

BENEFIT BYLINES

*Timely Articles Intended To Be Of Interest To Sponsors Of
Qualified Retirement Plans and Their Professional Advisors*

Fall 2014

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PPA Plan Document Restatement

As discussed in our mailings to clients and most recent newsletters, plan document restatements are now required for profit sharing, money purchase and 401(k) plans. We have begun the restatement process for those clients who have responded thus far. If you have received our mailing and have not yet responded, we urge you to do so in the near future. Although the restatement deadline is April 2016, we should have discussions over the coming months (which may require some in depth consulting) to determine what features to incorporate in the restatement. Please don't hesitate to call Marie Dawson, our Director of Compliance, or your ABP administrator should you have any questions regarding the process ■

Washington Update

In prior issues of Benefit Bylines, we have alerted readers to various proposals coming out of Washington, some of which, if enacted, would be highly detrimental to the private retirement system and the financial security of American workers. Fortunately, none of the more problematic proposals (such as capping retirement savings or double taxing elective deferrals) has gained traction thus far. While we can all be critical of Congress and the Administration for not getting much done in 2014, the failure to enact major pension legislation this year may have actually been a positive development. The status quo is better than some of the far-fetched ideas that were being proposed.

Looking ahead to 2015, there continues to be considerable differences among various factions in Washington over the direction we should take with respect to Federal spending, the budget, immigration, foreign policy, separation of powers between Congress and the Administration, and other matters. Despite this, there is cause for optimism that a few positive legislative initiatives may actually be passed by Congress and signed into law next year. Republicans increased their majority in the House and took control of the Senate in the recent mid-term elections. However, elected officials in both parties know that there is a high level of voter dissatisfaction with "business as usual". (Continued on Page 3)

Should You Consider a Cash Balance Plan?

With the economy continuing to show improvement, do you find that your business has more substantial and predictable taxable income than in recent years past?

As you move closer to retirement, are you concerned that your retirement savings may not be sufficient?

Are you maximizing your 401(k)/profit sharing deductible contribution allocations year after year and want to go beyond these savings levels?

If you can answer "yes" to the above questions, now may be the time for you to consider or revisit the possibility of adding a Cash Balance Plan to your employee benefit programs.

A Cash Balance Plan is a hybrid type of defined benefit pension plan that has many of the characteristics of a defined contribution type of tax qualified retirement plan. (Continued on Page 2)

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(Should You Consider a Cash Balance Plan? - Continued from Page 1)

In a Cash Balance Plan, a hypothetical account is established for each participant. This account is credited with contributions and interest each year. The benefit that is ultimately distributed to a plan participant upon retirement or other separation from service is the value of this hypothetical account.

In a Cash Balance Plan, the annual contribution credit is specified by the plan document, producing a more predictable annual funding requirement than is typically the case with traditional defined benefit plan designs. With prudent plan investments, it is very likely that the contribution credits defined by the plan will fall within the range of acceptable funding requirements each year. Because Cash Balance Plans are not subject to the maximum annual contribution limits applicable to defined contribution plans, contribution credits/deductible contributions may be significantly higher than would be possible in a defined contribution plan. For example, deductible contributions could be as high as \$230,000 for a 60-year-old executive making \$250,000 per year and retiring at age 62.

The interest crediting rate is also defined by the plan document and is typically a fairly conservative rate of return. This means that participants' accounts are generally not exposed to market swings, so they can be assured that their cash balance accounts will be there at retirement.

Cash Balance Plans can allow business owners who have put off saving for retirement in order to grow their businesses to establish and rapidly accumulate substantial retirement savings in their hypothetical accounts, often at minimal additional cost for their employees. The opportunity for substantial and predictable funding levels for this type of plan also provides a great vehicle for additional tax deductions.

If your economic outlook has turned rosy, now may be a great time to check out the benefits of a Cash Balance Plan. (For more information about these plans, please see the article "Are You a Candidate for a Cash Balance Plan?" in the Fall 2013 issue of *Benefit Bylines*.) ■

Small Plan Audit Exemption Not Absolute
(be aware of issues when investing plan assets in non-qualifying investment alternatives)

As a general rule, small retirement plans (those covering fewer than 100 participants) have been administratively exempted from the requirement to engage an independent accountant to perform a financial audit of the plan each year. This is good news given the

substantial expense associated with such an audit. However, as indicated by the title of this article, the small plan audit exemption is not absolute.

Audit Exemption

One of the following prerequisites must be satisfied for a small plan to qualify for the audit exemption:

1. *At least 95% of the assets of the plan must be invested in what is called "qualifying assets", or*
2. *The plan's fidelity bond must be sufficient to cover at least 100% of the value of non-qualifying assets, **and** the Plan's Summary Annual Report (SAR) must include additional information, as discussed below.*

"Qualifying assets" are assets held by a bank, insurance company, broker-dealer, mutual fund and certain other regulated entities. Participant loans, qualifying employer securities, and self-directed accounts held by a regulated financial institution also generally satisfy the definition of qualifying assets.

"Non-Qualifying assets" are assets that are not held by a financial institution. This includes limited partnerships, real estate, mortgages, artwork, and securities of closely held corporations.

ERISA/Fidelity Bond

The option for small plans to cover "non-qualifying assets" using the Plan's ERISA/fidelity bond is almost always more attractive than incurring the work effort and expense associated with an independent audit. Further, the basic minimum required bond (10% of total plan assets) may cover or nearly cover the amount of non-qualifying assets. Significantly, the requirement to have the bond cover 100% of non-qualifying assets is **not** in addition to the 10% of total asset rule. Therefore, if the aggregate value of non-qualifying assets is less than 10% of total assets, no additional coverage is necessary to meet the minimum bonding requirement.

Summary Annual Report

In addition to satisfying the fidelity bonding requirements discussed above, small plans with greater than 5% of assets in non-qualifying investments must provide increased disclosures in order to avoid the expense of an audit. Specifically, each year's Summary Annual Report which is distributed to employees must (a) include the names of financial institutions holding plan assets as well as the name of the insurer issuing the

fidelity bond, (b) notify participants of their right to receive copies of financial institution plan records, and (c) inform participants of their right to contact the Department of Labor (DOL) regional office if the employer fails to provide required disclosures. Further, on request, the employer must provide copies of the fidelity bond and financial statements at no charge.

Observations

Clients who invest plan assets in limited partnerships, real estate and other non-qualifying assets (as identified above) need to monitor those investments in light of these rules. They cannot assume that their plans automatically qualify for an audit exemption just because they cover fewer than 100 participants.

Clients who invest in non-qualifying assets also need to be mindful of other ERISA requirements such as the need to value those assets annually, potential Unrelated Business Taxable Income (UBTI), and a variety of potential traps that could result in prohibited transactions. Further, having a high percentage or dollar value of total plan assets reported as “Other Assets” on the plan’s Form 5500 return creates a “red flag” that may invite an audit by the IRS.

The majority of ABP’s clients invest 100% of plan assets with regulated financial institutions. Those clients who have fewer than 100 participants automatically qualify for the small plan audit exemption.

We encourage clients who are inclined to invest plan assets in non-qualifying arrangements to discuss those investments with their plan’s investment advisor and possibly an ERISA attorney. Non-qualifying investments often provide significant financial opportunities, but some involve problematic issues such as the need for independent appraisals, potential prohibited transactions, and Unrelated Business Taxable Income, to name a few. ■

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As a result, there is increased interest among members of both parties in finding areas where agreement can be reached and legislation passed.

Pension/retirement savings reform legislation is one of the areas where there is bipartisan interest in doing something. Of course, what constitutes “reform” is in the eyes of the beholder. The risk of ill-conceived ideas finding their way into law continues to be present. However, there appears to be strong support for measures that would expand the private retirement system to cover more workers in 401(k) plans or payroll deduction IRAs without necessarily requiring employer contributions.

Significantly, two staunch supporters of the private retirement system will move into positions of substantial influence in the next session of Congress. Orrin Hatch (R-Utah) will become Chair of the Senate Finance Committee and Paul Ryan (R-Wis) is likely to become the next Chair of the House Ways and Means Committee. Both of these committees have jurisdictional responsibilities over tax legislation which (for better or worse) typically includes pension matters.

Last year, Senator Hatch introduced comprehensive pension legislation called the “Secure Annuities for Employee Retirement Act”, better known as the “SAFE Act”. That bill is divided into the following 3 Titles:

Public Pension Reform

Private Pension Reform

Individual Retirement Investment Reform

The 2014 version of the SAFE Act proposal included some interesting provisions that, in general, were viewed positively by the private retirement community. Senator Hatch intends to reintroduce an updated version of the SAFE Act in the next session of Congress where it is expected to help shape the debate on pension reform.

Observation

Despite deep philosophical differences regarding spending priorities and taxes, there is the possibility that at least modest tax-reform may occur in 2015. It is perhaps more likely that pension legislation will be enacted, given increased interest in retirement issues by influential members of both political parties. There also appears to be heightened awareness of the need to expand worker coverage and increase retirement savings. In future issues of Benefit Bylines, ABP will provide updates on significant legislative initiatives and other issues impacting private retirement plans and our clients. ■

Survey Says 401(k) Plan is a “Must Have” Employee Benefit

In a recent survey commissioned by Charles Schwab, having a 401(k) plan was selected as a “must have” employee benefit program by 87% of those who responded. This was second only to employer-sponsored health insurance which was rated the highest.

The same survey revealed that 401(k) participants spend less time making 401(k) plan investment decisions than they do researching other choices such as buying a car. (Continued on Page 4)

(Survey Says 401(k) Plan is a “Must Have” Employee Benefit - Continued from Page 3)

The lack of participant attention to 401(k) plan investments reinforces the need to provide ongoing participant education. ABP strongly recommends that all of our 401(k) and 403(b) plan clients retain the services of a qualified investment advisor. As part of their service engagement, most advisors agree to meet periodically with participants to discuss general investment principles and the specific investment choices available in their employer's plan.

The Schwab survey is further evidence of the fact that Participants understand the importance of having a retirement savings vehicle at work but may not be sufficiently educated to take full advantage of its benefits. ■

DOL Inspector General Audits EBSA

In a companion article in this issue of Benefit Bylines, we discuss the fact that the “small plan exemption” from the requirement to engage an independent accountant is not automatic. ABP's motivation to publish that article is due, in part, to issues being raised by the Office of the Inspector General of the Department of Labor. Specifically, the Inspector General is looking into whether or not the Employee Benefits Security Administration (EBSA) is providing sufficient oversight of small retirement plans that are not required to be audited by independent accountants. Among other functions, the EBSA provides oversight of Form 5500 Annual Report filings, SPD and Summary Annual Report disclosures to participants, and independent plan audits.

Large retirement plans (generally those covering more than 100 participants) receive extensive scrutiny by reason of their annual audit by an independent accountant. However, small plans (generally those covering less than 100 participants) escape that layer of scrutiny.

The Inspector General's office is looking at the documentation used to determine the number of participants at the beginning and end of each year. In addition, they appear to be particularly interested in small plans that are invested in non-qualifying assets (see companion article for definitions) and the types of disclosures being provided by those plans related to plan assets.

You May Be Hearing from the Inspector General

As part of this initiative, the Inspector General has begun sending out letters to an undisclosed number of small plan sponsors. The letters request copies of the Plans' Summary Annual Reports, documentation of qualifying investments, financial institution certifications, trust statements and related asset schedules, and documentation of the calculation of the number of participants at the beginning and end of the year.

What To Do

At this juncture, we have no way of predicting how many of ABP's clients will be contacted as part of this initiative. If you should receive a letter, please forward it to ABP. Your plan's dedicated ABP administrator will guide you through the process and help you prepare a response. There is no need to panic, but please do not ignore any correspondence you might receive. ■

Associated Benefit Planners, Ltd.

Associated Benefit Planners, Ltd. (ABP) is an independent consultant and third party administrator (TPA). We specialize in the design and administration of employer-sponsored retirement/savings plans, including 401(k) arrangements. ABP also provides plan document and compliance support for Section 125 Plans and Employee Welfare Plans, operating on a fee-for-service basis.

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