ASPA
Dedicated to the Private Pension System

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Responding to the Mutual Fund Scandals

by C. Frederick Reish, APM, Kenneth R. Robertson, CPC, and Debra A. Davis, Esq.

BY NOW, MOST CONSULTANTS TO 401(k) PLANS HAVE RECEIVED COUNTLESS QUESTIONS REGARDING MARKET TIMING AND LATE TRADING—AND THE IMPACT ON THE MUTUAL FUNDS HELD BY 401(k) AND 403(b) PLANS. FIDUCIARIES WANT GUIDANCE ON THEIR LEGAL RESPONSIBILITIES AND ON THE STEPS NECESSARY TO FULFILL THOSE DUTIES.

WHAT SHOULD YOU TELL THE FIDUCIARIES?

In short, the answer is that fiduciaries need to engage in a prudent process to evaluate the facts and their impact on participants. This article discusses the process fiduciaries should use and the factors and issues they should consider in reaching a decision.

WHAT ARE THE PRINCIPAL TYPES OF MISBEHAVIOR INVOLVED IN THE SCANDALS?

Late trading and so-called "market timing." As explained by the SEC's Director of Enforcement:

> ***Late trading*** refers to the practice of placing orders to buy or sell mutual fund shares after the time at which the funds calculate their net asset value (NAV)—typically 4:00 p.m. Eastern Time (ET)—but receiving the price based upon the prior NAV already determined as of 4:00 p.m. Late trading violates the federal securities laws concerning the price at which mutual fund shares must be bought or sold and defrauds innocent investors in those mutual funds by giving to the late trader an advantage not available to other investors.
>
> ***Timing abuses*** refer to excessive short-term trading in mutual funds in order to exploit inefficiencies in mutual fund pricing. Such inefficiencies are based on pricing anomalies in securities held by certain types of funds. It is a

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WASHINGTON UPDATE

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Late-Day Madness

by Brian H. Graff, Esq.

As we predicted in *ASPA ASAP 03-27*, in early December the Securities and Exchange Commission (SEC) proposed rules that would, if finalized in their current form, dramatically impact 401(k) plan administration. Specifically, the proposed rules would require that all mutual fund trades, including those through retirement plans, be received by the mutual fund company by 4:00 p.m. EST in order to get that day's closing price (referred to as the "hard 4:00 p.m. close"). For those of you familiar with the administration of daily-valued retirement plans, such a requirement would clearly affect how participants' trade requests are processed. As a practical matter, it would result in 401(k) plan participant trade requests being processed at least the next day, or possibly two days after the request is made. Treating 401(k) plan participants as such second-class investors is clearly unacceptable from a retirement policy standpoint.

ASPA's Government Affairs Committee has been extremely involved in responding to these proposed rules. We have taken a leadership role in creating a coalition of representatives from all sectors of the retirement plan industry affected by the proposed rule including third-party administrators, financial

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From the Editor

Details are Important

by Chris L. Stroud, MSPA

WORKING IN THE RETIREMENT PLANNING PROFESSION REQUIRES US TO PAY ATTENTION TO CERTAIN DETAILS. WE OFTEN USE MANUAL CHECKLISTS SO WE DO NOT FORGET ANY OF THE MANY TASKS INVOLVED IN DOING OUR JOBS CORRECTLY. THE MORE TECHNOLOGICALLY ADVANCED FOLKS HAVE PDS DEVICES OR COMPUTERIZED CONTACT MANAGEMENT AND TASK TRACKING SOFTWARE TO MAKE SURE NO DETAIL IS FORGOTTEN. WE RELY HEAVILY ON THESE TOOLS (ESPECIALLY THOSE OF US WHO ARE RAPIDLY APPROACHING OR BEYOND "CATCH-UP ELIGIBILITY AGE") BECAUSE EVERY DETAIL IS IMPORTANT TO US.

Our training in retirement plans also requires us to store certain details in our heads. Specific IRS code sections are indelibly etched in our memories. Certain calendar dates have special meanings to us because they represent government form due dates for various plan years. We have voice mail, cell phones, and e-mail to make sure we are always accessible in case anyone has more details for us that we need to act upon. We juggle our working and our home lives, doing our best to remember not only the details regarding our work, but also those details that are important to family members and friends.

But how good are we at taking note of details in other aspects of our lives? I recently realized that I had been missing out on some very important details. My husband and I travel frequently to the West Coast (of Florida, that is). It is a two-hour drive from Miami—mostly a straight, bumpy two-lane highway spanning across the Everglades. I usually considered it a boring drive, and since my husband always volunteered to do the driving, I would use this time to catch up on reading or to flip through my favorite magazines. Fortunately, I recently had to make the trip by myself late one afternoon, forcing me to keep my eyes on the road and forego the books and magazines. However, worried that I would be bored during the drive, before I began my trek I bought a book on CD to entertain me during the trip. Interestingly enough, I never listened to the CD. Once I was out of the city, I made a game out of looking in the canals for alligators (and yes, I saw several). While entertaining myself looking for alligators along the way, I also noticed many beautiful birds perched in the trees and others stalking fish in the canals. (Even the birds know that Florida is the place to spend the winter!) Just as I began to realize that I was actually enjoying the drive and the scenery, the most spectacular thing happened. The sun began to set, and as it lowered, the sky lit up in the most radiant colors. As I observed in awe the beauty that was unfolding before me (while occasionally forcing myself to watch the road!), I suddenly understood why numerous artists have devoted their entire careers to capturing the details of the unique beauty of the Everglades on canvas.

For the first time, I had paid attention to details that had never before been important to me. It was somewhat of a revelation to realize what I had been missing during past drives. As a result, I have resolved as this New Year begins to increase my awareness of the details of my surroundings. Practicing my new resolution just a few days ago, I noticed a small child in the car next to me, seated in a car seat facing backwards in the back seat. While at the stoplight, I amused myself by trying to make her wave. My efforts paid off, and the little girl quickly began waving her head and her hands, laughing and singing in such a way that her mother turned around to see what was amusing her. When the mother realized that I was the source of the entertainment, she looked at me and we exchanged a laugh and a smile. The stoplight changed and we all got on with our lives—but I realized, as I captured the details of that moment in my memory, that my heart was a little lighter and my life was a little richer for the experience. ▲

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The purpose of ASPA is to educate pension actuaries, consultants, administrators, and other benefits professionals, and to preserve and enhance the private pension system as part of the development of a cohesive and coherent national retirement income policy.

ASPA members are retirement plan professionals in a highly diversified, technical, and regulated industry. ASPA is made up of individuals who have chosen to be among the most dedicated practicing in the profession, and who view retirement plan work as a career.

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A Word from the Enrolled Actuaries Meeting Committee

IT IS HARD TO BELIEVE WE ARE 29! THE 29TH ANNUAL ENROLLED ACTUARIES (EA) MEETING AT THE MARRIOTT WARDMAN PARK HOTEL IN WASHINGTON IS COMING UP ON MARCH 21-24, 2004.

As always, the meeting's general sessions will explore timely topics that are relevant to all enrolled actuaries, such as discussions of some recent court decisions, Precept 8 of the Code of Professional Conduct, and the future of defined benefit plans. Our concurrent sessions have something for everyone, from discussions of restricted lump sums to a panel on cash balance plans. You will have several opportunities to interact with personnel from the Internal Revenue Service and the Pension Benefit Guaranty Corporation—one of the traditional attractions of the EA Meeting. The meeting committee is also keeping up with proposed legislation that affects funding requirements and will offer relevant sessions in those areas as they develop.

For the Monday luncheon speakers, we are pleased to have Tucker Carlson and James Carville. Both are co-hosts of CNN's "*Crossfire,*" and they should provide lively political commentary for this election year.

The EA Meeting is a great place to keep up with our ever-changing profession and a wonderful opportunity to network. Since this is the last year of the continuing education cycle, keep in mind that you can satisfy half of your EA continuing education requirements when you attend. ▲

Register today!

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Sal L. Tripodi, APM, a frequent and respected speaker at ASPA conferences, is the author of the 2004 edition of *The ERISA Outline Book*. Features include:

- **Full incorporation of recent Treasury regulations** on catch-up contributions, proposed rules under 401(k) and 401(m), ERISA §204 notices, retroactive annuity starting dates, Section 457 plans, age discrimination, and deemed IRAs;
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- **Final DOL regulations** on blackout notices; DOL guidance on allocation of plan expenses under a defined contribution plan, DOL opinion letters on 12b-1 fees, float earned by financial services providers, overdraft protection fees, and demutualization proceeds;
- **Key court cases** during the last few months, including cases on fiduciary liability, disclosures to employees, nonfiduciary liability, QDROs, and protecting accrued benefits;
- Reformatting of discussion in Chapter 6 on **notice and consent rules for distributions**;
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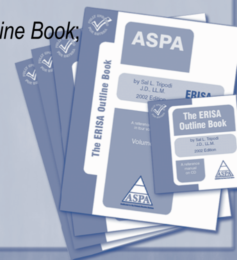

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Electronic Loan Process Using a Credit Card

by Michael E. Callahan, FSPA, CPC

FROM START TO FINISH, THE PROCESS OF INITIALIZING, MODELING, AND STRUCTURING PARTICIPANT LOANS IS LABOR INTENSIVE. WE MEASURED THE PROCESS OF COMPLETING A PARTICIPANT LOAN IN OUR OWN OFFICE AND FOUND THAT THE PROCESS INCORPORATED OVER 300 STEPS, NOT INCLUDING THE FUNCTIONS THAT THE RECORDKEEPER OR THE PAYROLL SYSTEMS PERFORM AND EXCLUDING REPORTING FEATURES TOO! SOME RECORDKEEPERS HAVE STREAMLINED THE PROCESS INTO A SELF-SERVICE, INTERNET-BASED DELIVERY SYSTEM, BUT UNFORTUNATELY, THERE ARE STILL MILLIONS OF PARTICIPANTS WHO ARE NOT INTERNET SAVVY OR WHO USE RECORDKEEPERS WHO HAVE NOT BUILT THOSE APPLICATIONS.

A new form of electronic loan processing is coming to the rescue. The "Credit Card Loan" detaches the loan processing from payroll and seamlessly provides loan services to plan participants with the help of the service provider.

This innovative concept was designed and patented by Nobel Laureate Professor Franco Modigliani and Francis Vitagliano. Professor Modigliani has written many papers on the subject of participant loans, employee savings, and the enhanced participation achieved by plans that have a loan program. Francis Vitagliano, Ed Burrows, MSPA, and Howard Phillips, MSPA, have championed this innovative program over the years.

HOW IT WORKS— FROM THE PARTICIPANT'S PERSPECTIVE

From the participant's viewpoint, the credit card loan process is similar to a revolving line of credit from a credit card issuer. In the pension business, our loans have been installment loans: normally a specific amount borrowed and repaid with a set amortization schedule not to exceed the limits specified in the law.

In order to facilitate revolving credit loans, the participant obtains a "line of credit" against the account balance. This line of credit is up to the maximum loan amount. The investment of the line of credit is limited to a fixed account in order to stabilize the loan balance. The loan amount is determined under standard loan procedures and a credit card is issued to the borrowing participant. The loan documentation is changed to reflect the necessary disclosure items.

When the participant needs the proceeds from the line of credit, the card is used to obtain cash or the participant uses the card with a merchant. The credit card issuing company extends the credit to the participant and then the credit card processing company (not the card issuer) electronically reaches into the fixed account of the recordkeeper on behalf of the participant and withdraws the funds needed to replenish the temporary credit provided to the participant by the credit card issuer.

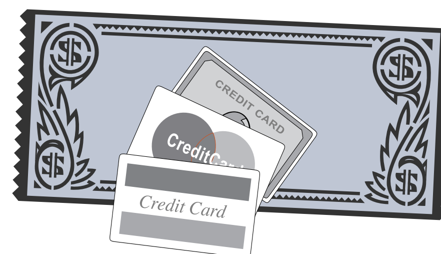
The participant receives a bill from the credit card processing company in the mail at home just like any other credit card. The minimum amount of the payment is based on a complex repayment process to ensure that the loan is repaid within 54 months.

Additional payments over the minimum are applied to the outstanding balance.

(*Note:* The plan sponsor, the payroll company, and the compliance specialist are not involved in the loan payback.)

Example: Assume a participant wishes to borrow against her 401(k) retirement plan for her daughter's first year at college. Let's assume the participant has a maximum loan amount of $10,000 (the "line of credit") and wishes to use some of the proceeds for purchasing books and other essential items. Assume again that the cost of those items is $1,700. The participant requests a loan amount for the maximum line of credit of $10,000. After executing the proper documents, a credit card is issued in the name of the participant with a maximum borrowing amount of $10,000. Money from the assorted investment choices is liquidated and transferred to the fixed account specifically set up for this loan purpose. In September 2003, the card is used to purchase the books and other essentials. A bill is sent at the end of the month showing the outstanding loan balance of $1,700 and an additional borrowing limit of $8,300. An amortization schedule is established using the specified interest rate for the card using a schedule that ensures the repayment occurs before the 60-month limit.

As the second semester starts, not all of the original loan was paid, but more than the minimum. The participant paid $500 of the loan balance. The second semester books were only $1,000 and the card was used for that



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Washington Update

Late-Day Madness

intermediaries, and daily valuation recordkeeping computer system companies. The objective of this coalition is to explore alternative solutions to the hard 4:00 p.m. close that will not so negatively affect retirement plan administration and participant's investment rights. As of this writing, there are two chief alternatives discussed below that we are exploring—one legislative and the other regulatory. However, it is certainly likely that these alternatives will be modified as the process continues and that other alternatives will emerge.

RELIANCE ON EXISTING AUDITED SYSTEMS

ASPA's Government Affairs Committee was successful in adding to the House mutual reform bill (H.R. 2420), which passed overwhelmingly in December, a provision that would require the SEC in any late-day trading rules to permit retirement plan administrators and intermediaries to continue to process trades after hours at that day's closing price, provided they rely on independently audited systems designed to prohibit the acceptance of trade requests after market close.

Under the legislation, an alternative to the hard 4:00 p.m. close would have to be provided for trades collected by TPAs and intermediaries who utilize these audited systems. Under this alternative, "after-hours" processing of any trade collected using the system would be permitted under current procedures, provided the TPA or intermediary receives the trade request before 4:00 p.m. EST. Generally, retirement plan administration is currently conducted using sophisticated software systems, which date and time stamp every trade receipt. These systems can be modified in a matter of months to ensure that there is no possibility of manipulation. The legislation would also require that the systems would be subject to an annual independent SAS70 or similar audit, as required by the SEC, to make sure that the system is performing as intended. Importantly, to reduce the potential financial impact of an annual audit, the legislation would permit TPAs to rely on the independent audits of retirement plan administration systems maintained by unaffiliated entities.

CLEARINGHOUSE TO PREVENT LATE-DAY TRADING

The proposed SEC rules suggest the possibility of a clearinghouse to process mutual fund trades as an alternative to the hard 4:00 p.m. close, which could also be used for processing retirement plan trades. Under the clearinghouse concept, the National Securities Clearinghouse Corporation (NSCC) or another qualified clearinghouse would act as an independent warehouse of retirement plan trade information. This concept would permit the SEC and mutual fund companies to objectively verify that retirement plan trade requests sent by retirement plan intermediaries and recordkeepers to the NSCC for processing after 4:00 p.m. EST were, in fact, received by such intermediaries or recordkeepers prior to 4:00 p.m. EST. The NSCC would be responsible for reconciling retirement plan trade request data received from intermediaries and recordkeepers prior to the close of the market with the retirement plan trade data subsequently sent to, as well as ultimately processed by, the NSCC after the close of the market. This reconciliation process would provide interested parties (*i.e.,* SEC, mutual fund companies) with exception reporting, which would allow them to objectively determine whether any late-day trading has occurred.

ASPA and representatives from all sectors of the retirement plan industry have met with the NSCC several times to discuss how the clearinghouse might work, as well as the feasibility of the clearinghouse. As of this writing, although some progress has been made as to how the clearinghouse might work, there is no consensus on its feasibility in terms of the technological capability at the NSCC as well as the significant systems costs that would be incurred by TPAs and intermediaries to utilize the clearinghouse. Further, additional efforts to simplify the clearinghouse will no doubt be made.

DATA PARADIGM

In addition to the clearinghouse trade processing function that the NSCC currently provides, the NSCC would become an independent warehouse of retirement plan trade data. The NSCC would be responsible for date and time stamping all such data in order to allow for verification of when it was received (*i.e.,* before or after 4:00 p.m. EST). Further, as outlined in more detail below, the NSCC would produce reconciliation reports weekly comparing the retirement plan trade data sent to the NSCC prior to market close with the trade data subsequently sent to, as well as ultimately processed by, the NSCC after the close of the market. The NSCC would have the role of informant, but not enforcement. It would be the role of the mutual fund companies (or the SEC through

audits) to determine whether any late-day trading (or other trading irregularity) is occurring. However, the reconciliation reports, as well as the retirement plan trade data sent to the NSCC by the intermediaries and recordkeepers, would be in a format that would permit the mutual fund companies (or the SEC) to objectively make such a determination.

Under the paradigm, intermediaries and recordkeepers would deliver daily to the NSCC three sets of retirement plan trade data as set forth below. Only retirement plan trade data could be delivered using this method. In other words, retirement plan data could not be commingled with non-plan trade data when delivered to the NSCC.

The first two sets of data (Sets A and B) would be stored by the NSCC and used to reconcile pre-close trade data with post-close trade data. The data would also be available for extraction and review by mutual fund companies (or the SEC). Mutual fund companies reviewing such data would be required to respect the confidentiality of the information and could only use it for the purpose of confirming the nonexistence of late-day trading. The third set of data (Set C) would be the actual retirement plan trades for the day processed after-hours by the intermediary or recordkeeper under existing rules and procedures. Intermediaries and recordkeepers who follow this paradigm would be permitted to process preliminary trade requests submitted to the NSCC before 4:00 p.m. EST (Set A) on an after-hours basis using that day's closing prices.

Set A— Preliminary Retirement Plan Trade Data

This data would reflect all trade requests made during the day by retirement plan participants. These "preliminary" trades would be delivered to the NSCC reflecting the previous trading day's closing prices. All data under Set A would have to be received by the NSCC before 4:00 p.m. EST. As a result, some intermediaries and recordkeepers may choose to have an earlier cut-off for certain kinds of plan transactions (*e.g.,* to verify that plan loans comply with ERISA). Any trade request sent to the NSCC under Set A could be revoked, provided, however, that the revocation is also received prior to 4:00 p.m. EST.

Data delivered to the NSCC under Set A would be divided into two subsets, A.1 and A.2. A.1 trade data would consist of all retirement plan trade data that would, if reflecting today's closing prices as opposed to the prior day's closing prices, only differ due to the change in net asset values of the underlying mutual fund investments. Retirement plan trade data sent to the NSCC under subset A.1 could be batched. However, subset A.2 trade data would have to be submitted on a participant-by-participant basis and would consist of retirement plan trades that would, if reflecting today's closing prices as opposed to the prior day's closing prices, differ for reasons in addition to the change in net asset values of the underlying mutual fund investments. Preliminarily, the kinds of requests that generate A.2 trades have been identified as participant-level loans, rebalances, and partial withdrawals. Each of the participant driven trades transmitted to the NSCC would need to be tagged with an identifier indicating the type of trade (*i.e.,* loan, rebalance, or partial withdrawal). The subset of participant-level data would be delivered to the NSCC using unique participant identifiers maintained by the data transferor (*i.e.,* the intermediary or record-keeper). The data transferor would be obligated to reveal the individual identity of the participant to the mutual fund company (or the SEC) upon demonstration of potential late-day trading abuses by such participant.

Set B— Closing Price Retirement Plan Trade Data

This data would reflect all of the same trade requests made by retirement plan participants during the day and transmitted to the NSCC under Set A. However, Set B would be delivered to the NSCC after market close and would reflect that day's closing prices. As with Set A, Set B would be transmitted to the NSCC in two identical subsets. Also, as with Set A, participant-level trade data would need to be tagged with an identifier indicating the type of request (*i.e.,* loan, rebalance, or partial withdrawal) generating the trade, and would be transmitted using unique participant identifiers.

With respect to retirement plan trade data submitted under Sets A and B, the NSCC would produce the following reconciliation reports. First, it would produce a report reconciling the retirement plan trade data submitted (optionally on a batched basis) in subset A.1 and subset B.1 based on the change in net asset values from the prior trading day's close to today's close. In this regard, the intermediary or recordkeeper would need to submit net cumulative trade totals with respect to the underlying investments for subsets A.1 and B.1, which would be used for reconciliation purposes.[1] Any differences between subsets A.1 and B.1 that cannot be explained merely due to changes in net asset values would be identified as an exception in the reconciliation report available for review by the mutual fund companies or the SEC. Regarding retirement plan trade data submitted to the NSCC in subsets A.2 and subsets B.2, a program would be developed that would compare the trades for each participant using the unique identifiers. The program would then produce a report highlighting any participant-level trades that differ outside permitted tolerances. Such flagged trades would be reported to the respective intermediary or recordkeeper who

submitted the trade for an explanation, which would be maintained by the NSCC for further analysis by interested parties (*i.e.,* mutual fund companies and the SEC). Because participant level trades would be tagged based on the type of trade involved (*e.g.,* loan, rebalance, or partial withdrawal), the reasons for any difference (*e.g.,* a change from a buy to a sell in connection with a rebalance) can be objectively reconstructed allowing such interested parties to identify illegal late-day trading.

Set C—
Processed Retirement Plan Trades

This data would reflect all of the trade requests made by retirement plan participants during the day processed after hours using the current day's closing prices under existing procedures utilized by intermediaries and recordkeepers. In other words, the trades actually processed through the NSCC could be transmitted entirely on an omnibus basis or any other basis convenient to the intermediary or recordkeeper. As noted above, only retirement plan trades would be permitted to be submitted under Set C.

In addition to the retirement plan trade data sent under Set C, the intermediary or recordkeeper would need to submit the net cumulative trade totals (as discussed under Set B) to the NSCC. The NSCC would reconcile these totals from Sets B and C confirming that the net cumulative trades under Sets B and C with respect to any mutual fund investment are identical. This report would be maintained by the NSCC for possible verification by the mutual fund company (or the SEC).

TRADING DIRECTLY WITH A MUTUAL FUND COMPANY

The paradigm suggested above for submitting retirement plan trade data to the NSCC could also be used by intermediaries and recordkeepers who choose to trade directly with a mutual fund company, but still desire the ability to process trades after hours.

OPEN ISSUES

In addition to questions about the technical capabilities of the NSCC and the significant industry costs that would be incurred, there are other open questions. First, ASPA strongly believes that, if the clearinghouse ends up as the chosen alternative, all retirement plan trades should have to be processed through the clearinghouse model. Mutual fund companies selling plans with only a single family of funds should not be given a market advantage, particularly given the enhanced risks to participants associated with such single fund family plans. Second, if the NSCC is chosen as the clearinghouse, it must permit all entities involved in the retirement plan industry access. Currently, some smaller entities do not have access to the NSCC, and if the NSCC has this clearinghouse responsibility, then the NSCC should not be permitted to deny access to smaller firms. Finally, and there will probably be more, the SEC would have to allow sufficient time for the NSCC and the retirement plan industry to develop and modify their systems to comply with the fairly complex paradigm discussed earlier.

SUMMARY

Although the legislative approach is clearly preferable, due to its minimal impact on current administrative practices, it is necessary to explore the regulatory alternative since it is not clear whether the provision in the House bill will be acceptable to the Senate. Further, it is unclear when or if the Senate will actually consider mutual fund legislation. The SEC has already informally indicated that they do not view the approach taken in the House bill as acceptable. Consequently, although the clearinghouse is far from simple and will clearly result in significant costs to the industry, it may well be the only option available for TPAs and intermediaries who want to continue providing same-day trading for plan sponsors or participants.

The extensive media focus on the mutual fund scandals has placed a great deal of pressure on the SEC and Congress to be seen as "doing something" to protect investors. The SEC's late-day trading rules are just the first set of rules that will affect retirement plan administration—there will certainly be others. Unfortunately, in these situations the government may sometimes adopt rules that incur costs in excess of the costs resulting from the abuses the rules are intended to prevent. ASPA's Government Affairs Committee will continue to stay very involved to try to minimize this effect as much as possible. ▲

Footnote

[1] The intermediary or recordkeeper would need to submit net cumulative trade totals with respect to all of the underlying NSCC-traded investments under data Set B for comparison with data Set C.

Brian H. Graff, Esq., is the Executive Director of ASPA. Before joining ASPA, he was pension and benefits counsel to the US Congress Joint Committee on Taxation. Brian is a nationally recognized leader in retirement policy, frequently speaking at pension conferences throughout the country. He has served as a delegate to the White House/Congressional Summit on Retirement Savings, and he serves on the employee benefits committee of the US Chamber of Commerce and the board of the Small Business Council of America.

Dynamics of a Deal:

Considerations When Buying or Selling a Pension Service Business

by Elliot D. Raff, APM

IN RECENT YEARS, CONSOLIDATION HAS RESHAPED THE PENSION SERVICES INDUSTRY. SMALL LOCAL FIRMS WITH LIMITED RESOURCES AND DWINDLING PROFITS ARE COMBINING WITH OTHER FIRMS TO OFFER NEW SERVICES AND CAPTURE NEW REVENUES. REGIONAL INSTITUTIONS ARE CREATING FULL SERVICE FINANCIAL SERVICE SUBSIDIARIES BY ACQUIRING LOCAL FIRMS, AND NEW NATIONAL FIRMS HAVE EMERGED BASED ON A STRATEGY OF SERIAL ACQUISITIONS. THROUGHOUT THE INDUSTRY, OWNERS ARE SEEKING EXIT STRATEGIES AS THEY CONTEMPLATE THEIR OWN RETIREMENT. THERE ARE MANY WAYS TO STRUCTURE A TRANSACTION, EACH WITH DIFFERENT ADVANTAGES AND DISADVANTAGES TO THE BUYER AND SELLER. SETTLING ON THE MOST APPROPRIATE STRUCTURE REQUIRES AN UNDERSTANDING OF THE TAX AND OTHER LEGAL CONSEQUENCES, AN OWNER'S GOALS, AND THE PRACTICAL CHALLENGES FACING THE BUSINESS, WHERE RELATIONSHIPS ARE CRITICAL AND THE CALENDAR UNFORGIVING. THIS ARTICLE DISCUSSES THE REASONS FOR BUYING OR SELLING A PENSION PRACTICE, HIGHLIGHTS THE DIFFERENT LEGAL STRUCTURES THAT CAN BE USED, AND DISCUSSES SOME OF THE MOST IMPORTANT PRACTICAL ISSUES THAT MUST BE ADDRESSED FOR A TRANSACTION TO SUCCEED.

LETTERS OF INTENT AND CONFIDENTIALITY AGREEMENTS

Whether buying or selling, early on, a company may engage a business broker or other agent to help find an interested party, arrange financing, and negotiate the terms of the transaction. When a prospective buyer/seller has been identified and the basic terms of a deal have been agreed upon, the parties will typically be asked to sign a letter of intent, often written by the broker, describing the general terms of the transaction in easily understood language. Banks provide commitment letters describing the terms of their financing.

While a party may view a letter of intent as simply a checklist to confirm that everyone is "on the same page" before proceeding to incur the expense of engaging in due diligence and drafting formal contracts, parties are often surprised to discover that they are contractually bound by the letter of intent. Preliminary agreements, which may seem innocuous, can nevertheless have significant *and binding* legal consequences, making it difficult and/or costly to change agreed upon terms (or back out of a deal).

Equally important, the parties should enter into a confidentiality agreement. Key terms to consider carefully include what is covered as confidential information, its return in the event the deal does not close, and legal remedies for violation (immediate injunction). The agreement should also include a process for handling requests by third parties for confidential information (*e.g.,* providing advance notice of the request, allowing the other party to object to disclosure, etc.) so the party whose information is at risk can take steps to prevent disclosure. Although it may be impossible to totally eliminate concerns about disclosure, a well-drafted confidentiality agreement can go a long way in protecting a seller from improper disclosure.

WHY BUY OR SELL A PENSION SERVICE BUSINESS?

WHY BUY?

There are many reasons for buying a pension service business:

Roll Up for Eventual Sale: An owner may desire to acquire other firms as the first phase of his/her own eventual exit strategy. Having greater market share may attract the interest of a larger institution that may ultimately buy out the owner. Greater market share may also enable the owner to command a premium price in the ultimate sale.

Leverage Infrastructure: As a company acquires additional business, adds new services, and engages more employees, it creates a greater overall ability. Size alone attracts new business, opportunities for cross marketing become prevalent, new ideas are attracted to firms that are growing, and more resources are available for marketing and development.

Leverage Buying Power: Having greater market share may allow a firm to obtain better pricing and servicing from other institutions. For example, an administration firm with hundreds of clients all in the same insurance company product will receive the most favorable pricing available and the highest level of service.

Enter New Markets: Rather than incur the cost and risk of entering a new locale by renting new office space, hiring new staff, and competing with existing firms, buying an existing local firm may be more attractive—the firm has clients, employees, a reputation, and a financial history that can be evaluated.

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Responding to the Mutual Fund Scandals

form of securities arbitrage—more specifically, "stale-price arbitrage." Because mutual funds are priced once daily, at market close, certain type of funds will sometimes have out-of-date security prices used in the calculation of the fund's NAV. Certain sophisticated investors rapidly bought and sold shares of those funds with NAVs that were too high or too low, and were able to realize substantial profits at the expense of the other shareholders.

An example of stale price arbitrage, or "market timing," can be found with international funds. If the US stock markets have large gains on a given day, the "market timers" would transfer their money into an international fund. As long as they made the transfer by 4:00 p.m. EST, they would buy in at the prior day's results in the international markets. The next day the speculators would move their money out of the international fund, together with a part of the gains that would have belonged to the long-term investors, but for the in-and-out trades. This scheme works, more often than not, because the international markets usually follow the lead of the US markets and because of news made public after the international market close. Such arbitrage has also occurred in small-cap equity funds (international and domestic) and several types of bond funds (such as high-yield bond funds).

Although stale price arbitrage (also referred to as market timing) itself is not illegal, mutual fund advisers have an obligation to ensure that mutual fund shareholders are treated fairly and that one group of shareholders (*i.e.,* market timers) is not favored over another group of shareholders (*i.e.,* long-term investors). In addition, when a fund states in its prospectus that it will act to curb market timing, it must meet that obligation.[2]

Both late-trading and market-timing favor a small group of short-term traders over long-term investors. As a result, 401(k) fiduciaries should decide whether funds that permit those activities are consistent with the purpose of a retirement plan. The answer seems obvious...that they are not—because ERISA Section 404(a) requires that fiduciaries act for the purpose of providing retirement benefits to participants. These practices would drain retirement benefits from the participants who are buy-and-hold investors.

In testimony before Congress, Eliot Spitzer summed it, thusly,

> *Permitting market timing is contrary to the interests of a fund's long-term investors. As the* Financial Analysts Journal *observed last summer: "Because the gains [of market timers] are offset by losses to other investors in the fund, the funds clearly have a fiduciary duty to take some preventive action. All the gains are being offset, dollar-for-dollar, by losses incurred by buy-and-hold investors."*
>
> *Indeed, mutual funds recognize that market timing works to the detriment of funds' long-term shareholders, which is why their prospectuses convey to shareholders the impression that market timing is not permitted.*[1]

ARE THESE PRACTICES WIDESPREAD?

Yes.

According to Congressional testimony:[3]

- About half of the 88 largest mutual fund complexes (responsible for approximately 90% of all fund assets) acknowledged having arrangements with certain shareholders to allow market timing.
- Out of 34 large broker-dealers, almost 30% admitted to assisting customers in making market-timing trades, and 70% said they were aware of customers making those trades.
- Approximately 10% of the fund companies appear to have permitted late trades.
- More than 25% of the brokerage firms allowed late trading.
- Over 30% of the mutual fund companies disclosed details about their holdings to favored customers—which could help those customers with market timing.

DO FIDUCIARIES NEED TO ACT?

Yes.

ERISA Section 404(a) requires fiduciaries to act prudently and in the best interest of participants and beneficiaries. While ERISA does not specifically address issues of mutual fund management, it does require that a fiduciary give "appropriate consideration to those facts and circumstances that...the fiduciary knows or should know are relevant to the particular investment...."[4]

The Preamble to the Final Regulation for ERISA Section 404(c) explains, "All of the fiduciary provisions of ERISA remain applicable to both the initial designation of investment alternatives...and the ongoing determination that such alternatives and managers remain suitable and prudent investment alternatives for the plan. Therefore, the particular plan fiduciaries responsible for performing these functions must do so in accordance with ERISA."[5]

As one federal court has explained "To enforce [ERISA's fiduciary duties], the court focuses not only on the merits of the transaction, but also on the thoroughness of the investigation into the merits of the transaction."[6] Another court stated "In determining compliance with ERISA's prudent man standard, courts objectively assess whether the fiduciary, at the time of the transaction, utilized proper methods to investigate, evaluate, and structure the investment; acted in a manner as would others familiar with such matters; and exercised independent judgment when making investment decisions."[7]

In a recent speech, a high-ranking Department of Labor official discussed the prudence requirement in the context of the mutual fund scandals:[8]

> Allegations of improper mutual fund practices where a plan is invested must be factored into the fiduciary's determination of the continuing appropriateness of that investment. The plan fiduciary may need to contact the mutual fund's management for information regarding the trading practices and take appropriate action.
>
> We expect that fiduciaries will be attentive to activities that materially affect the plan's investment in the mutual fund or expose the plan to additional risk. Therefore, plan fiduciaries should have more active communication with mutual fund management in order to meet their obligations under ERISA.
>
> Fiduciaries may also ultimately have to decide whether and how to participate in lawsuits or settlements arising from improper mutual fund activities. Of course, a plan fiduciary must weigh the cost of participating in a lawsuit against the likelihood and amount of potential recovery.

The message is clear...fiduciaries must be attentive to the practices of the mutual funds and their management companies. The State of Maryland provides some questions for mutual fund management companies that fiduciaries may want to use as guidance. (*See*, http://www.reish.com/publications/pdf/maryland.pdf.) However, fiduciaries cannot "blindly" rely on the statements of the mutual fund management companies.[9] Instead, they should verify those statements with their outside consultants, investment advisors, or independent industry sources.

HOW SOON DO FIDUCIARIES NEED TO MAKE DECISIONS?

If a fund no longer engages in these improper activities, then fiduciaries may have time—three months, six months, or even longer—to conduct a diligent examination and reach a conclusion.

By their very nature, mutual funds move, more or less, in tandem with the market (or with the particular investment style or market sector they represent). That is, their value reflects the aggregate market values of the stocks in the companies they own. Bad news about the behavior of a particular fund or its management company will typically not directly or immediately affect the value of that fund. Unlike the stock of an individual company, the share value of a mutual fund should not drop precipitously because of scandals involving the management of the fund. As a result, fiduciaries should have time to conduct a prudent and thorough analysis. *[Author's note: A scandal could, in some cases, lead to a "run on the fund," in which case the resulting liquidity crunch and the need to sell off blocks of securities could adversely affect the fund's redemption price.]*

If the fiduciaries believe that a fund continues to allow market timing or late trading, though, they should move quickly to remove it. Also, fiduciaries should pay close attention to collateral issues at the investment advisory firms for the mutual funds in their plans. For example, a firm may have acted improperly and, as a consequence of remedying the matter, may have undergone significant organizational changes, including changes in executive staff, the chief investment officer of the advisor, and/or managers of the fund. If such changes are significant, that may be a factor that contributes to a decision to replace a fund.

WHAT ARE INVESTMENT EXPERTS RECOMMENDING?

There are a wide range of opinions among investment advisors, attorneys, industry experts, academics, and media commentators. However, with some exceptions, the voice of reason is to keep informed as information emerges and be thoughtful and deliberate in making decisions.

From the legal perspective of ERISA's fiduciary rules, the conclusions of other plans and well-known fund advisors are simply informative. That is, fiduciaries must engage in a prudent process to:

- Gather the relevant information; and
- Make an informed decision.[10]

Fortunately, there is time to be deliberate and thorough.

What are some of the factors that should be considered by fiduciaries in making the decision about an implicated fund or advisor?

As a first step, fiduciaries should perform their usual procedures for monitoring the funds offered by their plans. Independent of these improper activities, they should make sure that the funds are reasonably expected to

perform well in the future, have reasonable expenses, and satisfy the other criteria in their investment policy statements.

Next, fiduciaries need to determine the significance of these revelations for the future performance of these funds. Was it just a mistake made by an otherwise reputable advisor? Was it through inadvertent lack of oversight? Or, does the management company have an opportunistic culture that emphasizes immediate profit over long-term shareholders and/or revenues over investment excellence? In other words, is the organization itself worth the fiduciaries' continuing trust? Here are some guidelines that will help fiduciaries answer those questions:

- **Have the management company and the directors of the fund acknowledged the impropriety** of their conduct, apologized for that conduct, and promised to restore all money taken by late traders and market timers—even if it wasn't illegal—and all profits earned by the management company on the "fast money"? These actions will indicate if the organization is focused on legalities or on doing what is right for long-term shareholders.
- **Has the investment management company responded quickly to the situation—**communicating its intentions and standards, removing people and implementing better procedures, engaging an independent party to review activities, and working with the regulatory authorities to resolve the enforcement activities? The quicker the management company can correct its deficiencies, resolve the government examinations, and re-focus its energies, the better it is for participants.
- **Has the organization terminated the people involved in the improper conduct—**even if it wasn't illegal, including the senior managers who oversaw the people involved? That will give some insight into whether the organization views the issue as a legal matter or a cultural and ethical matter. If the organization prioritizes legal compliance, but not ethical values, then there may be other "legal" ways to injure participants in the future.
- **Has the fund instituted specific procedures to eliminate late trading and market timing?** The first step is for the fund to publish a statement that it will not tolerate either practice. Then, look for specific fixes, like a redemption fee for "buys-and-sells" of a fund within a limited time period, for example, one week or 30 days.
- **Has the fund issued a statement** that it supports its long-term investors and will take steps to prohibit any activities that will deprive them of the full benefit of their investments? Late trading and market timing are today's issues. We can only imagine what will come next—but we need to know that the investment advisors of the funds in our 401(k) plans are committed to delivering full value to participants.

In making a determination, it is important to be attentive to the principles underlying any judgment. Procedural prudence is at the heart of fiduciary actions, and procedural prudence requires consistency and even-handedness. The reasons for taking a particular action should be identified, and will set a precedent for subsequent actions in the future.

There is also an alternative scenario that may be appropriate where the investment option line-up only offers one option for a major asset class (such as an international fund), and the fund has been put on watch as a result of the scandal or organizational changes. In that case, it may be appropriate to add an alternative fund in the same asset class.

WHAT SHOULD FIDUCIARIES TELL EMPLOYEES?

ERISA does not specifically require that fiduciaries communicate with participants about their review of participant-directed investments. Further, there is nothing in the general fiduciary responsibility or disclosure rules that requires fiduciaries to advise participants during their inquiry into the continuing suitability of a particular investment option. However, there are a number of factors that should be considered when deciding whether to inform participants of the review of these activities:

- **If a plan offers one of the implicated funds:**
  - While it may not be legally required, it may be reassuring to participants to receive an explanation that the fiduciaries are investigating the situation and will act to protect the interests of the participants.
  - While the 404(c) regulation is not clear, a conservative reading would require that fiduciaries [for plans that want 404(c) protection] provide the participants with "sufficient information to make informed decisions with regard to investment alternatives available under the plan...."[11] Arguably, until the fiduciaries' examination of the implicated fund is complete, there is nothing material to report. Once a decision is reached, though, it would be advisable to communicate that decision to the participants. [Note that, if a participant requests information received by the fiduciaries regarding the investments, the 404(c) regulations require that any materials provided to the plan that relate to the plan's investment alternatives be given to that participant.[12]]
- **If a plan does not offer an implicated fund:** It may be reassuring to the participating employees to confirm that fact and to advise them that the fiduciaries are monitoring the situation.

- **If the plan decides to remove an implicated fund**, the fiduciaries *must* advise the participants of that fact and of the replacement fund. Specific information about the replacement fund should be communicated to comply with the fiduciary duties under ERISA Section 404(a). In addition, if the plan intends to comply with 404(c), the required notices and information about the replacement fund should be conveyed. Finally, the participants should be notified of the fiduciary decisions regarding mapping and timing.
- **If participants ask about the plan's investment options,** fiduciaries are required by ERISA to give full and truthful answers to such questions.
- **If, after examining the matter, the fiduciaries decide to communicate with participants about an implicated fund** offered by their plans, it would be helpful to educate participants on what their alternatives are (such as an alternative fund in the same asset class), if they choose not to retain money in a fund that has been tainted by the scandal.

CONCLUSION

In the final analysis, the issue is whether fiduciaries believe that the mutual fund and its advisor will support their responsibilities for providing prudent investments to participants. Fiduciary decisions must be reached through analytical and deliberative processes, and not through reactions to newspaper headlines. ▲

Footnotes

[1] Testimony of Eliot Spitzer, New York Attorney General, before the US Senate Subcommittee on Financial Management, the Budget and International Security, Governmental Affairs Committee, November 3, 2003.

[2] Testimony of Stephen M. Cutler, Director, Division of Enforcement, US Securities & Exchange Commission, before the US Senate Subcommittee on Financial Management, the Budget and International Security, Committee on Governmental Affairs, November 3, 2003.

[3] Testimony of Stephen M. Cutler, supra.

[4] DOL Reg. ß 2550.404a-1.

[5] 57 FR 46906, 46922 (October 13, 1992).

[6] Howard v. Shay, 100 F.3d 1484 (9th Cir. 1996).

[7] Laborers National Pension Fund v. Northern Trust Quantitative Advisors, Inc., 173 F.3d 313 (5th Cir.), cert. denied sub nom, Laborers Nat'l Pension Fund v. American Nat'l Bank & Trust Co., 528 US 967, 120 SCt 406, 145 L.Ed.2d 316 (1999).

[8] Speech by Ann Combs, Assistant Secretary, Employee Benefits Security Administration, US Department of Labor, to the Stable Value Investment Association National Forum, October 22, 2003.

[9] Howard v. Shay, 100 F.3d 1484, 1489 (9th Cir. 1996).

Footnotes (cont.)

[10] See, e.g., Laborers National Pension Fund v. Northern Trust Quantitative Advisors, Inc., 173 F.3d 313, 317 (5th Cir. 1999); Donovan v. Cunningham, 716 F.2d 1455, 1467 (5th Cir. 1983).

[11] DOL Reg. ß 2550.404c-1(b)(2)(i)(B).

[12] DOL Reg. ß 2550.404c-1(b)(2)(i)(B)(2)(ii).

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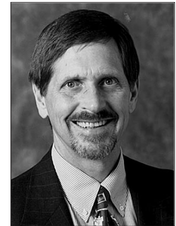

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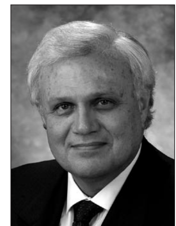

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Electronic Loan Process Using a Credit Card

purpose in January 2004. Traditionally, there would be two loans outstanding: the first for $1,700, with a minimum payment computed with a 60–month amortization schedule from September 2003 (and an outstanding balance of $1,200), and a second loan of $1,000 with an amortization schedule of 60 months beginning January 2004. The total minimum payment would normally be the sum of the two amortization schedule amounts. Under the new arrangement, a more complicated process has been developed that ensures that each charge is repaid within a 54-month period.

When payments are made, the credit card processing company sends a transaction to the recordkeeper and the amount in the fixed account is updated with the payment amount. The selected fixed account is periodically swept to maintain the exact line of credit initially requested. The swept interest from the fixed account is reinvested into the selected fund choices of the participant.

If the participant misses payments on the loan, the credit agencies are notified and the credit card processing company sends all dunning notices and attempts to collect on the loan on behalf of the trustees or plan administrator. If the minimum payments are not made, the participant's loan goes into default and the credit card processing company issues the necessary tax forms (Form 1099-R and Form 945).

If the participant separates from service, the loan does not need to go into default. The loan payments can continue as if the participant is still employed, since there are no payroll issues. This process should help dramatically in the retention of pension assets. This concept will also facilitate loans for Taft Hartley plans which normally do not have a common payroll.

How It Works— From the Recordkeeper's Perspective

The transactions associated with this electronic loan processing will look almost identical to the transactions for self-directed brokerage accounts, with the additional sweeping of interest periodically. Transaction files are uploaded and downloaded through the credit card processing company through a singular roll-up mechanism. Aggregate loan balances are transferred too, with the credit card issuer having all the details of the loan and line of credit online for easy access by the participant, plan sponsor, recordkeeper, and compliance specialist.

Summary

The policy issues allowing, or not allowing, for loans in qualified plans are beyond the scope of this article. The debates will go on forever with good arguments on both sides. A 1998 GAO study found that participants considered having participant loans more valuable than having a company match. Others say that borrowing against your future is a bad decision since many people cannot afford the loan and default. Others contend that the loan interest is taxed twice; once when it is repaid with after tax money and a second time when it is ultimately taken out of the plan. This author defers those considerations to the plan sponsors that offer loan programs in their retirement plans.

Loans in our business are a fact of life. The credit card loan process dramatically simplifies the processing of loans, detaches the payroll complexity, offers a new and valuable service to the plan administrator, helps in the collection of loan payments, simplifies the reporting of defaulted loans, and provides easy access to information for the reporting and disclosure requirements under ERISA. Participants have more control over personal budgets and, if they separate from service, they can continue to repay loans in the same manner as before the separation. The employer and recordkeeper are not directly involved, and the ability to continue repayments should help dramatically in the retention of retirement assets.

From a compliance perspective, the loan concept can turn a process that currently costs more than recordkeepers can charge to a process that may actually be a revenue generator. ▲

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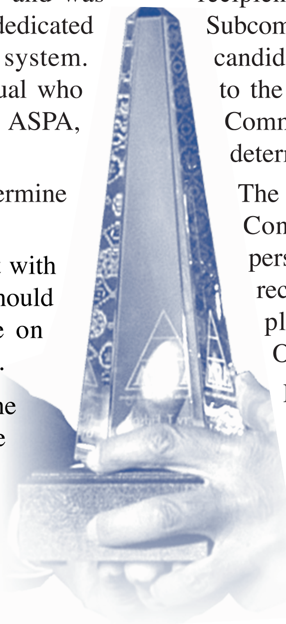
2004 Harry T. Eidson Founders Award Nomination Deadline is Approaching

NOMINATIONS FOR THE HARRY T. EIDSON 2004 FOUNDERS AWARD WILL BE ACCEPTED UNTIL JUNE 1, 2004, AND CAN BE SUBMITTED DIRECTLY FROM THE HOME PAGE OR MEMBERSHIP AWARDS AND HONORS SECTIONS OF ASPA'S WEB SITE AT **www.aspa.org**. YOU CAN ALSO COMPLETE AND SUBMIT THE NOMINATION FORM INSERT IN THIS EDITION OF *THE ASPA JOURNAL*.

In 1995, ASPA established the Harry T. Eidson Founders Award to honor the memory of our founder, Harry T. Eidson, FSPA, CPC. Eidson was the initial inspiration behind the formation of ASPA in 1966. Eidson firmly believed in the importance of a private pension system for the United States and was committed to building an organization dedicated to preserving and enhancing such a system. This award is presented to an individual who has made a significant contribution to ASPA, the private pension system, or both.



The following criteria are used to determine the nominee:

- The contribution must be consistent with the ASPA mission statement and should have a lasting, positive influence on ASPA or the private pension system.
- The contribution may be current, one that spanned many years, or one made years ago that ASPA or the private pension system benefits from today.
- The contribution should be a result of time devoted above and beyond reasonable expectations, not a result of time spent primarily for personal gain.
- The contribution may be have been made and/or recognized on a national or regional level; however, publicity is not a criterion.

Any voting ASPA member who knows someone who meets the award criteria can submit a nomination form. All nominations are reviewed by a special Eidson Award Subcommittee working with ASPA's Membership Committee Chair. Please note that the recipient need not be an ASPA member. If the Subcommittee determines that there is a deserving candidate, then such recommendation is made to the Board of Directors by the Membership Committee Chair. The Board makes the final determination at its July meeting.

The award is presented at the ASPA Annual Conference with the recipient receiving a personalized award memento. In addition, the recipient's name is engraved on a permanent plaque displayed in the ASPA National Office.

Previous winners include: Robert D. Lebenson, MSPA, in 2003; Curtis D. Hamilton, MSPA, CPC, in 2002; Ruth F. Frew, FSPA, CPC, in 2001; Leslie S. Shapiro, JD, in 2000; Howard J. Johnson, MSPA, in 1999; Andrew J. Fair, APM, in 1998; Chester J. Salkind in 1997; John N. Erlenborn in 1996; and Edward E. Burrows, MSPA, in 1995.

We encourage you to take the time and nominate a worthy candidate for this prestigious award. ▲

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Dynamics of a Deal:
Considerations When Buying or Selling a Pension Service Business

Offer New Services/Capture New Revenue: Again, rather than incur the cost of building the infrastructure needed to provide additional services, buying an existing business that specializes in that service may be much more attractive. For example, consider deals where banks with financial planning subsidiaries entered into the retirement plan consulting and administration market by acquiring established regional pension consulting/administration firms.

Of course, a transaction can provide a combination of these goals. For example, buying a firm that provides investment advisory brokerage and administration/recordkeeping services can provide a plan administration firm with entrance into a new business (investment advice), added market share, and buying power.

WHY SELL?

The two most common reasons for selling are the desire of the business owner to exit the business and to remain competitive in an increasingly tight market.

Exit Strategy: As owners of pension service businesses age, many are looking for strategies to realize the value of their equity and diversify their investments. Some owners want to preserve the independence of their firms, transferring ownership to a few key employees over time. Other owners want to maximize the value they receive, regardless of the purchaser and its ultimate plans for the business. Different goals lead to different transactions, but the ultimate goal remains similar—retiring from the business.

Remain Competitive: There is constantly increasing pressure on smaller firms when large financial institutions offer "free" administrative services in order to capture assets under management. Firms experiencing dwindling profits and client losses may seek to combine with other firms offering asset management or advisory services in order to remain competitive and boost profitability. These firms may want to become part of a larger organization that offers greater marketing and distribution channels, greater resources for technological expansion, and additional complementary services.

DIFFERENT WAYS OF STRUCTURING DEALS

ASSET SALE

An asset sale entails the transfer of legal title of assets from one firm to another. Most, if not all, of the assets sold will be intangible assets, such as client lists, existing client service contracts, leases, and goodwill. (Some tangible assets, such as computers, furniture, and supplies may be included, but these are incidental to the intangibles that are the reasons for the sale.)

Buyers usually prefer an asset sale because the buyer acquires only the assets and liabilities that are subject to the agreement. Undesirable assets and liabilities remain the seller's, unless expressly assumed by the buyer. In this way, a buyer can limit or eliminate liability for the seller's conduct (*e.g.,* taxes and penalties due to mistakes in plan administration).[1] Of course, many aspects of plan administration from a prior year affect administration in subsequent years, which can, if not handled carefully by the buyer, create liability for the buyer. Nonetheless, asset sales give a buyer greater ability to contain or avoid these liabilities.

For a seller, asset sales may be less desirable, mainly because of the typical tax treatment. Usually gain or loss is recognized upon the sale and, if the seller is a C corporation, the proceeds may be taxed twice—once to the corporation and again when received by the owner. To some extent, allocating some of the price to an owner's personal goodwill or a personal restrictive covenant may mitigate double taxation. Although double taxation is not an issue for an S corporation or limited liability company, the gain (or at least some of it) may be taxed as ordinary income.

STOCK SALE[2]

A stock sale involves the transfer of ownership of a business. The seller is the business owner, rather than the business itself. Business operations remain intact, subject to the new ownership, and the business retains whatever obligations and liabilities it previously held. Acquired liabilities may be "walled-off" in a separate legal entity, insulating other operating assets (*e.g.,* owners are not personally liable for corporate liabilities in most circumstances). Nonetheless, concern over hidden liabilities usually makes buyers less willing to purchase stock.

Despite this, there are many reasons for a buyer to purchase stock. Buying stock allows the buyer to obtain not only the business's operating assets, but also its existing legal structure and status, including licenses and contractual relationships (which may not be assignable in an asset sale).[3] Further, key employees may want to invest in their employer

and take over as the next generation of owners of an existing, successful business.

From the seller's perspective, a stock sale may be more desirable. The tax treatment is likely to be more favorable, as there would be no double taxation even for a C corporation and the gain is taxed as capital gain. Thus, the business owner will realize more net tax proceeds in a stock sale than in the typical asset sale. Also, the stock sale eliminates the post-transaction wind-up of the business, which can absorb a good deal of time and money. Thus, a stock sale is a more attractive exit strategy for the business owner.

REORGANIZATIONS

A "reorganization" under the Internal Revenue Code can take a variety of forms, all of which result in a tax-free transaction. Most reorganizations involve a merger of the seller (referred to as "the target") into the buyer or a subsidiary. A reorganization can also take the form of an exchange of assets for stock (allowing the buyer to leave liabilities behind). Like all other tax-advantaged structures, a reorganization is subject to strict requirements under the Internal Revenue Code. For example, the shareholders of the target must obtain ownership in the continuing entity. Because of this requirement (and others), reorganizations are not always favored, despite the tax treatment. Thus, a shareholder seeking to diversify his/her holdings probably will not be willing to receive stock, particularly if it is stock of a privately held corporation.[4] Similarly, owners of a privately held corporation may not want to admit minority shareholders.

On the other hand, where a publicly traded corporation is making the acquisition (so there is a ready market, and an established market value for the stock) or the selling shareholder will continue as a key employee of the acquirer (thus desiring an equity-stake in the venture), a reorganization may satisfy the parties' goals.

In addition, the credit risk is more complex than in a stock sale paid in part with a promissory note. The risk is that the enterprise will not succeed and that the stock received will not retain or increase in its value. In the case of a closely held company, there is also a lack of marketability and potential minority shareholder issues. Nevertheless, there are strategies to address these concerns. For example, a shareholders' agreement can create a market for the stock by requiring the corporation to buy out a shareholder's interest upon termination of employment, death, etc. (also important for an S corporation to avoid having ineligible shareholders), and by establishing the value of the stock (by a set formula, by process of appraisal, or by agreement to a set value).

PRACTICAL CONSIDERATIONS

In any transaction, regardless of motivation or structure, there are a number of practical issues and problems that must be addressed. Among the most crucial and sensitive are: pricing, staffing, due diligence, and transition. Circumstances are always dynamic and decisions on one issue often affect others.

PRICE AND PAYMENT TERMS

Pricing is totally dependent on the circumstances and should not be agreed to until substantial financial due diligence is completed. Because the primary assets purchased are intangible, pricing is usually a function of revenue or profits, and typically involves a range of multiples. Higher multiples, though, may be subject to certain client retention, revenue, and profit levels being realized. Price need not be a function of revenue—it can be based on profits traced to the acquired business, and again, can have limits (*e.g.*, a set percentage over a set time, with or without an absolute limit). Even after the price is established, purchase price adjustments can be used to account for circumstances discovered during due diligence.

Proper pricing requires careful review of the seller's finances (highlighting the importance of a confidentiality agreement and carefully written letter of intent) as well as the buyer's plan for the acquired business (keep the existing staff and office space and honor the seller's fees or consolidate clients at a central location without hiring staff). Other issues relative to pricing include payment terms. For instance, a seller will often accept a lower price if paid in full at closing. Buyers may insist on spreading payments of a higher price over time, possibly with periodic adjustments based on performance. Other issues to consider include who receives continuing trail payments for investments and income derived from restatements and major amendments affecting all plans.

Payment term options must be considered carefully. Although payment in cash in full at closing will usually justify a lower price, this approach makes enforcing an indemnification claim harder since there are no payments to withhold. Typically, therefore, payment is in a combination of cash and note. Negotiation of a note involves many terms, including interest rate (whether fixed or variable), events of default, grace periods, remedies, and collateral. Typical collateral includes a stock pledge (in a stock sale), a security interest in the buyer's assets, and personal guarantees—again, all negotiated. Depending on the bargaining strength of the parties, collateral arrangements can also include various restrictions on the buyer's conduct, for instance, limiting the amount of debt it may incur, capital expenditures, and compensation paid to owners. In all events, these are individually negotiated and carefully documented.

STAFFING

Buyers need to consider carefully whether existing staff is sufficient to provide attentive service to the acquired clients. A buyer also needs to give much attention to understanding how best to preserve client relationships—value lies in intact, strong relationships. Thus, if a buyer needs more staff to support the new clients, hiring the seller's employees has many obvious advantages—the buyer obtains institutional knowledge about clients, their expectations, and how the plans were administered, and client-consultant relationships are preserved. As a result, the transition as a whole is less disruptive to clients and other advisors. An added advantage is that it can greatly speed up and ease the transition, thus reducing the cost, increasing client retention, and increasing the long-term value of the acquired business. On the other hand, new employees must be compatible with existing culture and be trained on new systems and procedures. A buyer intending to hire a seller's employees should still use standard hiring practices (*i.e.,* interview each person and check references). Even if the additional staff is not needed, a buyer should consider whether to hire (as an employee or contractor) the seller's principal and/or key employees to facilitate the transition, progressively transfer knowledge, and help integrate staff.

If the buyer wants to hire the seller's employees, he or she should carefully review applicable employment agreements and consider whether to assume them, or instead, have the seller terminate the agreements and establish new terms and conditions of employment. Consideration should be given in this situation as to whether, under applicable state law, the buyer could enforce restrictive covenants (*e.g.,* non-compete provisions, if the agreements are assumed).[5] Similarly, the seller's owners should be required to sign confidentiality, non-solicitation, and non-competition agreements, whether or not they are hired. Such agreements should tie-in with payment terms so that a buyer can suspend payments upon breach, and for this reason it will often be appropriate, even in an asset sale, to allocate a portion of the total consideration to the restrictive covenants.

The importance of all of these staffing issues cannot be understated. As a service business, a pension consulting practice's true assets are the people, their professional and technical skills, and relationships built up over time. A buyer may spend a great deal of time, effort, and money transitioning clients, only to face high levels of client turnover as clients find and follow their trusted consultant (often a non-competition covenant will not prevent a consultant from accepting a client where the client initiates contact). Further, inadequate staff leaves new clients disgruntled and more prone to seek services elsewhere. Thus, staffing is one of the most important issues to address early on in a transaction.

TRANSITION

The transition of business can make or break a transaction. In an asset sale, the parties have to decide who will complete work in progress (*e.g.,* testing and annual administration). Typically, there will be a date on which the seller stops all new work and has until closing to complete work in progress. Other work a seller may retain may include completing pending plan terminations and mergers and plan document restatements/amendments. Where the seller is shutting down, arrangements should be made for following up on completed work and finishing retained work.

Transition of such financial matters as billing also need careful planning, especially if billing cycles differ. The parties need to decide when the buyer will start billing in its name, and in this regard, the buyer needs to decide if it will continue to abide by the seller's fee schedules and billing cycle or change all clients to its schedules/cycle. (Typically, this financial transition is done over time.) Also, decisions must be made regarding billing and payment for any work the seller completed as of closing and any post-closing work the seller will finish. Assuming the seller keeps its receivables, the seller should consider and discuss with the buyer how the seller intends to collect these receivables and whether the collection activities will be disruptive.

Finally, the timing of the announcement to clients needs careful thought. The proper timing depends on the structure of the deal—a stock deal or reorganization is less disruptive, so clients may tolerate less advance notice. Similarly, in an asset sale where the buyer is hiring seller's employees, advance notice may be less important. Also, a seller may want shorter notice to reduce the chance that business will move simply due to the announcement. Typically, the announcement is handled through a joint mailing coupled with telephone calls.

DUE DILIGENCE

Due diligence is the term used to broadly encompass a review of the seller's assets, finances, and operations. In a reorganization, due diligence will be two-way. In a simple asset sale, due diligence will focus on the assets being sold. For example, a third party administrator acquiring an administration business should review at least a wide sampling of the administration files, plan documents, and computer records relating to the client; interview the responsible consultant; and investigate the fee structure, billing cycle, revenue, and profitability. Due diligence becomes more involved where a buyer will be assuming leases (such as for office space),

licenses, and contracts. In these circumstances, all relevant documents and laws need to be reviewed to determine if they can be assigned (in an asset sale) or will be affected by a change in ownership. In a stock sale or reorganization, due diligence will include a review of tax returns and corporate records, including bylaws, shareholder agreements, minutes, and corporate standing (compliance with state corporate filing requirements), and will be two-way (*i.e.*, the seller will also conduct due diligence on the buyer.) Employment-related due diligence in stock sales and reorganizations should also include a review of the seller's benefits and compensation arrangements, as a result of which decisions will be made as to whether or not to retain them. (It may be simplest to terminate all benefit plans before closing, but a buyer may want to continue existing employment contracts.) The seller should be required to obtain all third-party consents. In large transactions, often consultants/accountants conduct the due diligence. Nonetheless, given the many legal issues involved and the potential impact on the overall deal, counsel should be closely involved as well, particularly where contractual and other legal issues are involved.

Often due diligence reveals liabilities of which the seller was unaware (or hoped the buyer would not discover). These liabilities may not be so severe as to cause the buyer to abandon the transaction, so the parties may need strategies for managing these items in practical and financial terms. Some approaches include:

(1) requiring corrective action before the closing;

(2) holding sale proceeds in escrow as a reserve against certain types of claims;

(3) including specific indemnification/hold harmless provisions in the agreement of sale; and/or

(4) requiring seller to obtain tail insurance to cover these liabilities.

A BRIEF MENTION OF JOINT VENTURES

Because of the many complexities of a transaction, parties may decide to conduct a joint venture as an interim step on the path to a merger or reorganization, allowing the parties to become comfortable with each other, test assumed synergies and efficiencies, and develop joint operational procedures. Careful planning of who will manage the joint venture, who will govern the joint venture and how, what responsibilities the parties have, and how the joint venture may be unwound are issues of paramount importance. Without fully discussing these issues and carefully documenting the agreements, inefficiency and disputes will be inevitable.

REALITY CHECK

This article addresses many issues that arise in most transactions and suggests a variety of strategies for

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The following webcast recordings are currently available:

QDRO Administration
Linda R. Morra
Available until November 30, 2004

IRS/ASPA 401(k) Update
Lisa Mojiri-Azad
Janice M. Wegesin, CPC, QPA
Available until October 31, 2004

Deemed IRAs
Charles J. Klose, FSPA, CPC
Available until August 30, 2004

IRS Voluntary Correction—Easier, More Flexible, AND Lower Fees
James C. Paul, APM
Joyce Kahn
Available until July 30, 2004

How Much is That Required Minimum This Year?
Richard Hochman, APM
Available until July 30, 2004

401(k) Fiduciary Issues and Opportunities for Financial Consultants
Fred Reish, APM
Available until June 30, 2004

2002 Form 5500 and Related Compliance Issues
Valeri L. Stevens, APM
Available until April 30, 2004

IRS/ASPA Washington Update
Brian H. Graff, Esq., *et al.*
Available until March 31, 2004

Participant Loans
Jane E. Armstrong
Available until March 31, 2004

Cost: $125 for Members, $225 for Non-members

addressing them. Every deal is different and has its own dynamic depending on objective and subjective factors, from finances to personalities. The degree of formality, the extent of due diligence, and the amount of detail included in the documentation will vary depending on these dynamics. A transfer of administration clients between firms well known to each other may proceed based on a simple letter describing price, timing, and identifying clients. By necessity, a reorganization entails more complex documentation and due diligence. The formality also depends on the relationship between the parties—two local firms may combine based on a short agreement given the knowledge and trust they have in each other. Transactions with large institutions will be much more formal. All of the issues discussed above should be considered, even in a small deal, and understandings reached, otherwise expectations are sure to be frustrated. Experienced counsel is sensitive to these dynamics and can provide advice and guidance, anticipate issues, offer pragmatic solutions, and effectively document the deal so that the business can move forward with a clear plan of action.

CONCLUSION

It is likely that, as more baby-boomer business owners retire, the pension service industry will go through additional consolidation. Developing the most efficient transaction and shepherding it to a successful conclusion is a highly fluid process requiring technical knowledge and practical experience. Owners should spend time carefully considering their goals in pursuing a transaction and thinking through the many practical issues involved. With careful analysis, time spent on planning and implementation, and a measure of luck, transactions can succeed and the difficulties recede into memory. ▲

Footnotes

[1] Of course, if the seller is shutting down, clients may be left without recourse, leading clients to look toward the buyer. Also, if the buyer employs the seller's employees, clients may not appreciate the distinction between seller and buyer. Thus, a buyer may agree to assume some or certain types of liabilities of the buyer. If so, this should be taken into account in pricing the deal, through a purchase price adjustment (perhaps if the buyer's costs of correction exceed a specified threshold), and/or through indemnification (coupled with a purchase price escrow and/or tail insurance).

[2] Although the term "stock" is used in this discussion, it would be more accurate to refer to "equity" sales, to encompass ownership of non-corporate entities, such as limited liability companies.

[3] It is also possible that aspects of an entity's legal infrastructure may not be conveyed despite the sale being a de facto assignment of the entity's ownership (e.g., certain licenses). Again, careful review of applicable contracts, licenses, and regulations is essential.

[4] Optimal tax treatment and maximum diversification can be achieved through a "Section 1042 exchange," in which a C corporation shareholder sells at least 30% of the outstanding stock to a leveraged ESOP, and reinvests the proceeds tax-free. A full discussion of Section 1042 exchanges is beyond the scope of this article but should be considered where an owner is looking for a tax-advantaged exit strategy.

[5] Another concern is the issue of enforcing restrictive covenants if the buyer does not hire the employee.

Elliot D. Raff, APM, is an attorney with Flaster/Greenberg PC, a business and commercial law firm in Cherry Hill, NJ. Elliot is a member of the firm's Employee Benefits and Tax and Business Law Practice Groups. His practice focuses on advising plan sponsors and benefit consultants in the design, implementation, and ongoing administration of qualified, non-qualified, and welfare plans. Elliot has represented businesses, including pension administration firms, and their owners, in connection with business acquisitions and sales.
Note: Elliot would like to thank his colleague, Allen P. Fineberg, APM, also of Flaster/Greenberg PC, for his assistance in the preparation of this article.

ASPA Benefits Councils Calendar of Events

Date	Location	Event	Speakers
March 29	Delaware Valley	DB/DC Combinations, Including 401(k) Plans	Joan A. Gucciardi, MSPA, CPC
April 21	Central Florida	TBD	Richard A. Hochman, APM
April 27	Delaware Valley	Financial Issues in Defined Benefit and Defined Contribution Plans	Clark Frese, CPC, Mitch Welsch
May 24 & 25	Delaware Valley	IRS Seminar	TBD
June	Delaware Valley	Turning Administrative Headaches into Consulting Opportunities	Linda Loretti, Steve H. Rosen, MSPA, CPC
September 9	Delaware Valley	Topic TBD	Sal L. Tripodi, APM

ASPA Benefits Council of the Great Northwest

Update from Our Newest Council!

by Gregory R. Rund

It was a cold and rainy night when the most northernly of the lower 48 finally established a Seattle-based ASPA Benefits Council (ABC) in the Great Pacific Northwest. We had the benefit of a number of early entrants in the ERISA sweepstakes (for instance, the home offices for Milliman & Robertson, Howard Johnson Company, Safeco Insurance, and G. Russell Knobel & Associates). The Howard Johnson Company (an early winner) and Safeco (of more recent notoriety) were both significant supporters of ASPA continuing education in the 1970s and 1980s, spawning many early CPCs into the murky ERISA waters. We have a proportionately large number of sophisticated, competent plan administration firms in the Pacific Northwest and competition is fierce during our extended courting season. Unfortunately, we're so far removed from everywhere, and a local need for very competent continuing education opportunities was emerging. It was incumbent on the gamest members of this complex species to bring unity among the Silvers, Sockeyes, Chinooks, and the most "knobel" Kings. Drawing members from Oregon, Washington, Alaska, Idaho, and Montana, the ABC of the Great Northwest emerged!

Actually, we were very fortunate to have Sal Tripodi, APM, as our inaugural speaker for an all-day ERISA seminar in September 2003, which was sold out.

We provide confirmation of attendance to ASPA and other professional associations at our seminars. We have an excellent group of individuals on our Board. One of our Board members, Colin Southcote-Want, MSPA, will be conducting roundtable reviews of the actuarial exams, and is looking for other individuals who are interested in acquiring speaker credits for participating in our actuarial events. Another very active Board member (and our Treasurer), Jim Huffine, is bringing Derrin Watson, APM, in the spring for a half-day session. Betsy Vincenti, QKA, is available to help individuals form study groups for the ASPA exams. Jeff Roberts, CPC, one of our most active Board members, is our Membership Chair, and is planning a session on non-qualified plans. Our fledgling organization has not embarked on regular meetings; however, our membership is over 60 members. As our membership grows, I'm sure we'll spawn more activities.

Brian Graff, Esq., Executive Director of ASPA, has agreed to visit the Great Pacific Northwest to participate in a future chapter meeting. We promise we won't be too hard on him, but we will ply him with some Great Northwest games (as we do all of our speakers). We really appreciate all the support we received from the folks at the ASPA national office and from ASPA's Board of Directors during our unique courtship with ASPA. We look forward to making a very positive contribution to providing continuing education opportunities in the Pacific Northwest and to the continuation of the efforts of ASPA.

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Gregory R. Rund is chairman of the ABC of the Great Northwest and has been a member of ASPA since 1982. Greg founded G. Russell Knobel & Associates in 1976 and has been a member of the Western Pension & Benefits Conference since 1971. He was an armored cavalry officer from 1968 to 1970 and is a graduate of Seattle University (1968). Currently, he sits on the boards of the American Liver Foundation and the Arthritis Foundation. He was formerly active with Big Brothers.

Lone Star Council Shines Deep in the Heart of Texas

by Richard A. Shulman, MSPA

NOW IS A GOOD TIME, AS 2003 HAS COME TO A CLOSE, FOR THE ASPA BENEFITS COUNCIL (ABC) OF THE TEXAS GULF COAST, "*THE LONE STAR COUNCIL,*" TO REFLECT ON OUR GROWTH, OUR SUCCESSES, THE EVENTS OF THE PAST YEAR, AND OUR PLANS FOR 2004.

We realized early on that in order to succeed and be responsive to the nearly 1,000 members of the benefits community in the Southeast Texas region, we'd have to develop the ability to effectively communicate with the people we aim to serve. Thanks go to our Membership and Communications Chairperson, Marilyn Doolittle, CPC, QPA, for taking on this challenge with the passion that makes her a driving force on our Council. Spearheading a project to develop a database of interested professionals in the area, Marilyn and her group compiled and now maintain an e-mail database of nearly 500 records that is used to interact with the community regarding our activities. The result is that 123 people have joined our ABC as active members and attendance at Lone Star Council functions this past year has been well in excess of 300 people.

Speaking of activities, we began 2003 with a dynamic presentation from Adrien LaBombarde on the provisions of the Sarbanes-Oxley Act. Adrien's talk was so timely and so well received that we wondered how we were going to maintain the enthusiasm. The answer was Derrin Watson, APM, "The Impresario of Aggregation," whose unique blend of humor and basso profundo song stylings made the important and very complex topic of controlled groups, affiliated service groups, etc., somewhat less mysterious and surprisingly more interesting.

We kicked things up a notch in the summer when Rajean Bosier, CPC, QPA, QKA, shared her boundless enthusiasm and unraveled the complexities of the new catch-up contribution rules and other 401(k) issues. The overwhelming response to Rajean's energetic presentation can best be described by quoting the comment on the Program Evaluation Form of one of the attendees who said, "*Rajean Rocks!*"

The formal portion of our year ended on a high note when Brian Graff, Esq., Executive Director of ASPA, joined us to share his unique perspective and insight into what's happening on Capitol Hill. We were introduced to the Three Sisters of Savings, the Bush Administration's questionable answer to the retirement savings dilemma. We also heard the news, some good and some not so good, about key issues that impact the areas in which we practice. Those members of the audience who were newcomers to our ABC, and to ASPA in general, were understandably impressed by Brian's instinctive grasp of the situation in Washington, his first-hand knowledge of the mood on Capitol Hill, and his practical vision of the prospects for change in the foreseeable future.

Because of the quality of the programs we present, our Council members, along with other local professionals who regularly attend our events, have come to expect great things from us. The success of our Council is primarily due to the people who work so tirelessly and selflessly to ensure that success. The Lone Star Council is extremely fortunate to have Sadie Gensler-Hooker, QPA, QKA, as our Program Chairperson. Sadie has set the bar high for 2004 and has already begun the work of putting together a series of top-notch programs for our members and program participants. We also must thank Asya Karpinos, QPA, who carries the title of CE Coordinator but is also a key player on our Membership Committee. Through her business contacts as well as her own hard work, Asya was able to help supply us with custom designed Lone Star Council logo golf shirts that we look forward to presenting to our members in 2004.

Since our Council was formed nearly three years ago, we have come to depend on Mike Brasher, QPA, to keep tabs on our finances as our Treasurer,

to make sure we follow all the rules, and to offer his sound advice on how we can make the best use of our resources. Mike has been a key player on our Board and we forced him to extend his normal two-year term as Treasurer until we could find a worthy successor. We're proud to announce that effective January 1, 2004, Dennis Fox, QKA, will assume the post of Council Treasurer. We all look forward to working with Dennis. Mike will continue to serve on our Board and his talents and enthusiasm will continue to be put to good use.

Our Council is also indebted to many other volunteers who dedicated the time needed to make it all work. Among these are Dianne Loomis, CPC, QPA; Tina Leonard, QPA, QKA; Jim Chapman; Lilia Pivetta; Malcolm Thompson; and Stephen Mason.

We're deeply committed to enhancing the value of membership in our ABC in the future. We hope to organize specialized technical seminars led by local professionals in addition to our general program events in 2004. We will also try to make use of our communication capabilities to identify and bring together people interested in forming local study groups.

We welcome suggestions, comments, and inquiries from anyone interested in becoming a part of the Lone Star Council.

Contact us at **ASPAHouston@yahoo.com**.

Richard A. Shulman, MSPA, is an enrolled actuary and consultant with Malcolm Thompson and Associates, Inc. Consulting Actuaries in Houston, TX. Richard currently serves as president of the ASPA Benefits Council (ABC) of the Texas Gulf Coast. He is also a member of the American Academy of Actuaries and has over 30 years of consulting actuarial experience in the design and administration of qualified plans.

WELCOME NEW MEMBERS!

MSPA

Matthew W. Carlton
Jeffrey C. Liter
Teena M. Sarkissian
Mark A. Vidal

QPA

Linda S. Bair
Thad R. Coward
James F. Harrigan
Patricia A. Hellenbrand
Laura J. Houston
Matthew J. Krywicki
Mitchell A. Kurtz
Daniel G. Mazzola
Steven Rabinaw
Eric C. Wallace
Bradley W. Whitley

QKA

Tracy T. Andrews
Linda Bailey
Gary R. Charles
Nancy J. Clark-Smith
Cecily A. Crook
Marlene M. Debrosse
Racquel N. Dirden
Gregory Gounaris
Marie Herron
Tami L. Ireland
Sharon Kangeter
April M. Kilpatrick
Connie H. Kolodziej
Sharon E. LaMarca
Carolyn F. Lovell
Colleen R. Manuel
Debra J. Moran
Desmond S. Mularski
Kim A. Newton
Kevin L. Perry
Linda L. Sewak
Cynthia L. Small
Marianne E. Snow
Ronald H. Ulrich

APM

John A. Ficarrotta
Steven Fraidstern
Joel J. Phillippi

Affiliate

J. David Batchelor
Michelle D. Boltik
Le Ann A. Budeski
Natale J. Coraci
Carol L. Drake
Dwight G. Edwards
Jacob R. Iverson
George J. Kasper
Diana Love
Brenda May
Bijan Mohseni
Daniel Molloy
Jay J. Sims
Joyce Slattery

Letter from the President

by Bruce L. Ashton, APM

Dear Fellow Members:

A little over three years ago, during George Taylor's term as President, the Board of Directors began a review of the ASPA Strategic Plan. The object was to determine where the organization was going over the next 10–30 years and to provide some direction as to how we'd get there.

I am pleased and proud to tell you that—building on the hard work of the Directors who've served over the past three years, the leadership of George Taylor, MSPA; Craig Hoffman, APM, President in 2001–2002; and Scott Miller, FSPA, CPC, President in 2002–2003, and with the invaluable assistance of Brian Graff, Esq., Executive Director, and Jane Grimm, Managing Director—this year's Board has adopted a new Strategic Plan and identified six major goals that will carry ASPA through the rest of this decade. A copy of the new Plan and goals follow this article and appear on the ASPA Web site at www.aspa.org. I am especially excited about the core values we've adopted as an organization, because I think they reflect what's best about our members and what they bring to our profession.

When you look at the Plan, you'll realize that the Board has set audacious, far-reaching—and some might say unrealistic—goals for your Society. To the nay-sayers, I only ask that you look at what we've already accomplished:

- We've grown to over 5,250 members.
- We have, thanks to Brian Graff, Esq., and our hard-working Government Affairs Committee, an important and recognized voice on legislation and regulations affecting our industry. We don't always get what we want, but at least our voice is heard at the highest levels of government. And we have, in fact, achieved some remarkable successes.
- Our E&E program serves more than 8,000 students annually, and our eight conferences and numerous webcasts provide continuing education and information on new developments for more than 5,000 others.
- Through its members and programs, ASPA touches over 10,000 pension professionals who work on nearly half the plans in the country. Put another way, our members and others with whom we come into contact—you, in other words—help provide meaningful retirement benefits to nearly 50% of the workers in America.

So, to the nay-sayers, I say, look at what we've already done.

That's not to say this will be easy. Nothing worth doing is. There will be challenges, hurdles, and, I suspect, setbacks. But with our new Strategic Plan and the goals we've set for ourselves, with the strength of our existing programs, with the vision of our current and future leadership, and the dedication of our hundreds of volunteers and thousands of members, there's no telling what we'll accomplish next. Stay tuned—it's going to be fun.

Feel free to call or e-mail me if you have questions or would like to get more involved.

Bruce L. Ashton, APM, is a partner with Reisch Luftman Reicher & Cohen. His practice focuses on all aspects of employee benefits issues, including representing plans and their sponsers before the IRS and DOL's EBSA. He has served on ASPA's Board of Directors and as Co–Chair of ASPA's Government Affairs Committee. He currently serves on the Executive Committee as ASPA's President.

E&E Seeks Technical Education Consultant

ASPA's Education and Examination (E&E) Committee is in search of pension professionals interested in working part time on writing and editing study guides.

If interested, please respond to the RFP posted on the Members Only section of our Web site: **www.aspa.org**.

ASPA

CORE IDEOLOGY

CORE PURPOSE

To educate all retirement plan professionals and preserve and enhance the employer-based retirement system

CORE VALUES

Mutual Respect
among retirement plan professionals

Integrity
ethical conduct; accountability; fostering compliance

Strategic Thinking
fostering innovation and creativity; looking toward the future; advocating changes needed to reach goals

Responsiveness
when change occurs, taking initiative to help make it work

Courage
taking the high road and doing what is right for the system and participants

Dedication
committed to dignified retirement for individuals; committed to professionalism in the system; striving for excellence

FUNDAMENTAL POLICY STATEMENTS

- The employer-based retirement system is an essential part of a national retirement income policy
- All employers, regardless of size, should have equal and fair access to the retirement system
- Flexibility is important in the design of retirement programs
- We are committed to the role of professionals in employer-based retirement programs
- Education is fundamental to professionalism

ENVISIONED FUTURE

ASPA is the premier educator of all retirement plan professionals and the preeminent voice and advocate for the employer-based retirement system. Retirement plan professionals view ASPA membership as essential to their success.

VIVID DESCRIPTION

THE RETIREMENT SYSTEM

- The percentage of Americans covered by the employer-based retirement system is substantially increased.
- All employers, regardless of size, perceive employer-based retirement plans as essential to doing business.
- Flexibility exists in retirement plan design to address the individualized needs of employers.
- The government provides meaningful oversight of all employer-based retirement plans.

ASPA

- ASPA is the visionary shaping the future of the employer-based retirement system.
- ASPA is the preeminent voice and resource on retirement plan policy.
- ASPA sets the standard for professionalism in the retirement plan industry.
- ASPA is respected for its capacity to adapt to changes in the retirement plan industry and government policy.
- Organizations in related fields view ASPA as the preeminent organization for retirement plan professionals.
- The public views ASPA as the preeminent organization for retirement plan professionals.
- ASPA is recognized by national media as a preeminent resource on retirement policy and the retirement plan industry.

ASPA MEMBERSHIP

- Membership in ASPA is considered an essential part of being a retirement plan professional.
- The public recognizes the value of and seeks the expertise of credentialed ASPA members.
- Plan sponsors and their advisors seek credentialed ASPA members to help them develop and maintain retirement plans.
- Retirement plan service providers seek credentialed ASPA members as employees.
- Universities and other educational institutions incorporate ASPA accreditation programs into their curriculum.
- The government recognizes credentialed ASPA members for their expertise on retirement plans (*e.g.,* power of attorney, DC certification).

AMBASSADOR OUTREACH PROGRAM

Thanks to all of the ASPA members and industry employers who participated in our new Ambassador Outreach program. This new member recruitment program enlists the assistance of ASPA members in spreading the word about the benefits of ASPA membership. ASPA members attending ASPA's Summer and Annual conferences are contacted and asked to assist in member enrollment campaigns during the conferences. It is a great opportunity to meet and network with your colleagues and build a stronger organization at the same time.

Michael Callahan, FSPA, CPC
Amy Cavanaugh, CPC, QPA, QKA
James Christenson
Kim Cochrane, QPA
Jim Comer, APM
Judi Cox
Dick Curtin
Terry Dunger, APM
Kathy Eggiman
Bart Flemming
Manny Garcia
Ginny Grimble
Susan Hajek, QKA
Patricia Hargrove, CPC, QPA
Dianne Hart, APM
Mark Heller, CPC, QPA
Richard Hochman, APM
Sadie Hooker
Richard Jolley, MSPA
Stephanie Katz, CPC, QPA
Diane Kelley, QPA
Norman Kerner
Chuck Klose, FSPA, CPC
Jim Kreder, CPC
Theresa Leiker, CPC, QPA
Larry McClung, QPA, QKA
Jo Ann Massanova, CPC
Linda McClure, QPA
Ronica McGovern, QKA
JJ McKinney, QPA, QKA
Michelle Parks
Paul Polapink, MSPA
Adam Pozek
Mike Preston, MSPA
David Pursifull
Toni Ramos, QPA, QKA
Adrienne Robertson, CPC, QPA
Leslie Schafer, QPA
Sharon Severson, CPC, QPA
Kathy Silva
Timothy Slavin
Rose Smith
Larry Starr, CPC
Donald Whitmire

Congratulations to Terry Dunger, APM, ASPA's top new member recruiter for 2003!

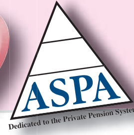
For his recruitment efforts, Terry has earned a free ASPA conference registration for any 2004 ASPA conference.

Great work Terry!

Become an ASPA Outreach Ambassador and help spread the word about the many benefits of ASPA membership. Please contact the Membership Department at (703) 516-9300 for information.

FUN-da-MENTALs

Roses are red,
Violets are blue.
Pensions are sexy
And so are you.



2 young-looking
2 be eligible
4 catch-up contributions

"Talk about disposable income!"

Contest Winners!

Last issue, we held a contest asking readers to take any word from the dictionary, alter it by adding, subtracting, or changing only one letter, and supply a new definition. Here are the winning entries, along with a few others that deserve honorable mention:

First Place:

Henry Riger

Ragulations: *IRS-published interpretation and guidance that are as clear as Bolognese sauce.*

Second Place:

Eileen Whitmore

Safe Arbor: *Where to go for a drink after completing year-end testing.*

Honorable Mentions:

Kathy Malo

Defiled Benefit: *Cash balance plan.*

Rhonda Corbitt

Gactuary: *An actuary who is a member of the Government Affairs Committee.*

Pactuary: *An actuary who is a member of the Political Action Committee.*

Word Scramble

Unscramble these four puzzles—one letter to each space—to reveal four pension-related words. Answers will be posted on ASPA's Web site at **https://router.aspa.org**. Once you have logged in, place your cursor over the Membership tab in the navigation dropdown menu. Move to Membership Benefits, then click on *The ASPA Journal*. The answers are located near the bottom of the page.

BONUS: Arrange the circled letters to form the Mystery Answer as suggested by the cartoon.

RAG TREE ❍ _ ❍ _ ❍ _ _

WISH PAW ❍ _ _ _ ❍ ❍ _

HYMN LOT _ _ _ ❍ _ _ ❍

TEE SAT ❍ _ ❍ ❍ _ _

Mystery Answer

He passed the "_ _ _ _ _ _ _ _ _ _ _ _."

Why the guard let the plan sponsor proceed

Bulletin Board

Education

April 30, 2004
Final Registration Deadline for Spring Examinations

Conferences

April 29–30, 2004
IRS/ASPA Great Lakes Employee Benefits Conference
Chicago, IL

May 24–25, 2004
Mid-Atlantic Benefits Conference
Philadelphia, PA

Membership

Renew Your ASPA Membership before February 27 to avoid late fees!

ASPA's newly restructured education program:

The More Things Change…

After two years of research, analysis, and planning, ASPA's Education Program has been newly restructured. Now, study material will be presented in smaller segments, in a more logical, easier-to-understand way.

The More They Stay the Same.

ASPA's newly restructured education program debuts January 1, 2004. But the same high educational standards for which ASPA is known won't change.

PA-1: An introduction to qualified retirement plans and pension plan administration practices, with a focus on the annual administrative cycle

PA-2: An introduction to qualified retirement plans and pension plan administration practices, with a focus on event processing

PA-3: Daily Valuation terminology, concepts, and procedures

DC-1: Defined Contribution Basic Concepts

DC-2: Defined Contribution Compliance Issues

DC-3: Defined Contribution Advanced Topics

REGISTER NOW!

PA-1, PA-2, PA-3 take-home exams:
Available any time beginning January 1, 2004

DC-1, DC-2, DC-3 computerized exams:
Offered in May, August, and November

For questions, contact ASPA at:
(703) 516-9300
or email: educaspa@aspa.org
www.aspa.org/edu

Calendar of Events

2004 — ASPA CE

Date	Event	ASPA CE
Mar 31	Early Registration Deadline for Spring Examinations	
Apr 29-30	IRS/ASPA Great Lakes Employee Benefits Conference Chicago, IL	15
Apr 30	Final Registration Deadline for Spring Examinations	
May 1-31	DC-1, DC-2, and DB Spring Examination Window	
May 14	Postponement Deadline for Spring Examinations	
May 19	C-3 Examinations	
May 20	C-4 Examinations	
May 24-25	Mid-Atlantic Benefits Conference Philadelphia, PA	16
Jun 1	Registration Available for EA Review Classes	
Jun 10-11	Northeast Area Employee Benefits Conference	8
Jun 30	Early Registration Deadline for Summer Examinations	
Jul 18-21	Summer Conference San Francisco, CA	20
Jul 31	Final Registration Deadline for Summer Examinations	
Oct 24-27	Annual Conference Washington DC	20

Did You Know?

Currently, ASPA's Education & Examination Committee is seeking applications for two positions. One position is for a Technical Education Consultant to edit study guides for the 2005 course schedule. The second position is a textbook author who will work with Sal Tripodi, APM, in designing a student edition of *The ERISA Outline Book*.

For additional information about these positions go to the home page of ASPA's Web site www.aspa.org, and go the "E&E Seeks Pension Professional" link or contact Jamie Pilot, Director of Education Services at jpilot@aspa.org.