Mueller Prost
CPAs + Business Advisors

BENEFITS IN BRIEF

COMPLIANCE MATTERS:

How Plan Sponsors Get Into Trouble

As beneficial as it may be to your employees and your company, sponsoring a tax-qualified retirement plan is not without its risks. The rules are complex and ever-changing, and the IRS cuts plan sponsors no slack. Penalties for noncompliance — even unintentional errors — may be severe, and can even result in the loss of a plan's tax-qualified status.

Learn from Others' Mistakes

There are a number of common mistakes plan sponsors make that can cause them to run afoul of IRS regulations. Consider these typical compliance errors:

- **Not following the terms of the plan document**
  The plan document must not only comply with the Internal Revenue Code (IRC), but its provisions must also be followed to the letter. In other words, how your plan is being operated today must exactly match the original plan document. For example, if as a matter of practice the plan uses automatic enrollment — which is permitted by the IRC — but the plan document does not state that automatic enrollment is allowed, the plan is in violation of the plan document and the IRC.

  Action: Perform periodic reviews of plan activities to ensure compliance with the plan document. In addition, communicate any changes to your plan document or plan operations to your human resource and payroll personnel, plan service providers and plan participants.

- **Incorrectly including or excluding plan participants**
  For 401(k) plans, minimum service requirements may be established to determine eligibility for an employee to participate. Of course, this needs to be specifically defined in the plan document and can be hours-based or service-based (i.e., 1,000 hours in an annual period or some defined period of time after the start of employment). Common eligibility errors include:
  - Inclusion of union employees who are not eligible.
  - Prematurely providing an employer match.
  - Incorrectly applying eligibility dates.

  Action: The plan sponsor is ultimately responsible for maintaining an accurate list of eligible participants. Provide current plan provisions and census data to your third-party administrator and have them determine if you have improperly excluded any class of employees. Also make sure to document that you have notified employees of their eligibility to begin participating in the plan, as well as maintain documentation of participants who elect not to participate.

- **Making mistakes with participant loans**
  Participant loans must meet strict rules so the IRS doesn't consider them to be taxable distributions to employees. Mistakes come in many different forms, including:
  - Permitting loans that are too large. In general, participant loans cannot exceed $50,000 or 50 percent of the employee's vested account balance.
  - Granting repayment terms that are too long. Five years is generally the maximum loan term, unless the loan is for a principal residence.
  - Failure to obtain/require a spouse's signature on a loan document. As pension assets are considered communal property, many plans require spousal consent for a loan (although this is not federally mandated). It is a common error for a plan to not be in compliance with this aspect of the plan document/provisions.
  - Charging an unreasonable interest rate. Employees should pay the same interest rate they would expect to receive from a financial institution, which is most commonly prime plus 1 percent.

  Action: Go back and review the loan provisions in your plan document. Compare these to participant loan agreements to make sure that all plan loans have been made in compliance with the plan document and that the plan document complies with IRC Section 72(p).

- **Not remitting employees' contributions in a timely manner**
  All participant contributions must be remitted to the retirement plan on the earliest date on which they can reasonably be segregated from the company's general assets. In no case can this be later than the 15th business day following the end of the month in which amounts are contributed by employees or withheld from their wages. However, the key consideration is the earliest date that the assets can be reasonably

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segregated. For most plans, this will be less than the 15-day maximum period and based on the historical timing of contributions. For many plans, this could be as little as a couple of days.

It should be noted that a safe harbor provision is in place for small retirement plans, which are defined as plans with fewer than 100 eligible participants on the first day of the plan year. For these plans, employee contributions and loan payments are considered to be timely if they are deposited to the plan no later than the seventh business day following the pay date.

Action: If you are a large plan, consider your processes and determine the earliest date that employee deferrals/contributions can be segregated and remitted. Make sure you have monitoring controls in place to ensure remittances are made according to schedule. If you do make a late remittance, consider entering the Department of Labor's Voluntary Fiduciary Correction Program, which allows you to calculate lost earnings on the late contributions and make corrective contributions without penalty. If a remittance is made later than a plan typically would, but it is not determined to be late, the plan administrator should document the circumstances that account for the longer contribution period.

- **Incorrect hardship distributions or inadequate documentation of a hardship distribution**

  the plan document dictates the terms of a hardship withdrawal and the vesting of the employer contributions. Any distribution must adhere to the plan provisions. Hardship distributions are allowed for specific reasons defined by ERISA (from meeting medical and funeral expenses to preventing eviction from/foreclosure on a principal residence).

  A hardship distribution may not exceed the amount of the need. However, the amount required to satisfy the financial need may include amounts necessary to pay any taxes or penalties that may result from the distribution. Further, hardship withdrawals are subject to income tax and, if the participant is not at least 59½ years of age, the 10 percent withdrawal penalty. Plan sponsors must maintain documentation and approve these distributions to ensure they meet the requirements for hardship. And when a hardship distribution is taken, the participant's contributions must be stopped for six months.

  Action: Develop a process internally or with the assistance of a third-party service provider to ensure that the basis for hardship distributions is clearly documented and that the amounts distributed are calculated based on the participant's available benefits and needs for the hardship event.

The Buck Stops Here

Many plan sponsors choose not to go it alone, instead relying on a number of outside service providers to maintain the plan. Unfortunately, outsourcing operation of your retirement plan does not relieve your organization of liability for noncompliance. In addition, the named plan administrator (the individual who signs the plan's Form 5500) may also be personally liable. The bottom line is that the plan sponsor is always responsible for the plan's operation.

With so many compliance challenges, many plan sponsors choose to outsource plan operations to third-party administrators. Yet, outsourcing does not relieve you of liability for noncompliance.

Do you have questions about compliance? Contact your Mueller Prost advisor for guidance 314.862.2070.

FEE DISCLOSURES:

DOL Simplifying Fee Disclosure Requirements

In 2012, the U.S. Department of Labor's Employee Benefits Security Administration issued regulations (Section 404(a)(5) of ERISA) that require plan sponsors to provide detailed information about plan fees and investment options to participants. Included with the participant disclosure requirement were regulations addressing how service providers disclose their fees to plan sponsors and participants, which are covered by Section 408(b)(2).

The regulations were intended to help plan fiduciaries better understand the range and value of services that they and plan participants receive from providers and to ensure the compensation of the services providers is reasonable.

While this sounds good in theory, the DOL has acknowledged that many of the disclosure forms are long and confusing. A recently proposed DOL rule promises to simplify the process by making it easier for plan sponsors and participants to locate and understand the fees and expenses associated with a plan. The DOL is currently seeking input from various stakeholders before finalizing the new rule.

Fiduciary Duty Remains

Even if plan sponsors do comply with the disclosure requirements and ensure that the information is disseminated properly, they are still not alleviated of their fiduciary duty under ERISA to determine the reasonableness of all fees. As a plan sponsor, you are required to thoroughly review fees to benchmark or compare against industry norms, and review the disclosures (which are typically based on information provided by the plan's service providers) to verify that the information meets the disclosure requirements. As a fiduciary, you will need to evaluate the need to make changes in your service provider relationships if you determine that fees are too high.

You can assume responsibility for reviewing fee disclosures yourself or hire advisors to help you with this task. However, if your service provider does not provide the required fee disclosures, your contract or agreement with the provider is considered to be prohibited by ERISA — and you will have engaged in a prohibited transaction. This could result in excise taxes and penalties being assessed against your company.

The DOL regulations do provide some relief should a service provider fail to adequately disclose fee information. However, this relief is limited and only applies in certain situations:

- You must not have known that the service provider failed (or would fail) to comply with the disclosure rules.
- You must have reasonably believed that the provider disclosed (or would disclose) the required fee information.
- If you discover that the service provider has failed to comply with the disclosure rules, you must make a written request for the missing information from the service provider.
- If the service provider does not provide the requested fee information within 90 days, you must notify the DOL of this failure. You can do so via the DOL's Fee Disclosure Failure Notice, which you can access at www.dol.gov/ebsa/regs/feedisclosurefailurenotice.html. You also must decide at this time whether or not to terminate your contract with the service provider.

The DOL is trying to make it easier for plan sponsors and participants to locate and understand the fees and expenses associated with a plan.

Review Contracts and Agreements

Because of these changes, now is a good time to review your contracts and agreements with your service providers. Your goal should be to make sure that you are in material compliance with the DOL's fee disclosure regulations.

In particular, look carefully at the contract's termination provisions. You want to have flexibility to terminate an agreement quickly and easily if the service provider fails to comply with the fee disclosure requirements. Also examine the contract's provisions dealing with fee schedule changes. Consider adding provisions to your agreements that give you as much protection as possible should the service provider fail to comply with the fee disclosure requirements.

How Service Provider Fees Are Calculated

Service providers typically determine plan fees using one, or a combination, of the following methods:

- Asset-based – Fees are based on the amount of assets in the plan and generally are expressed as percentages or basis points.
- Per-person – Fees are based on the number of eligible employees or actual plan participants.
- Transaction-based – Fees are based on the delivery of plan services or transactions.
- Flat-rate – Fees are based on a fixed charge, regardless of the plan's size.

If you have more questions about retirement plan fee disclosures, please contact Mueller Prost at 314.862.2070.

Understanding Your Investment Fiducuary Duties

When it comes to performing investment fiduciary duties, plan sponsors generally fall into one of three categories:

1. They are comfortable selecting the investment menu without any advice or assistance from an outside registered investment advisor (RIA). Here, the plan sponsor acts as the sole named investment fiduciary and assumes full liability for the selection of the plan's investment options.

2. They would like some assistance from an RIA. This is known as a 3(21) fiduciary assistance scenario, in which the RIA is acting as an investment advisor that is a limited-scope, section 3(21) fiduciary to the plan. The RIA can provide a wide range of services — from investment consulting to help with plan design, vendor selection and participant communication and education. But, when they hire an RIA as a 3(21) fiduciary, plan sponsors still retain some degree of fiduciary responsibility for the selection and monitoring of investment options for the plan. If it is later determined that one of the RIA's recommended investment options is inappropriate under ERISA, the sponsor is still liable.

3. They would like an RIA to select and monitor the investment menu. This is known as a 3(38) investment manager scenario. The RIA acknowledges in writing that it is acting as a fiduciary to the plan, and accepts full discretionary authority for making all plan investment decisions. This includes managing, acquiring and disposing of investment options over time. The plan sponsor is not completely relieved of investment responsibility in a 3(38) scenario, but the sponsor's potential liability is defined very narrowly.

No matter what category a plan falls under, it is essential that the sponsor understand the limitations on the services they are receiving and the liability that is being assumed or not assumed by their investment advisors.

Please contact your Mueller Prost advisor if you have more questions about your investment fiduciary responsibilities. 314.862.2070

For more information, please contact **Quinn R. Martin, CPA, MBA** or **MaryPat Davitz, CPA, CITP** at 314.862.2070 or **qmartin@muellerprost.com** and **mdavitz@muellerprost.com**.