



Year-End Planning for Benefit Professionals

Presented by

Marcia Wagner, Esq.

The Wagner Law Group

125 High Street, Oliver Street Tower, 5th Floor

Boston, MA 02110

617.357.5200 / www.wagnerlawgroup.com

Introduction

- ◆ Today's presentation has two components
- ◆ Required year end 2022 actions
 - Execution of certain plan amendments
 - Correction of ADP/ACP 2021 plan failures
 - Distribution of 401(k) Plan Notices for 2023 Plan Year
 - Required Minimum Distributions under Code Section 401(a)(9)
 - Conclusion of Code Section 410(b)(6) transition period for events occurring in 2021 plan year
- ◆ Recommended best practices for 2023 plan year

401(k) Plan Notices

- ◆ Number and type of notices depends on plan design:
 - ACA Disclosure Notice
 - QACA Disclosure Notice
 - EACA Disclosure Notice
 - QDIA Notice
 - Participant Fee Disclosure
- ◆ Combined DB/DC Plan under Code Section 414(x) can use same type of notice as ACA Disclosure Notice.
 - Generally provided 30-90 days before beginning of plan year.

401(k) Plan Notices

- ◆ 401(k) plan notices must satisfy the following conditions:
 - Comprehensive and sufficiently accurate to inform employees of their rights and obligations under the retirement plan's; and
 - Understandable by the average employee.

QACA Notice

- ◆ QACA Notice must explain the following:
 - The plan's default percentage rate for automatic enrollment contributions, including the amount and timing of any increases;
 - The type and the amount of any employer contributions;
 - The right to not participate; and
 - How to elect not to participate.

QACA Notice

- How to elect to contribute an amount different from the plan's default percentage rate for automatic enrollment contributions.
- How to make an investment election, if plan permits this.
- If QACA contains two or more investment options, how the plan will invest automatic enrollment contributions if the employee does not elect investment options.
- Plan sponsor may also be required to provide additional information to employee under DOL regulations.

EACA Notice

- ◆ EACA notice must contain the following:
 - The plan's automatic enrollment contributions default percentage rate;
 - The right not to participate;
 - How to elect not to participate; and
 - How to elect to contribute an amount different from the plan's default percentage rate for automatic enrollment contributions.

EACA Notice

- How to make an investment election, if permitted by the plan.
- How automatic enrollment contributions will be invested if the employee does not elect investment options, if plan permits employees to direct investments.
- If plan allows, how and when to withdraw contributions.

QDIA Notice

- ◆ Concern about target date funds has some plan sponsors questioning the use of target date funds as the QDIA.
- ◆ Necessary for Plan Sponsors to understand all aspects of the target date fund, not just whether to or through.
 - Treatment Reserved in ERISA Section 404(a)(5) regulations
- ◆ Managed accounts or balanced funds are alternatives.
- ◆ Selection of appropriate QDIA is a fiduciary responsibility under ERISA
 - Same prudence standards that apply to other investments on investment platform apply to QDIA -2

QDIA Notices

- ◆ Annual notice is in addition to initial notice provided to employees before initial investment in QDIA.
- ◆ Annual Notice must be given at least 30 days before beginning of plan year.
 - DOL regulations do not specify how far in advance of plan year end notice can be provided but, based on other notices, presumably 90 days prior to beginning of plan year.
- ◆ Notice required to be distributed to all QDIA participants.
 - As a practical matter, customary to deliver to all Plan participants.
- ◆ Failure to provide notice leaves fiduciaries without protection under ERISA Section 404(c)(5) for the period during which notice not provided.

◆

Discretionary Matching Contribution Notice

- ◆ May apply only to preapproved plans.
- ◆ Was introduced in Cycle 3 preapproved process, and plan sponsor may have adopted this plan in 2020, 2021, or 2022.
- ◆ Based upon IRS regulation requiring plans to provide a predetermined formula for allocation contributions to plan participants.
 - Sometimes referred to as the definitely determinable benefit rule.
- ◆ Two conditions must be satisfied:
 - Plan sponsor must communicate the match in writing to the plan administrator; and
 - Plan sponsor/plan administrator must communicate the matching contribution to participants eligible to receive the matching contribution.

Discretionary Matching Contribution Notice

- ◆ If restatement was adopted in 2021, notice required by December 31, 2022, for calendar year plan.
- ◆ If discretionary match is made annually, the annual match notice must be provided to plan participants within 60 days after the match has been deposited to the plan for the plan year.
- ◆ If discretionary matching contributions are made periodically, notice must be provided to plan participants within 60 days after the last match has been deposited to the plan for the plan year.
 - For a periodic matching contribution, a plan sponsor may provide a prospective notice to indicate the match the plan sponsor intends to make on a prospective basis.

Discretionary Matching Contribution Notice

- ◆ Notice to participants should include:
 - The effective date of the match;
 - The type of matching contribution (percentage or flat dollar amount);
 - The limits applicable to deferrals, for example, capped at deferrals on first 6% of compensation;
 - The period used to determine the match-payroll period, monthly quarterly, or annually;
 - Plan name and contact information; and
 - Date of Notice.
- ◆ Additional information can be provided in summary plan description.

Year-End Amendments

- ◆ IRS distinguishes between Discretionary and Qualification Required Amendments.
 - Discretionary amendments must be adopted by end of plan year;
 - May be substantive-change in benefit formula or eligibility; and
 - May be procedural-venue, internal statute of limitations, mandatory arbitration.
- ◆ Congress generally provides a date for adoption of statutorily required plan amendments, such as SECURE Act and CARES Act.

Year-End Amendments

- ◆ Under Secure Act, plan sponsors initially had until December 31, 2022, to implement SECURE Act provisions.
- ◆ Changing the required beginning date to April 1 after year in which participant reaches age 72 (instead of 70½) for participants born after June 30, 1949.
- ◆ Changing the distribution rules for benefits payable after the death of a participant to require distributions within 10 years after a participant's death unless the beneficiary is the participant's spouse, or a member of a specific list of other eligible designated beneficiaries.
- ◆ Allowing part-time employees to be eligible to make elective deferrals if they are credited with at least 500 hours of service for three consecutive years beginning January 1, 2021.
- ◆ Inclusion of an optional feature, qualified Adoption distributions.
- ◆ These provisions were required to be implemented operationally for the 2020 plan year.

Year-End Amendments

- ◆ IRS has discretion to extend deadlines for adopting Code required tax qualification provisions.
- ◆ In Notice 2022-33, IRS extended the deadline to amend plans for these provisions and the CARES Act provision with respect to required minimum distributions in 2020 until December 31, 2025.
- ◆ No explanation provided for the extended deadline.
 - If SECURE Act 2.0 is adopted, further modifications will be made to Code Section 401(a)(9).
 - The anticipated final regulations with respect to Code Section 401(a)(9) to reflect the SECURE Act revisions, will not be issued until 2023, and IRS did not want plans to be required twice for the same subject matter.
 - Final 401(a)(9) regulations might also contain model amendments to reflect Code Section 401(a)(9) regulations, as occurred with prior update of Code Section 401(a)(9) regulations.

Year-End Amendments

- ◆ Notice 2022-45 extended the deadline until December 31, 2025 for CARES Act provisions related to coronavirus related distributions, increased loan limits, and loan repayment deferrals.
 - If plan does not increase automatically dollar increases, for maximum elective deferrals, catch-up contributions, maximum permissible compensation, and Code Section 415 limits, plan should be amended.
 - For efficient administration, may consider adopting amendments earlier than required.
 - Plan sponsor does not want to recall in 2025 the manner in which plan was administered in 2020.

Long-Service Part-Time Employees

- ◆ SECURE Act changed requirements for eligibility to make pre-tax deferrals in plans in which eligibility determined on an hours-of-service basis.
- ◆ Plan could permissibly require 1,000 hours of service before a participant became eligible to participate in the plan.
 - SECURE Act eligibility requirement: At least 500 or more hours of service in 3 consecutive calendar years.
 - 2022 would be second year for keeping track of service for eligibility.
- ◆ Necessary to begin keeping track of part-time employees currently, to ensure they properly become eligible to participate in 2024.
- ◆ Accelerated eligibility rules only apply to elective deferrals.
 - 1,000 hours of service can continue to be required to become eligible to receive allocation of matching or nonelective contributions.

Plan Document Inventory

- ◆ Not a legally mandated plan year end activity, but appropriate in connection with determination of whether year end amendments are required.
- ◆ Confirm that all plan documents have been executed.
- ◆ Good practice to keep binder of amended and restated plans and plan binders.
- ◆ If amendment adopted at Board level, executed copy of amendment should be part of Board minutes.
 - If amendment adopted at the Committee level, executed copy of amendment should be part of Committee minutes.

ADP and ACP Corrections

- ◆ IRS Regulations specify time periods for correcting ADP failures (excess contributions) and ACP contributions (excess aggregate contributions).
 - Those corrective actions usually made within 2½ months after close of plan year, to avoid 10% excise tax.
 - Six months if plan is an EACA.
 - QNECS can be made after year end to avoid plan disqualification.
 - If corrective distributions or corrective contributions are not made by year end, plan is technically disqualified.

Forfeitures

- ◆ Rev. Rul. 80-155: DC Plans not qualified unless all funds are allocated to participant accounts.
- ◆ Some plans can have three separate accounts holding unallocated plan assets:
 - ERISA account;
 - Suspense account for annual additions under Code Section 415; and
 - Forfeiture account:
 - Separation from service with nonvested benefits;
 - Matching contributions attributable to excess deferrals, excess contributions, and excess aggregate contributions; and
 - Excess aggregate contributions.
 - Uncashed checks and missing participants.

Forfeitures

- ◆ Plan document may require amounts be used by end of plan year in which forfeiture occurred, or immediately succeeding plan year.
- ◆ In DC plans, forfeitures can be used to:
 - Pay nonsettlor expenses, and
 - Offsetting contributions.
 - Check whether plan document contains sourcing rule for forfeitures (i.e., matching contribution forfeitures offset matching contributions, profit sharing contributions offset profit sharing contributions).
 - Reallocated to plan participants.
 - Restoration of forfeitures to affected participants.

Required Minimum Distributions

- ◆ Most plans being administered as if required beginning date has been increased from age 70½ to age 72, although change was not mandatory.
 - Distribution should be made based upon updated life expectancy tables for 2022:
 - Uniform Life Table-most commonly used;
 - Table I-non-spouse beneficiary; and
 - Table II-Participant whose spouse is at least 10 years younger and sole beneficiary.
 - Failure to satisfy RMD subjects participant or beneficiary to a potential 50% penalty.
- ◆ Distribution based upon December 31, 2021, account balance.

Remedial Amendment Period

- ◆ Remedial amendment period is the period during which a disqualifying provision in an individually designed tax qualified plan or a form defect in an individually designed 403(b) can be corrected to retain favorable federal income tax status.
 - The remedial amendment period for a disqualifying defect or form defect with respect to the provision of a new plan or the absence of a provision from a new plan expires on the last day of the second calendar year following the calendar year in which the plan is put into effect.
 - The remedial amendment period for a disqualifying provision or form defect with respect to an amendment to an individually designed plan, other than an amendment that arises as a result of changes in tax qualification requirements or Code Section 403(b) requirements expires on the last day of the second calendar year following the year in which the amendment is adopted or effective, whichever is later.

Remedial Amendment Period

- ◆ The remedial amendment period for a disqualifying provision or form defect that arises as a result of a change in Qualification Requirements or Code Section 403(b) requirements, as applicable, expires on the last day of the second calendar year that begins after the issuance of the Required Amendments List in which such change appears.
 - If the beginning date for any of these three circumstances began in 2020, the remedial amendment period will expire on December 31, 2022.

Favorable Determination Letter

- ◆ Plan sponsor of individually designed plan may submit a favorable determination letter for a merged plan if two conditions are satisfied:
- ◆ The date of the plan merger occurs no later than the last day of the first plan year that begins after the date of a corporate merger, acquisition, or other similar transaction between parties that are not part of the same controlled group under Code Section 414(b) or (c); or part of an affiliated service group under Code Section (m).
 - If the plan is a calendar year plan, and the date of the business transaction occurred in 2021, the plan merger must occur by December 31, 2022, in order to be eligible to submit an application for a favorable determination letter for a merged plan.

Favorable Determination Letter

- ◆ A determination letter application for the merged plan is submitted within the merged plan submission period.
 - The merged plan submission period is the period beginning on the date of the plan merger and ending on the last day of the first plan year of the merged plan that begins after the date of the plan merger.
 - If the plan is a calendar year plan, the date of the corporate merger, acquisition or other similar business transaction occurred in 2020 and the date of the plan merger occurred in 2021, then the determination letter for the merged plan must be submitted to IRS by December 31, 2022.

SAR Distribution

- ◆ Applies only to DC plans.
 - Tax qualified DB plans receive annual funding notice.
- ◆ Distributed 2 months after Form 5500 filed.
- ◆ Form 5500 on extension could be filed October 15.
 - SAR would need to be distributed by December 15.

SPDs and SMMs

- ◆ Not a required year end action, but appropriate action to take when looking at year end amendment requirements.
- ◆ Updated SPDS are required if there have been updates within the last 5 years.
- ◆ If no changes to the SPD, must be updated every 10 years.
 - Summary of material modifications required 210 days after close of plan year.
- ◆ May be necessary to include certain procedural provisions in SPD to ensure their enforceability.
 - Venue or internal limitations period.
 - Possibly mandatory arbitration provisions.

Designation of Beneficiary Forms

- ◆ Not a legally required activity.
- ◆ Plan administrator's obligation is to follow the terms of the plan.
- ◆ Participant's circumstances may have changed since initial designation of beneficiary.
 - Participant may have gotten divorced, did not change ex-spouse as beneficiary.
 - Some plans automatically revoke designated beneficiary upon divorce, but not all plans.
- ◆ Waiver by spouse in divorce order will not override terms of the plan.

Ending of Emergencies

- ◆ In response to pandemic, two national emergencies were declared:
 - National Emergency, declared by President; and
 - Public Health Emergency, declared by HHS.
- ◆ National Emergency reviewed annually, scheduled to expire February 2023.
- ◆ Public Health Emergency, will likely not expire before April 11, 2023.
 - Primary effect of the Emergencies on Welfare Plans.

Ending of Emergencies

- ◆ Affected retirement plans in two ways.
- ◆ Traditionally, spousal consent was witnessed by notary.
- ◆ IRS permitted remote notarization.
 - Not a required change, but plan sponsors, especially DB plan sponsors, adopted this change.
 - Even when emergencies end, Congress may make this change claim permanent feature of Code.

Ending of Emergencies

- ◆ Deadline for filing claims and appeals to be told, and reasonably delayed.
 - No specified period of extension.
 - Claimant still required to exhaust administrative remedies.
- ◆ 401(k) plan may require participant to file claim within a specified period of time after participant knew or should have known, of operational error.
 - Appeals generally need to be filed within 60 days of notice of claim denial.
- ◆ Consider notifying all participants that extensions for filing claims and appeals is ending, and deadlines to file claims and appeals will be forthcoming.
- ◆ Caution: Not all claims and appeals will be immediately due, just that deadline clock will be restarted.

Linked Plans

- ◆ Some nonqualified deferred compensation plans are linked to tax qualified plans.
 - Provide participants with the difference between what their account balance would have been had there been no Code limits, and actual account balance under the plan.
- ◆ Must comply with Code Section 409A.
 - Failure to comply subjects participant to 20% excise tax plus interest adjustment.
- ◆ General rule: Election should be made before beginning of plan year for employees for employees identified as participants before beginning of calendar year.
 - Exception for performance bonus arrangements.

Investment Policy Statement

- ◆ Not legally required under ERISA, but regarded as best practice by DOL.
- ◆ If plan has an IPS, many courts regard it as an instrument under which plan is governed.
 - Terms of IPS should be flexible.
 - Failure to follow precisely terms of IPS can be regarded as breach of fiduciary duty.
 - Not designed to be amended annually but should be reviewed annually.
 - DB plan may be considering switch to LDI.
 - DC plan may be considering increased emphasis on ESG or alternative investments addition/removal of brokerage windows.

Bonds

- ◆ Required under Section 412 of ERISA.
- ◆ Errors with respect to bonding reported on Form 5500 can be a trigger for DOL Audit.
 - Amount of bond must be at least \$10,000, generally not to exceed \$500,000.
 - Amount determined at beginning of plan year.
- ◆ Bond provides limited protection to plan by covering only fraud or dishonesty by persons handling plan assets.
 - But plan administrator needs to confirm that correct amount of bond is in place.

Automatic Cash Out

- ◆ Not statutorily required, but a frequent plan feature.
 - Plan may not state that distributions must be made by year end but rather as soon as soon as practicable.
 - \$1,000 or less account balance, cash distribution.
 - \$1,001-\$5,000 Participant has right to receive cash or elect rollover.
 - Proposed legislation would increase cash-out limit to \$7,500.
 - If no response within a specified period, account balance automatically rolled over to a designated IRA.
- ◆ Zero-dollar cashout for nonvested benefits.

Uncashed Checks

- ◆ Plan or Trust Agreement should specify treatment of uncashed checks.
 - Plan Administrator should periodically receive a report.
- ◆ If plan does not permit deferral of distributions, distributions may be required to commence at normal retirement date, generally age 65.
 - No specific statutory or regulatory requirements as to appropriate follow-up actions.
 - Emerging problem: Participants unresponsive because of the infirmities of old age.
- ◆ If participant cannot be contacted, follow appropriate plan procedure, such as forfeiture with restoration if participant fails to respond.

Missing Participants

- ◆ Terminated Vested Participant Project of DOL 2017.
 - Part of Protecting Benefits Distribution Project of DOL.
 - Commonly referred to as missing participant investigation.
- ◆ Leading enforcement activity for EBSA of DOL.
- ◆ Initial focus upon defined benefit plans, has expanded to defined contribution plans.
- ◆ EBSA secured billions of dollars in recovery for plan participants.

Missing Participants

- ◆ This is particularly difficult issue for defined benefit than 30 years.
- ◆ Both IRS and DOL have specified measures to be taken to locate missing participants.
 - Proposed Congressional action would establish national databank.
- ◆ No clear guidance as to required actions to be taken with respect to ongoing plans, particularly ongoing defined benefit plans.
 - In absence of clear guidelines, missing participant issue is a concern for plan sponsors.
 - Operational failures that in theory could disqualify a plan.
 - Breach of fiduciary duty or prohibited transaction under ERISA.

Missing Participants

- ◆ Failure to satisfy required minimum distributions under Code Section 401(a)(9).
- ◆ Failure to distribute benefits in accordance with terms of the plan an operational failure.
- ◆ Failure to locate a plan participant may be a prohibited transaction under ERISA, even if relevant plan fiduciary complies with all the plan's procedures for locating missing plan participants.
- ◆ Use of plan forfeiture account to reduce future employer contributions can be characterized as a breach of fiduciary duty, even if forfeited amounts are restored if participant is located.
- ◆ Plan participants who cannot be located arguably need to be searched for indefinitely.
- ◆ DOL Regional Office position: Conduct annual search, with a different search method to be used each year.

Missing Participants

- ◆ DOL focus on terminated vested participants and beneficiaries who:
 - Have not informed former employers of new address participants should be required to take this action, but their failure to do so does not reduce plan sponsor's obligations;
 - May not be aware that they are due a benefit;
 - Are deceased and beneficiary is not aware of a benefit; or
 - May have potential excise tax issues.

Missing Participants

- ◆ Compliance Assistance Release 2021-01
- ◆ Information requested:
 - Plan documents;
 - Census Reports;
 - Actuarial Reports; and
 - Action steps taken by plan sponsor to address missing participants.

Missing Participants

- ◆ Errors investigated:
 - Systemic errors in recordkeeping, and
 - Inadequate procedures for:
 - Identifying and locating missing participants;
 - Contacting terminated vested participants approaching normal retirement age;
 - Contacting terminated vested participants approaching retirement minimum distribution commencement date; and
 - Addressing uncashed checks.

Missing Participants

- ◆ “Red Flags” to identify potential problems:
 - Missing or nonresponsive participants;
 - Terminated vested participants at normal retirement date who have not begun to receive benefits;
 - Missing, inaccurate or incomplete contact information/census data;
 - Lack of sound policies for handling undeliverable mail; and
 - Lack of sound policies for handling uncashed checks.

Missing Participants

- ◆ Best Practices regarding missing participant issue:
 - Maintaining accurate census information.
 - Implementing effective communication strategies.
 - Running frequent missing participant searches.
 - Documenting procedures and actions.

New Withholding Forms

- ◆ Effective January 1, 2023, plan sponsors required to use redesigned Forms W-4P and new Form W-4R.
 - Previously, Form W-4P used to calculate withholding on pension or annuity payments, whether paid periodically or nonperiodically.
 - Use of both forms was optional for plan sponsors in 2022.
 - New forms must be used no later than January 1, 2023, or 30 days after the 2023 forms are released by IRS, whichever is later.
- ◆ New Form W-4 differs from prior withholding on nonperiodic distributions.
 - Withholding percentages, rather than default rates plus additional dollar amount.

New Withholding Forms

- ◆ Plan sponsors not required to obtain new withholding forms for all existing annuity payees.
- ◆ Whether based on existing forms or new forms, amount of withholding must be based upon new tables.
 - Publication 15-T, Federal Income Tax Withholding Method, provides several approaches.
- ◆ All methods may require updating programming in plan sponsor's payroll system.
- ◆ If accepting Forms electronically, ensure that electronic versions are compliant with IRS guidelines.
 - Publication 15-A, Employer's Supplemental Tax Guide.

Monitoring

- ◆ Selection of a service provider is a fiduciary function under ERISA.
- ◆ In addition to duty to select a service provider prudently, there is a duty to monitor.
- ◆ Monitoring responsibilities under ERISA not restricted to monitoring of service providers.
 - Board of Directors appointing committees has responsibility to monitor work of committees.
 - Some plans require committees to report to monitoring Board on their performance and activities during plan year.

Monitoring

- Duty to monitor is separate and apart from duty to exercise prudence in selecting investments.
- ◆ Specifics of the monitoring obligation is fact specific.
- ◆ Time for review depends upon standard of reasonableness.
 - One court found quarterly review of investments sufficient.

Monitoring

- ◆ Fiduciary with responsibility for reviewing recommendations of investment advisor or investment manager must understand the investment strategy.
- ◆ An investment strategy may be appropriate for a plan, but if reviewing plan fiduciaries do not understand the strategy, they are in a vulnerable position if particular strategy underperforms.
- ◆ DOL raised these issues in its 2022 guidance on private equity and cryptocurrency.

Monitoring

- ◆ With respect to investments, appointing fiduciary not charged with direct overseeing of investments.
 - Such conduct would be duplicative.
- ◆ In amicus brief, DOL set forth a 5-part standard for an acceptable monitoring procedure.
 - The appointing authority must adopt routine monitoring procedures.
 - The appointing authority must adhere to routine monitoring procedures.

Monitoring

- The appointing authority must review the results of its monitoring procedure.
- The monitoring procedure must alert the appointing authority to possible deficiencies.
- The appointing authority must take appropriate corrective action to correct any deficiencies.

Cybersecurity

- ◆ A mistake to believe plan is too small to be breached.
 - Governing assumption is that plan will be hacked at some point.
- ◆ DOL issued its initial guidance in this area on April 14, 2021.
- ◆ Guidance issued in the form of three documents for best practices:
 - Plan sponsors and plan fiduciaries;
 - Plan participants; and
 - Plan service providers.
- ◆ Guidance very similar to HIPAA's privacy and security guidance.

Cybersecurity

- ◆ Guidance not in the form of advisory opinion, information letter, field assistance bulletin, or proposed regulation.
 - No discussion of whether a participant's personal data held by a plan is a plan asset.
 - Courts that have addressed the issue have uniformly concluded it is not a plan asset.
 - Important issue from a prohibited transaction perspective
 - No discussion of the relative responsibility of plan sponsor/ plan fiduciary and plan service provider in the event of breach.

Cybersecurity

- ◆ No discussion of whether state data breach laws are preempted.
 - If not preempted, a service provider could be liable at both federal and state level.
 - Damages may be imposed under state law that could not be imposed under ERISA.
- ◆ No discussion as to whether these prescribed activities are fiduciary in nature.

Cybersecurity

- ◆ Guidance is prescriptive, not principles based.
 - If this guidance were to be challenged in court, would likely receive the lowest level of deference.
 - Security measures not part of DOL's expertise.
- ◆ Despite absence of formal guidance, and short time period after issuance of guidance, DOL is asking cybersecurity questions on plan audit.

Cybersecurity

- ◆ Plan sponsors would like to adopt as many of the DOL's best practices as possible but may lack the leverage to do so.
- ◆ Service providers cannot guarantee that a plan will not be hacked.
 - Service provider may have state of the art security system, but breach will occur because of human error.
- ◆ Permissible under ERISA for service provider to set low dollar cap on liability for any action on its part.
- ◆ Plan sponsors should consider adopting cybersecurity policy.

Internal Controls

- ◆ In retirement plan context, internal controls are policies and procedures designed promptly to detect errors and reduce the likelihood of errors in plan administration.
 - Plan sponsors and plan administrators must routinely follow established policies and procedures to self-correct many plan errors under EPCRS.
- ◆ Not required to be done annually, but if plan does not have policies and procedures in place, or if it has not updated them for some time, would be an appropriate year end activity.
- ◆ Four areas of internal controls:
 - Employee eligibility;
 - Contributions;
 - Plan distributions; and
 - Plan testing and administration.

Employee Eligibility

- ◆ Who determines when an employee is eligible to participate in the plan?
 - Plan might provide immediate participation for salary deferral contributions, and one year for matching contributions.
- ◆ What steps does the person take to determine if an employee is eligible to participate?
- ◆ How does this person track the amount of service an employee has completed?
 - Must understand difference between hours of service and elapsed time.
- ◆ How is an employee's date of birth verified?

Employee Eligibility

- ◆ Who is responsible for maintaining personnel records?
- ◆ How is information from personnel records shared with the plan administrator?
- ◆ In a 401(k) plan, what steps are taken to notify employees they are eligible to participate in the plan?

Contributions

- ◆ What steps does an employee take to elect to defer money or make a change to a previous election?
- ◆ If payroll is done by an outside service provider
 - How is information shared with the outside service?
 - How does the plan administrator share payroll data with the outside service provider?
 - Who reviews the outside service provider's work to ensure that it is accurate?

Contributions

- ◆ If payroll is done in house,
 - Who is responsible for preparing payroll?
 - Who reviews payroll to ensure that it is accurate?
 - How is payroll data shared with plan administrator?

- ◆ What is plan's definition of compensation?
 - Payroll system may have many more classifications of compensation than plan document.
 - Each payroll system compensation entry should be characterized as pensionable earnings or not.

Contributions

- ◆ Code Section 415 compensation includes, FICA compensation (IRC 3401) excludes amount includible in income from receiving group life insurance in excess of \$50,000.
- ◆ Code Section 415 compensation excludes, W-2 compensation includes:
 - Amounts realized from the exercise of a nonqualified stock option, and
 - Amount includible in income when restricted stock or other property becomes fully transferable or no longer subject to a substantial risk of forfeiture.
- ◆ Amounts includible in income upon making an election under Code Section 83(b).
 - Distributions from a nonqualified deferred compensation plan.

Contributions

- Who determines a participant's compensation based on the payroll information?
- ◆ Who verifies that participant's compensation that is used for plan purposes, matches the plan's definition of compensation?
 - Applying incorrect definition of plan compensation can result in an under allocation or an overallocation to a participant's account.
 - These defects are correctable, but the object of internal controls is to reduce the likelihood of such errors recurring.
 - Correction of overallocation becomes more complex if participant receiving over allocation separates from service and receives a distribution that is rolled over into an IRA.

Contributions

- ◆ How are employee deferrals remitted to the trust holding participant accounts?
 - Are employee deferrals, whether pre-tax, after-tax, or Roth, remitted to the trustee in accordance with DOL timeframes under the DOL plan asset regulations?
- ◆ Who verifies that the correct amount was remitted to the trust and allocated to the correct participant accounts?
- ◆ How are matching and nonelective contributions determined?
- ◆ Who ensures that each participant received the correct allocation of matching and nonelective contributions?

Plan Distributions

- ◆ How does a participant request a distribution from the plan?
- ◆ Who reviews and approves distribution requests?
- ◆ Who determines a participant's vested percentage when a distribution is made?
 - If participant previously had a separation from service, who determines that the break in service rules have been correctly applied?
- ◆ How do plan assets get from the plan trust to the participant?
- ◆ Who is responsible for completing and filing Form 1099-R and comparable state forms?
 - Who reviews the applicable state income tax withholding rules upon distribution?

Plan Testing and Administration

- ◆ Who is responsible for making sure the plan document is updated timely?
- ◆ Who completes the annual testing for the plan?
- ◆ Who determines which participants are highly compensated?
- ◆ Who determines which employees are key employees?
- ◆ Who reviews the annual testing to ensure that the correct data was used?

Plan Testing

- ◆ Who determines if there are any related employers that could cause a controlled group or an affiliated service group to exist?
- ◆ Who reconciles the trust statements to ensure their accuracy?
- ◆ Who completes the Form 5500 for the plan?
- ◆ How are notices distributed to participants?
- ◆ What is the process for correcting errors that are discovered in plan document or plan operation?

Loans

- ◆ Who verifies the plan's loan procedures?
- ◆ How does a participant request a loan from the plan?
- ◆ How are loan applications reviewed and approved?
- ◆ Who determines a participant's maximum loan amount?
- ◆ How is a loan delivered from the trust to a participant?
- ◆ Who notifies payroll of the date that loan repayments are to commence?

Record Retention

- ◆ General rule: 6 years after filing of Form 5500.
- ◆ However, records must be retained for as long as necessary to determine a participant's benefit.
- ◆ Primarily an issue for DB plans, particularly DB plans with a career average benefit formula, that has a limited definition of compensation.
- ◆ Penalty under ERISA Section 209 for failure to maintain records is \$10 per employee, but
- ◆ Failure to maintain adequate records likely to result in litigation with former participant.

Record Retention

- ◆ ERISA Section 209 does not specify how long records must be retained after a participant receives a distribution.
- ◆ Plan participant who separated from service of plan sponsor decades ago may claim that he or she never received a distribution.
- ◆ A properly completed Form SSA (now 8955-SSA) to Form 5500 should indicate when a terminated vested participant with a deferred vested benefit received a distribution.
- ◆ If proper Form 5500 filing was not made, unclear who has burden of proof.
 - Participant has burden of proof under ERISA to entitlement to benefits, but that burden may not extend to receipt of benefits.
- ◆ Electronic recordkeeping will allow plan administrators to retain records of distribution indefinitely but may be an issue with respect to earlier years.

Independent Qualified Public Accountant

- ◆ Plan sponsors of large employee retirement plans are required to include audited financial statements in connection with Form 5500 filing.
- ◆ ERISA Section 103(A) provides a plan must retain an independent qualified plan accountant to audit and render an opinion on the financial statements.
- ◆ ERISA Section 103(a)(3)(D) defines qualified public accountant but does not define independence.
- ◆ DOL Interpretive Bulletin 75-9, 29 C.F.R. 2509.75-9, provides guidance for determining when an accountant is independent.
 - DOL guidance in I.B.75-9 based on principles that parallel the SEC's independence requirements for auditing publicly traded companies.

Independent Qualified Public Accountant

- ◆ On September 6, 2022, DOL replaced IB 75-9 with Interpretive Bulletin 2022-01.
- ◆ DOL's concerns were that manner in which IB 75-9 was drafted might preclude plans from engaging high quality auditors and to reflect differences in the way that large accounting firms operate in 2022, compared to 1975-IB 2022-01 focused upon three issues:
 - Time period during which accountants and firms are prohibited from having financial interests in the plan or plan sponsor;
 - Other services an accountant or firm may provide to a plan or plan sponsor; and
 - Definition of office for purposes of determining who is a member of a firm for an independence analysis.

Independent Qualified Public Accountant

- ◆ No de minimis rule for purposes of determining independence.
 - Holding of even a single share of plan sponsor by an accountant, the firm, or a member of the firm during the period to be audited can be a “direct interest,” or “a material indirect interest,” which can disqualify the qualified public accountant.
- ◆ Under IB 2022-01, accountant or firm will not be disqualified from accepting a new audit engagement if interest is disposed of prior to period of professional engagement.
 - Divestiture window commences when there is an oral agreement or understanding that a new client has selected them to do the plan audit.
 - Divestiture window ends when an initial engagement letter or other written agreement is signed or audit procedures commence, whichever is sooner.

Independent Qualified Public Accountant

- ◆ This new audit engagement exception
 - Limited to publicly traded securities;
 - Appears to include options to purchase; and
 - Expands the group who must divest to include the accountant, his or her firm, shareholder employees, partners, professional employees and the immediate families (spouses and dependents) of each of them.

Independent Qualified Public Accountant

- ◆ Continues guidance from IB75-9 prohibiting an accountant or firm from engaging in certain plan or plan sponsor related employment.
 - Engaging in management functions that relate to financial records that would be the subject of the audit.
- ◆ IB 2022-01 permits accountant firm, or its members to engage in professional services that are not connected to an audit or review of a plan's financial statements.
 - Example: Rendering of actuarial services by an actuary associated with the accountant or firm.
 - Retention or engagement by the plan or plan sponsor of the accountant, the firm, or its members for nonplan work.

Independent Qualified Public Accountant

- ◆ DOL caveats to permissible other services rule:
 - Certain positions or connections, originally enumerated in IB 75-9, are still prohibited;
 - Independence test is facts and circumstances; and
 - DOL will give appropriate consideration to all facts and circumstances in determining whether an accountant or accounting firm is independent.
 - In other contexts, such as procedures for obtaining prohibited transaction exemption, independence is defined more precisely.
 - Caution about engaging in prohibited transactions in connection with multiple services agreements.

Independent Qualified Public Accountant

- ◆ Definition of office, for purposes of defining a member , has been changed from physical location to workplace group.
- ◆ Office defined as “a reasonably distinct subgroup within a firm, whether constituted by formal organization or informal practice, in which personnel who make up the subgroup generally serve the same group of clients or work on the same categories of matters regardless of the physical location of the individual.”
- ◆ Takeaway IB 2022-01 may present an opportunity for plan fiduciaries to discuss new services available to a plan.

ERISA Section 103(a)(3)(C) Audit

- ◆ Previously referred to as limited scope audit.
- ◆ Plan administrator required to instruct the auditor to perform an audit under ERISA Section 103(a)(3)(C), after first obtaining a certification from a qualified certifying custodian.
- ◆ Plan administrator must review certification carefully before submitting it to the plan's auditor.
- ◆ Common deficiencies include:
 - Omissions, errors, and qualifying language in the certification,
 - Ex-certification does not include all investments (for example, it covers separate account assets but not general account assets).
 - Qualified certifying institution certifies to either the completeness or accuracy of the investment information, but not both.

ERISA Section 103(a)(3)(C) Audit

- Certified assets include assets held by a separate custodian.
- Plan investments are improperly characterized.
- Certification includes statements purchased after year end.
- ◆ An issue that might arise in this regard is if plan holds hard to value assets.

Transition Period for Code Section 410(b) Nondiscrimination Testing

- ◆ One of the nondiscrimination tests that a tax qualified plan must satisfy is minimum coverage under Code Section 410(b).
- ◆ Can be satisfied either by a 70% ratio percentage test or a 70% average benefits test.
- ◆ Special rule applies for certain acquisitions or dispositions.
 - Acquisitions or dispositions refer to asset or stock acquisition, merger, or other similar transaction involving a change in the employer of the employees in a trade or business.
- ◆ Plan is treated as satisfying Code Section 410(b) during a transition period if the plan satisfied Code Section 410(b) immediately before the acquisition or disposition, and there is no significant change in the plan or the coverage under the plan other than the acquisition or disposition.

Transition Period for Code Section 410(b) Nondiscrimination Testing

- ◆ Transition period begins on date of change in the members of a controlled group or affiliated service group and ends on the last day of the first plan year beginning after the date of such change.
- ◆ If the transition period began in the 2021 calendar plan year, the transition period will end on December 31, 2022, and the generally applicable rules of Code Section 410(b) must be satisfied.

QUESTIONS?

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