

employee benefits update

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Defining the role of a plan fiduciary

If you're a retirement plan sponsor, no doubt you've heard or read the term "fiduciary" quite a bit. But does it include you? If it does, should you worry about innocent plan mistakes or only significant reporting matters? This article will help define who is a plan fiduciary and discuss the implications for plan sponsors.

Who is a fiduciary?

Generally, fiduciaries are individuals or entities who manage an employee benefit plan and its assets. In the broadest sense of the term, the plan fiduciary is generally the plan sponsor. ERISA defines a fiduciary as a person who:

1. Exercises management or control over the plan and the plan's assets,
2. Provides investment advice for a fee, and
3. Has discretionary authority over the plan's administration.

Even if you assign these duties to other parties, such as a retirement plan panel or a trustee, you aren't relieved from your fiduciary duty to the plan.

The key to determining whether an individual or an entity is a fiduciary is whether the person or entity exercises discretion or control over the plan. Although paid brokers or investment advisors provide advice for a fee, they generally aren't considered plan fiduciaries unless they exercise significant control over the plan. Also, attorneys, accountants and third-party administrators generally aren't plan fiduciaries.

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What must a fiduciary do?

Fiduciaries must act solely in the interest of plan participants and their beneficiaries and with the exclusive purpose of providing benefits to them. They must carry out all tasks associated with the plan prudently. This includes providing various investment choices, informing participants about plan options and provisions, allowing for educational opportunities, and ensuring that the plan complies with plan document provisions.

Plan fiduciaries must perform certain tasks at least annually. For example, you must review all transactions within the plan trust and reconcile trust performance. You'll also need to review employer census and payroll data, the distribution and loan processing procedures, and the timeliness of deposits. In addition, you must analyze plan contributions and distributions and review required tax reporting such as Form 1099R, Form 945 and Form 5500.

Moreover, as a fiduciary, you must know what fees you pay from plan assets and provide this information to participants. And ERISA requires plan sponsors to have a surety bond for at least 10% of the value of the plan's assets to cover individuals who perform administrative tasks.



Supreme Court addresses individual rights against plan fiduciaries

A U.S. Supreme Court ruling in February made it clear that plan participants have individual rights against plan fiduciaries for a fiduciary's failure to comply with participant requests that later result in plan losses. In *LaRue v. DeWolff, Boberg & Associates*, the plan participant (LaRue) alleged that he'd lost over \$150,000 in plan assets because the plan sponsor had failed to invest his account according to his instructions.

ERISA requires plan fiduciaries to correct plan mistakes and make whole any plan losses arising from breach of fiduciary duties, and ERISA allows lawsuits to enforce this provision. Generally, previous lawsuits involved plan losses as a whole. *LaRue* specifically addresses whether an individual plan participant can sue the plan administrator for losses to his or her individual defined contribution account.

The Supreme Court ruled that "whether the account includes 1% or 99% of the total assets in the plan," the legal issue didn't change. Justice Stevens found that the plan administrator's misconduct fell squarely within ERISA guidelines, and the law authorizes "recovery for fiduciary breaches that impair the value of plan assets in a participant's individual account."

Ultimately, the Court held that LaRue's suit against his employer was proper. This is a significant ruling setting aside recent precedents under ERISA.



What is a breach of duty?

Giving participants the option of directing their investment choices doesn't completely relieve fiduciaries of their fiduciary duties. There are, in fact, a variety of activities that can cause a breach of fiduciary duty and expose the plan to potential errors and losses.

Certain interested parties must not engage in specific prohibited transactions within retirement plans. These individuals generally are plan fiduciaries, owners providing services to the plan, the employer sponsor and any relatives of the sponsor. Prohibited transactions include:

- › Selling or exchanging property,
- › Lending money,
- › Providing goods or services,
- › Transferring assets for personal use, and
- › Holding employer securities or property with a value that is greater than allowed under ERISA.

How can you prevent mistakes from happening? Retirement plan specialists can monitor the plan's performance and advise you on ways to meet your obligations. In addition, ask your investment broker

and third-party administrator for a checklist of compliance-related tasks.

How do you correct a breach of duty?

In the event of an error or breach of fiduciary duty, you must restore the plan to the condition it would have been in had the breach not occurred. Both the Department of Labor and the IRS have correction programs available that provide step-by-step guidance for sponsors to follow in the case of errors.

By remedying plan defects, errors and omissions in a timely manner, you can reduce the likelihood of exposure to a lawsuit. Quickly addressing participant complaints and correcting problems can also prevent future administrative headaches.

Fulfilling your duties

With sound education, careful planning, professional advice and deft execution of proper plan administration, you can fulfill your fiduciary duties as plan sponsor and prevent a breach of duty. Mistakes and problems can occur but, with proper guidance, you should be able to keep the plan operating accurately and efficiently. ☺

Are your plan documents ready for EGTRRA restatement?

It's common for qualified retirement plans to use preapproved IRS plan documents. Such documents contain specific language and various options that plan sponsors may select for their retirement plans. The IRS, however, has "restated" many of the prototype documents this year to comply with the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), and plan sponsors will need to restate their plan documents to match those of the IRS.

The IRS began issuing opinion and advisory letters in April for master and prototype and volume submitter defined-contribution plans that were timely filed with the agency to comply with EGTRRA. Employers using these types of plans will need to completely restate their documents by April 30, 2010. Let's take a look at what this means for you as a plan sponsor.

Plan types

Plan documents generally fall into one of three categories:

1. Master and prototype plans,
2. Volume submitter plans, and
3. Individually designed plans.

Master and prototype and volume submitter plans are preapproved by

the IRS. Individually designed plans are basically just that — a retirement plan drafted for a particular sponsor and then approved by the IRS.

Plan preapproval

Law firms, third-party administrators, banks and other retirement plan administrators generally adopt pre-approved plans. Such entities can ensure the documents are drafted for each plan to comply with related rules and regulations. Also, preapproved plan documents can quickly handle changes, such as amendments, that the IRS may require.

You don't need to file for an individual determination letter if you have a master and prototype or volume submitter plan, because those plan documents are already approved. But if you modify your plan document from the preapproved format, you must submit an application to the IRS for an individual approval letter. (Plan sponsors shouldn't attempt to update documents on their own.)

A plan document is preapproved if it falls within a specific category:

The plan sponsor is a prior adopter of a prototype plan. This applies if the plan sponsor had adopted a preapproved plan as of Feb. 15, 2005, or a new plan based on a preapproved plan that complies with EGTRRA.

The plan sponsor is a new adopter. This means the plan sponsor either maintained an individually designed plan or hasn't maintained a plan during the current amendment cycle and is adopting a plan for the first time.



The sponsor is an intended adopter. Plan sponsors who currently maintain an individually designed plan but intend to adopt a preapproved plan must complete Form 8905 to certify that the sponsor will make the change.

The sponsor intends to adopt a preapproved replacement plan. This occurs when a plan sponsor who intended to replace a current preapproved plan failed to submit the new plan for an opinion or advisory letter — generally because the sponsor went out of business or due to other similar circumstances.

EGTRRA updates

The new EGTRRA restated documents allow cross testing in master and prototype documents. Cross testing involves the use of an advanced profit-sharing formula that previously had been allowed only in individually designed and certain volume submitter documents. But cross testing in master and prototype documents includes more restrictions than in individually designed or volume submitter documents.

If the IRS preapproves both master and prototype documents and volume submitter documents, what's the difference to plan sponsors? In the past, the master and prototype document was administratively easier to use, and it contained some features that weren't available in the volume submitter document.

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The new volume submitter document allows for full cross testing instead of the limited cross testing used in master and prototype plans. And it's relatively easy to amend.

Once you restate your document to reflect EGTRRA updates, you must provide your employees with a new summary plan description. Plan document design issues are complex and sponsors shouldn't undertake them without professional advice.



Plan cycles

So now you know whether you need to submit an application for IRS approval of your plan and its EGTRRA restatements. But when do you apply?

Before 2005, the IRS dealt with a deluge of document restatements. To curtail the influx, the IRS created staggered filing cycles throughout a retirement plan's existence to process approvals of restatements.

For example, master and prototype and volume submitter plans follow a six-year cycle, while individually designed plans follow a five-year cycle with the year corresponding to the last digit of the plan sponsor's EIN. This can cause some confusion, so ask your third-party administrator or legal counsel if you're not sure about when to submit your EGTRRA restatement documents.

Plan ahead

This is a vital time for employers to consider their overall plan designs. You should address changes to entry requirements, distribution or loan provisions, and vesting and other design options. Contact your benefit plan expert to ensure your documents reflect the latest updates brought about by EGTRRA and other legislation. ⌚

Education never ends

KEEP YOUR PLAN PARTICIPANTS UP TO DATE

Plan sponsors have a fiduciary responsibility to educate their participants in retirement planning. Many plan sponsors believe they have education covered with normal vendor/broker enrollment meetings and stuffers sent in the participant statements. Although these offerings are a good start, several studies by a Stanford University economics professor have shown that these passive forms of education are ineffective and often ignored by participants.

Education = success

Professor Douglas Bernheim has conducted several studies on the relationship between financial education and savings outcomes. The general conclusion is that the more educated participants are in planning their retirement, the better the chance they'll be successful.

When given the tools and understanding of how quickly employee deferrals, employer matching and profit-sharing contributions can grow, participants generally become excited about saving for retirement and plan participation increases. According to Robert Clark

and Sylvester Schieber in their study titled "Factors Affecting Participation Rates and Contribution Levels in 401(k) Plans," the amounts participants defer have been shown to increase when they're provided with specifically tailored plan information.

In 2005, Steven Nyce reported in "The Importance of Financial Communication for Participation Rates and Contribution Levels in 401(k) Plans" that employers using the Internet and Web-based programs to provide plan education had a larger impact on participation and contribution rates. He also found that improved communication can increase participation as much as offering a higher employer match.

The type of education you should provide will differ based on your plan type. Defined benefit plan participants need to determine whether the amount they'll receive in pension will be enough to sustain them in their retirement years. You can provide checklists or resources to help them determine retirement costs. They may need to contribute to supplemental savings plans as well.

For participants in defined contribution plans, such as 401(k) plans, most of their retirement income will be derived from the success and planning of their employer-sponsored retirement plans. Thus, you'll need to educate these employees about ways to optimally manage their accounts.

5 key topics to cover

Among the best ways to educate participants is by holding financial planning seminars with one-on-one help offered afterward. To convey your genuine interest in helping participants save for retirement, and to increase attendance, try to offer these seminars during work hours. Be sure to address the following five key topics:

- 1. Plan participation.** Educate your participants on the tax benefits of deferring part of their salary and taking advantage of employer match contributions.
- 2. The importance of deferral percentages.** Show participants how quickly their money can grow with



higher deferral percentages. The difference between deferring 3% of salary and 5% of salary can add up over the years.

3. Return on investment. Be sure participants understand the need to rebalance their funds periodically. Participants in their 30s generally have a different balance of funds than participants in their 60s. Also educate participants about the importance of diversifying their investment choices.

4. Plan loans. While many participants are correct that the money in their retirement account is theirs to borrow at any time, explain the risks of plan loans. These include potential tax penalties and diminished growth of their tax-deferred savings.

5. Early distributions. Explain the tax and penalty ramifications of taking premature distributions, which generally occur when participants change jobs or decide to take a hardship distribution. Specifically, participants will have to start over from scratch and may not be able to defer for a period of time. In the worst case scenario, participants may end up working beyond their planned retirement dates.

It's up to you

Nowadays, individuals have more power than ever to maximize their retirement savings. Your plan's success — as well as your employees' retirements — depends on the education you provide. 🕒

How to identify and correct SIMPLE or SEP plan errors

The IRS is well aware that some plan sponsors and administrators struggle to keep their Savings Incentive Match Plans for Employees (SIMPLEs) and Simplified Employee Pension (SEP) plans in compliance. So plan sponsors and administrators of these types of plans should be aware of their plan failures — and the resources available to correct them.

Operational failures are the most prevalent problem uncovered during IRS audits of SIMPLEs and SEP plans. The most common operational error is the failure to amend the plan for the new Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) limitations. Check with your plan administrator to make sure you're on schedule with your EGTRRA restatements.

For SEP plans in particular, another frequent error deals with plan participation and eligibility requirements. Many SEP plans inadvertently exclude eligible employees from plan participation. Employees are eligible to participate if they're at least 21 years of age, were employed for three out of the last five years, and earned a minimum of \$500 in the current year. For included SEP participants, sponsors and administrators often make mistakes in allocating contributions and allowing participants to make contributions that surpass the permissible limits.

Many SIMPLEs, on the other hand, aren't making employee-elective deferral deposits on a timely basis. The Department of Labor requires that plan administrators deposit salary deferrals no later than 30 days following the month in which the employee would have otherwise received the money.

Some SIMPLE and SEP operational errors occur because plan sponsors and administrators haven't taken the time to thoroughly read and understand their plan documents. For example, in a SIMPLE a plan administrator may use definitions of compensation and matching contributions that differ from what is actually stated in the plan document.

Review the requirements for operating your SIMPLE or SEP plan annually. Depending on the nature of the operational error, you may be able to correct it through the IRS's Voluntary Correction Program. This program was established as a means to correct certain operational plan failures without penalties.

The IRS also provides checklists and resources on its Web site at irs.gov/ep to assist plan sponsors and administrators in operating and maintaining SIMPLEs and SEP plans. Taking a few active steps now can make a world of difference should the IRS decide to audit your plan in the future.