Employers Get (Somewhat) Good News From IRS About Matching Contributions To Repay Student Loan Debt

Insights
11.30.18

In the recently issued PLR, an employer sought confirmation from the IRS that its proposed Student Loan Benefit Program did not violate the "contingent benefit" rule found in the Tax Code which, prohibits employers from conditioning "other benefits" on an employee's making (or not making) 401(k) contributions. Employer-matching contributions are specifically exempt from this requirement.

The employer explained to the IRS that its program would be part of its 401(k) plan, which provides for a regular employer-matching contribution equal to 5 percent of the employee's compensation for each pay period that the employee contributes 2 percent or more of their compensation. Under the program, if an employee makes a student loan repayment equal to at least 2 percent of their eligible compensation for a pay period, the employer would make a contribution to the plan equal to 5 percent of the employee's compensation for that period. This contribution would be made as soon as practicable after the end of the year, but only if the employee is still employed at the end of the year (unless termination was due to death or disability).

Further, employees enrolled in the program would not be required to make a student loan repayment each pay period and could opt out at any time. Enrolled employees who did not make a qualifying student loan repayment for a pay period, but who made an elective contribution to the plan equal to at least 2 percent of their compensation, would receive a "true-up" employer-matching contribution after the end of the year for that pay period if the employee is still employed at the end of the year.

The IRS ruled that the employer's program did not violate the contingent benefit rule. It explained that employer contributions under the program were not conditioned on the employee making (or not making) elective contributions to the 401(k) plan because (1) the employer contributions were conditioned on the employee making a student loan repayment, not plan contributions; and (2) employees participating in the program could still make elective contributions. However, this ruling was conditioned on the assumption that the plan sponsor will not extend any student loans to eligible employees.

Reactions To The IRS Ruling

The PLR triggered a sigh of relief for many employers utilizing similar programs, and an outbreak of interest from employers interested in establishing comparable arrangements. However, you should consider the risks associated with relying on the PLR before adding a similar program to your 401(k) plan.

Importantly, a PLR is only intended to provide guidance to the inquiring taxpayer. Unlike other IRS guidance, a PLR cannot be used or cited as precedent by other taxpayers or by IRS personnel. PLRs also are only intended to answer the narrow question presented by the taxpayer and not to comment generally on the plan's compliance with the Tax Code.

What Does This Mean For You?

The PLR provides useful insight into the IRS's thinking. However, because it is narrow in scope and cannot be relied on by other taxpayers, you should exercise some caution before diving into a similar arrangement. Additionally, the cost and administrative logistics associated with incorporating such a program can be troublesome and may be rejected by third-party administrators and document providers.

The renewed interest in student loan benefit programs will likely result in more plans adopting similar programs. Accordingly, we anticipate the IRS will eventually respond with more formal, broadly applicable guidance. Until then, you should seek advice from your Fisher Phillips counsel to assess the compliance risks associated with adding a student loan repayment program to your benefit options.

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