act of Congress to change that). Instead, exempt plans are covered by a patchwork of state laws or less stringent federal securities regulations.

Church 403(b) plans are also generally exempt from Erisa, unless they opt to follow those rules.

Plans run by certain nonprofits may or may not be covered by the more stringent federal law, depending on the employer's role in the plan. If a nonprofit employer offers a match, for example, it must comply with Erisa regulations. Some nonprofits choose to offer 401(k) plans instead of 403(b)'s.

Whatever their differences, all 403(b) plans are tax-deferred vehicles, so they must, at a minimum, follow Internal Revenue Service regulations to ensure the plans are properly operated and administered.

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