How Employers Can Help Employees Pay Off Student Loans *and* Save for Retirement

$1.3 trillion...that's how much student loan debt Americans had incurred by the end of June 2017. During that same time period, the Pew Research Center estimates that 37 percent of adults ages 18 – 29 had outstanding student loans[1].

As these statistics show, paying for college doesn't just end at graduation; it can go on for years. Getting younger employees to save for retirement is already challenging. And for those facing crippling student loan debt, it may be impossible. In response to this growing financial crisis, some employers have found a way to help employees pay off their student loan debt *and* save for retirement.

New Solution Found in IRS Guidance

On August 17, 2018, the IRS released private letter ruling (PLR) 201833012, which allows a proposed employer 401(k) plan feature to be associated with employees' student loan payments.

Under the proposed 401(k) plan feature, if an employee affirmatively elects to participate in the employer's student loan benefit program and makes a student loan payment equal to at least two percent of her compensation during a pay period, the employer will make a nonelective contribution (also known as a "profit sharing contribution") of five percent of that pay period's compensation to the employee's 401(k) plan account.

Some in the media have mistakenly referred to this proposed nonelective contribution as a "matching contribution". Although the PLR's proposed contribution formula would be identical to the 401(k) plan's current matching contribution formula (i.e., all eligible employees who defer at least two percent earn a matching contribution of five percent), a matching contribution is defined as an employer contribution made on behalf of an employee who makes a 401(k) plan deferral contribution. Under the PLR, the proposed contribution would be made only if an employee made a student loan payment—not a 401(k) plan deferral contribution.

The Best of Both Worlds

The PLR clarifies that an employee who participates in the student loan benefit program could simultaneously defer her salary into the 401(k) plan, and—if deferring at least two percent—earn the 401(k) plan's five percent matching contribution during those pay periods when she chooses not to make a student loan payment.

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[1] Anthony Cilluffo, "5 Facts About Student Loans", Pew Research Center, August 24, 2017, accessed August 23, 2018, http://www.pewresearch.org/fact-tank/2017/08/24/5-facts-about-student-loans/.

Example: Jane Smith, age 28, earns $36,000 per year and gets paid $1,384.62 every two weeks. Jane also owes $47,000 on her student loan and is enrolled in her employer's student loan benefit program. On September 7, 2018, Jane makes a $27.69 student loan payment (2% of $1,384.62). She also makes a 2% salary deferral ($27.69) to her 401(k) plan account. Jane's employer will make a $69.23 nonelective contribution to her 401(k) plan account for the student loan payment, but will not make a matching contribution for the salary deferral. On September 21, 2018, Jane does not make a student loan payment, but does make another 2% salary deferral to her 401(k) plan account. Therefore, Jane's employer will make a 5% matching contribution (based on her salary deferral) to her 401(k) plan account.

Clarification on Open Questions

The PLR states that the proposed nonelective contribution is subject to plan qualification rules including—but not limited to—eligibility and contribution rules as well as coverage and nondiscrimination testing. The PLR also mentions that because receipt of the nonelective contribution is contingent upon the student loan payment and not upon an employee deferring (or not deferring) into the employer's 401(k) plan, there is no conflict with the contingent benefit rules. (See Internal Revenue Code Section 401(k)(4)(A).)

Next Steps - How Can Other Employers Make Similar Contributions?

The student loan benefit program described in the PLR is just one way employers may design their retirement plan to simultaneously encourage repayment of student loans and help employees save for retirement. Employers who are interested in implementing a student loan benefit program similar to that described in the PLR should consider visiting with their attorney to determine whether to proceed because a PLR may be relied upon only by the party to whom it is issued.

If a decision to amend the plan to incorporate such a program is made, the employer should consult its plan record keeper or third-party administrator to discuss available options.
The easiest path for an employer with access to pre-approved plan documents is to have a customized volume submitter document prepared on its behalf. If an employer is flexible in how its program is designed, there may be other options (e.g. new comparability allocation formulas) that will allow the employer to satisfy its objective.