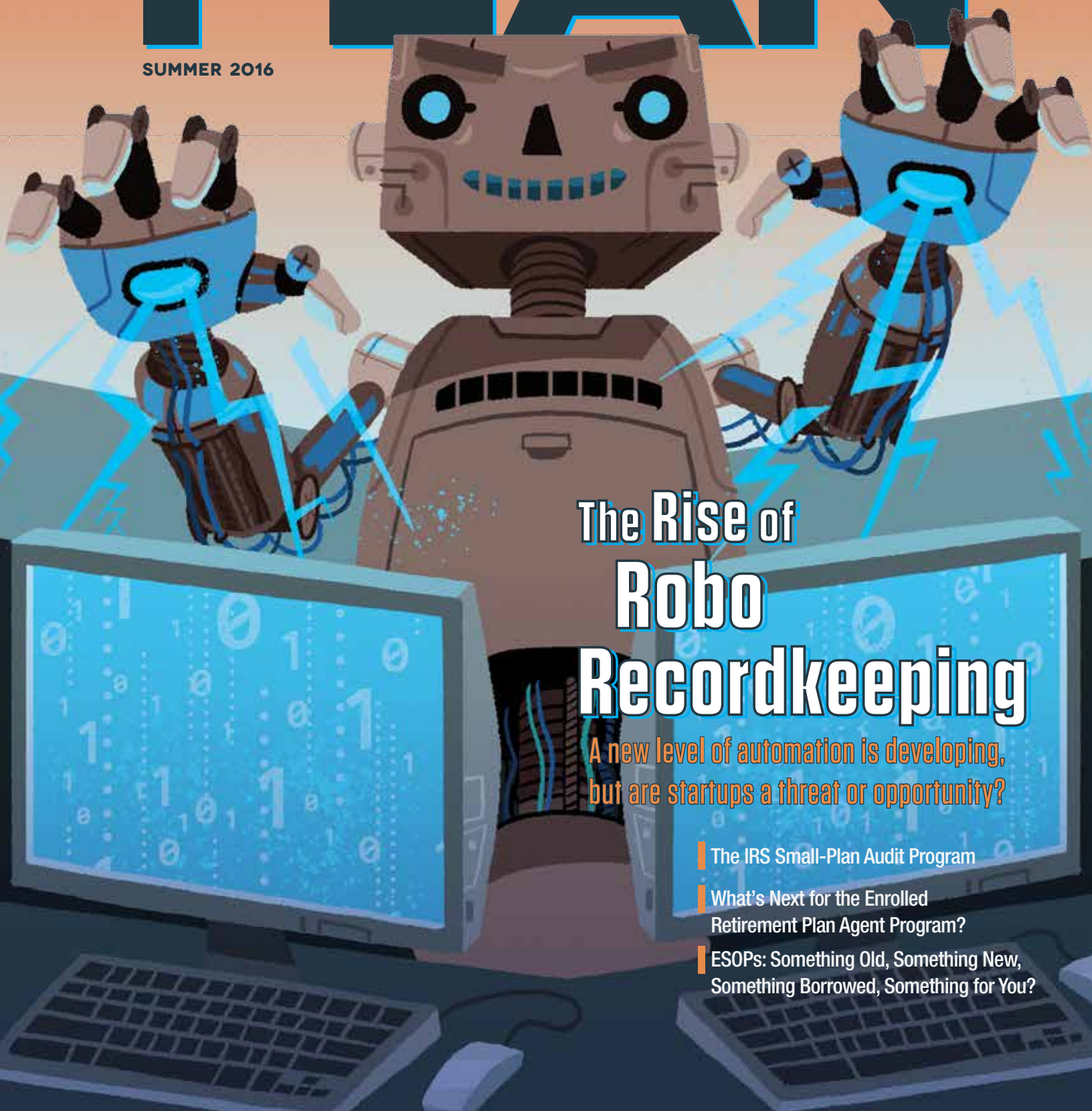


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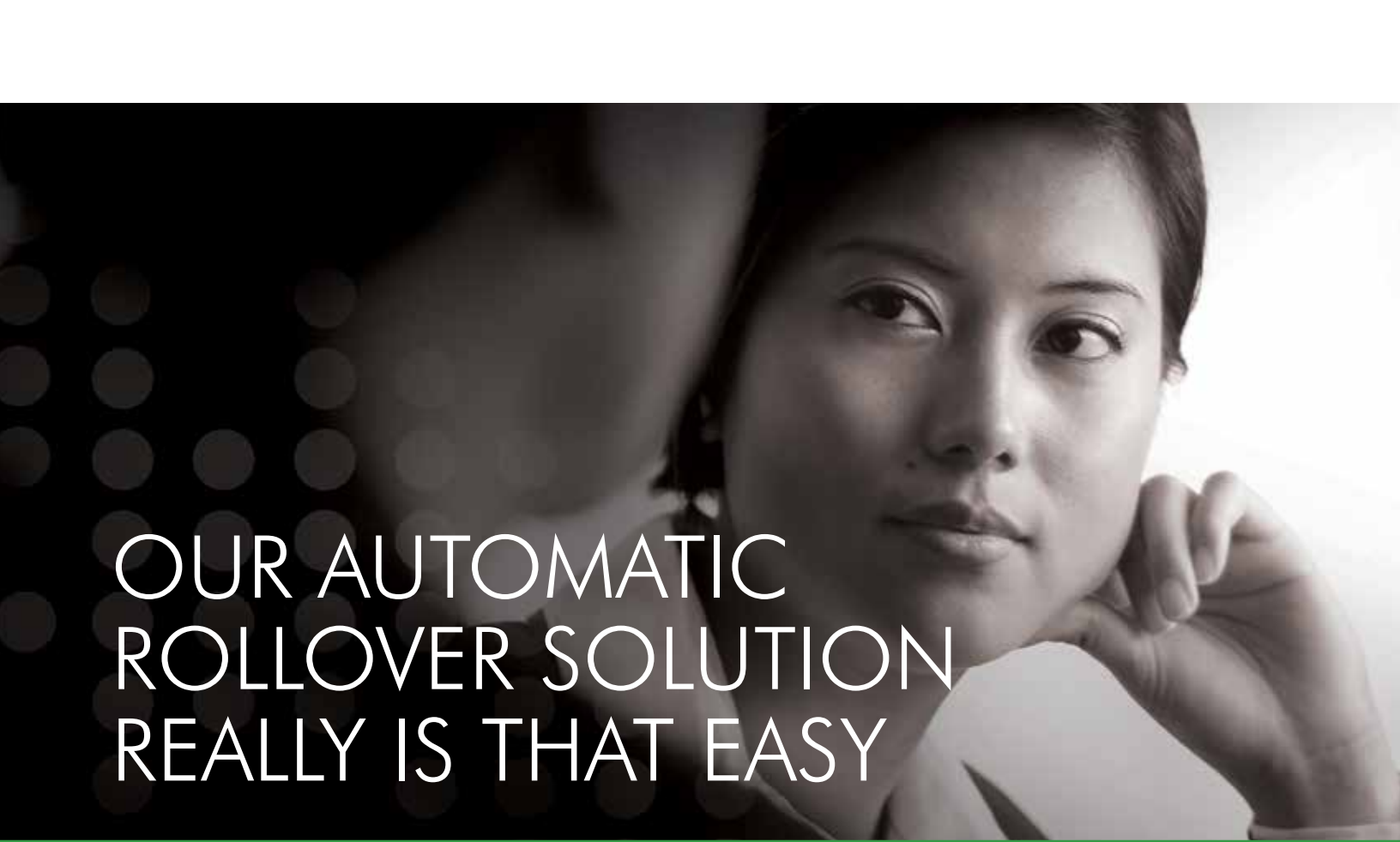
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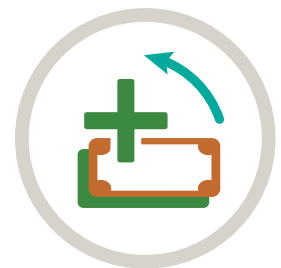
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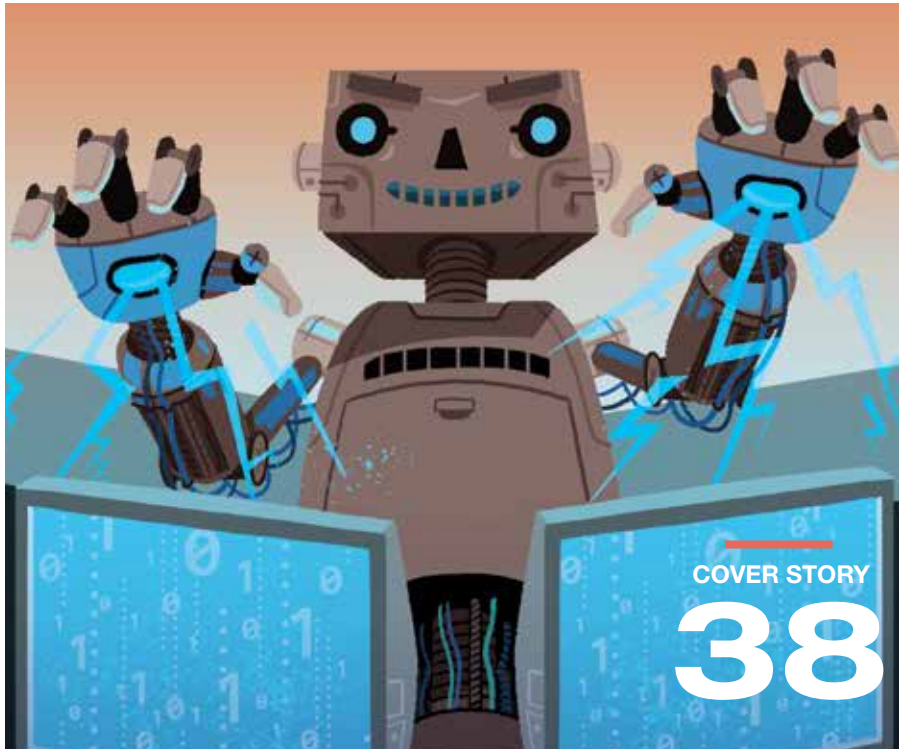


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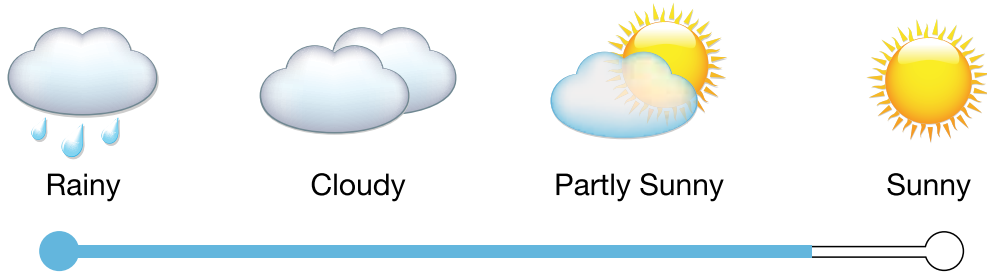
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Technopportunity

So here's my latest nomination for the three scariest words in today's retirement plan services space: "game-changing technology."

It makes me think of the travel agencies of yesteryear, whose close encounter with game-changing technology did most of them in. Or the typewriter repairmen, icehouses, and countless others before them for whom game-changing technology led pretty quickly to career-changing panic.

That's business. Or more accurately, progress. Because in every instance you could think of, the introduction of game-changing technology created new ways to

achieve a goal or serve a customer that were better, faster and easier. And in turn, that opened up new opportunities, new businesses, new clients, new careers, and new jobs.

The trick, of course, is to see that kind of change coming *before* it changes the game, and then make the right choices in embracing the parts of it that can boost your own pursuit of opportunity, wherever it may lie.

This issue of *Plan Consultant* includes a couple of must-read articles about the possible future impact of game-changing technology on you and your business, focusing on the opportunities that lie ahead. Our cover story, on page 38, explores the emergence of tech-based firms

seeking a foothold in the record keeping space. And in our Marketing column on page 58, David Witz outlines the unique opportunity now facing TPAs to take the lead in investing in tech-based solutions.

Here's a taste of what the cover story offers — a quote from The Wagner Group's Tom Clark: *You cannot automate out the expertise that an amazing, 30-year plan administrator on the TPA side brings to the table in understanding the nuances of how you meet the tax code and keep the IRS gods happy.*

And from the estimable Mr. Witz: *Developing new technology that will support the advisor's ability to stay focused on business development, client relationships and vendor management will give TPAs a shot at more opportunities to build their business valuation and achieve the success they covet.*

So if the mention of the term "game-changing technology" gives you a case of the yips, give both articles a read. They may change your perspective.

Comments, questions, bright ideas? Contact me at jortman@usaretirement.org. **PC**

JOHN ORTMAN
EDITOR-IN-CHIEF

ASPPA History Online

Have you visited the ASPPA history website yet? Designed to complement the ASPPA history book coming in October, the website includes material uncovered in the course of researching, writing and editing the book, including:

- **Photos** from ASPPA conferences going back to 1974.
- **Documents** from the ASPPA archives and other sources, including the 1966 certificate of incorporation, articles from *The Pension Actuary* by prominent leaders of the past, and more.
- **Videos**, including ones telling the histories of ASPPA's conferences program, Education and Examinations (E&E) program and advocacy efforts — all based on interviews with ASPPA Past Presidents and committee leaders.

We're adding photos, documents and new videos on a regular basis. When we do, we'll let you know in an *ASPPA Connect* post. Check it all out at <http://asppa50.org/>, or click on "ASPPA History" in the "About" section of ASPPA Net.

The following firms are certified* within the prestigious **ASPPA Service Provider Certification** program. They have been independently assessed to the ASPPA Standard of Practice. These firms demonstrate adherence to the industry's best practices, are committed to continuous improvement and are well-prepared to serve the needs of investment fiduciaries.

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BY JOSEPH A. NICHOLS



The ARA Wins!

It is the combined effort of the American Retirement Association sister organizations working together that allows our voice to be stronger and more influential than ever.

As chronicled throughout ASPPA's 50-year history, providing platforms for our voice to be heard has been essential to ASPPA's creation, survival and growth. The importance of our collective voice (and collective determination) was once again put into action a few months ago with our efforts to push back on what would have been devastating changes to the Section 410(b) non-discrimination rules. Through the leadership of our government affairs staff and volunteers, and because of our relationships with key members of the government (both elected and appointed), ASPPA's voice was heard, and changes that would have harmed qualified plan coverage was averted.

While ASPPA is still very well known in the halls of Congress and within the ranks of government agencies, it is the combined effort of the American Retirement Association working together that allows our voice to be stronger and more influential than ever. ASPPA and ACOPA have worked closely together for quite some time, but it is the new collaborations with NAPA and NTSA through ARA that helps broaden our reach and strengthen the relationships that protect our positions and the retirement security of millions of Americans.

Earlier this year, we began our second year of face-to-face ARA Board meetings. In our day-long meeting, we reviewed financials, shared achievements and concerns, and laid the groundwork for collective strategic planning.

Collaboration was the theme. It could have been very easy for each sister organization to approach each topic protecting their own turf. Instead, discussions centered around which organization was best positioned to lead a specific goal and how, by combining forces, the ARA strengthens its position as the leading voice protecting employer-sponsored retirement plans.

It has been a great year for our government affairs staff and volunteers. In addition to the Section 410(b) win, we finally got good news on safe harbor mid-year plan amendments (although work is still being done to make sure the guidance is workable) and successfully delayed poorly timed Form 5500 changes (more vigilance is needed here as well). We also helped NAPA in their fight to convince the DOL that if the fiduciary rule was to be a reality, certain changes were necessary to make the new fiduciary rule viable.

The majority of our success in helping the various government agencies craft qualified plan rules is the result of our incredibly talented and devoted GAC staff and volunteers. The history of ASPPA's success in forging relationships that get our phone calls answered and comment letters read is epic. However, sometimes common sense communications and hard work need a nudge. That nudge happens because of ASPPA PAC.

ASPPA PAC creates collaboration that is essential to our strength. In our latest victory, direct access to legislators was essential in making sure the detrimental language in the proposed 410(b) regulations was removed. As our industry grows, our membership

grows. That is great! Nonetheless, the complexities of new rules and attacks on what we feel is a system that greatly expands retirement coverage continue to grow. However, the ASPPA PAC has not grown at the same pace. We have a few very dedicated contributors, but our continued strength as an organization is dependent on a stronger collective group of PAC contributors.

As mentioned above, our PAC creates a nudge that is sometimes needed to get our message heard. However, we also need competent staff to deliver the message. Our entire government affairs staff is the best around. No one does it better than our own Judy Miller. To say ASPPA was fortunate to have Judy delivering our message is like saying we are fortunate the Earth has oxygen. I am lucky that I had the opportunity to work closely with someone so talented and devoted. I want to take this opportunity to tell Judy, "Thank you!" and to enjoy retirement.

So as we continue to celebrate our 50 years as an organization building this nation's retirement savings programs, let us also celebrate our wins and new relationships with our sister organizations — ACOPA, NAPA and NTSA. For the next 50 years and beyond, as part of the American Retirement Association, we will proudly be "Working for America's Retirement." **PC**

Joseph A. Nichols, MSPA, ASA, EA, MAAA, is ASPPA's 2016 President. A Senior Actuary with Cavanaugh Macdonald Consulting, LLC, he has provided pension actuarial services to a wide range plan sponsors for more than 25 years.

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The Judy Miller Story

Retirement happens.



BY BRIAN H. GRAFF

Judy Miller, the Director of Retirement Policy at the American Retirement Association, is going to retire at the end of August. Yes, retirement happens. And frankly, it's a good thing that the Director of Retirement Policy at the American Retirement Association is prepared to retire, because if she weren't, it would certainly not bode well for the rest of us.

That said, it's an enormous loss for this organization and the retirement industry overall. Judy's contributions to retirement policy since coming to Washington have been significant. Even more impressive, she garnered the equal respect of both Democrats and Republicans, having testified on behalf of both parties on retirement issues. Rep. John Boehner, the former Republican Speaker of the House, said of Judy that the Pension Protection Act of 2006 would not have happened without her. Judy was a Senate Finance Committee staffer for the Democrats at the time. In this era of partisan politics, her ability to cross the political divide was a rare skill and one she employed deftly. It's a credit to her notable policy acumen, but even more so her remarkable skills as an advocate. Judy was seen in Washington not as a lobbyist but as a trusted counselor. Not bad for an actuary.

As much as we may not like it, at the American Retirement Association we do have to let people retire. But before Judy goes, you should hear the story of how she got to Washington, DC. It's a good story.

In 2003, I got a call from Russ Sullivan, the Chief Tax Counsel for the Senate Finance Committee Democratic Staff. Russ was a friend, and we worked together for Congress in the mid-1990s. He told me that due to the increased focus on defined benefit plans, they wanted to have an actuary on staff. I, of course, told him that made a lot of sense. However, he said the actuary needed to be from Montana because the senior Democrat on the committee, Max Baucus, hailed from that state.

What? I responded that I wasn't sure how many pension actuaries were actually in Montana, but I would try.

So after hanging up with Russ, I grabbed my ASPPA membership directory (which was still printed at the time) and went to the Montana list of members — only to discover there was a total of three actuaries in Montana. Not what you would call a large pool, but at least it wasn't zero, I thought. So I called the first name that jumped out at me — Judy Miller — and she answered the phone. I proceeded to tell her about this really cool opportunity in Washington: "You know all those retirement plan rules that drive you crazy? You would be in a position to do something about them," I said — maybe a little bit of an exaggeration.

To my shock, she didn't laugh at me and say no. She wanted to think about it. So after talking some more, I suggested she meet with the Senate Finance Committee staff while she was in town for the Enrolled Actuaries meeting. Of course, they fell in love with her. She even met some of the Republican staff and they were impressed as well.

But then back in Montana, Judy started to get cold feet. If you lived in Montana, wouldn't you? Judy told Russ that as much as she was intrigued by the position, she thought it would be better to stay in Montana.

So I got another call from Russ. This time he said, "We loved Judy and we have to have her on staff, and Sen. Baucus is counting on you to convince her to come. Okay?" So I called Judy and laid it on thick — I am a lobbyist, after all. I told her that they are going to work on defined benefit plan legislation, and if you're not there, who knows what kind of mess they will make? I told her that if she doesn't take this job she will regret it for the rest of her life. I think I said something comparable to that six different ways. She finally said yes.

Of course, Judy did an amazing job while on staff. And yes, who knows what a mess they would have made of the Pension Protection Act without her presence. But the story doesn't end there.

In 2008, I asked her to come to lunch with me. ASPPA was in the process of forming the ASPPA College of Pension Actuaries (ACOPA) to ensure that our actuaries continued to have a strong voice as the overall organization continued to grow. It would clearly be best if an actuary were going to lead the group. Needless to say, a bunch of really smart pension actuaries are only going to listen to another really smart pension actuary — right? We were also in the very early stages of building a group for 401(k) plan advisors — the precursor to what ultimately became NAPA — and we



Judy Miller testifies at a Senate Finance Committee hearing, May 17, 2016.

needed someone with the right skill set to lead our policy and lobbying efforts on Capitol Hill so that I could focus on organizational growth.

Judy was the obvious choice and I sold her hard. Fortunately, she was intrigued. She had recently finished the Pension Protection Act, which was an incredible amount of work, and she needed a change of scenery. So we talked about the fact that before we moved any further we needed to inform her immediate boss, Russ Sullivan, who at that point was the Chief of Staff of the Senate Finance Committee. (It's common courtesy to do that when recruiting someone from Capitol Hill.) We were relieved that Russ gave us the thumbs-up.

So Russ informed Sen. Baucus, who had become Chairman of the Senate Finance Committee, that Judy was leaving. To say the least, he was not happy. He did not like losing his actuary from Montana, and he really didn't like the fact that no one asked him if he was okay with her leaving. Things got quite a bit worse from there.

Sullivan got yelled at, and I got a call from Jim Messina — also a friend — who was Sen. Baucus' personal Chief of Staff. You may have heard that name before. Jim went on to become White House Deputy Chief

of Staff for President Obama and then Obama's campaign manager in 2012 — kind of a big deal. He told me that despite the fact that we did discuss Judy with Russ, I was going to be banned from meeting with anyone on the Democratic Staff of the Senate Finance Committee. But because of our relationship, he convinced Sen. Baucus to only ban me for a year. Many lobbyists have been banned from meeting with certain committees for various reasons, but as far as I know I'm the only one to be *temporarily* banned from the Senate Finance Committee.

Still, it was a pretty big deal. *Roll Call*, the Capitol Hill newspaper, wrote a story about me being banned. Naturally, the ASPPA Board was concerned that it would impair our ability to be effective advocates for the membership. I told them that the year would go by quickly and the likelihood of any pension legislation, given the recent enactment of the PPA, was remote. More importantly, I promised them that Judy Miller would be worth it.

There is not enough space in this magazine to outline all that Judy has accomplished for the American Retirement Association. Most recently, Judy was instrumental in

our effort to get Treasury to withdraw its misguided proposal to change the nondiscrimination "cross-testing" rules. As my actuary friends will appreciate, watching Judy go at it with Treasury's Harlan Weller is a joy to behold.

Judy's efforts were also critical to our lobbying efforts on the fiduciary rule. She led our education efforts with Democratic senators on the need to have a level-to-level exemption, which was ultimately included in the final rule. Yes, an actuary lobbied on the fiduciary rule, and successfully so, I might add.

Since Judy announced her retirement, many folks in Washington and members of the organization have asked me what I'm going to do without her. My response is that it's like losing your right arm. But I would rather lose my right arm than never have had a right arm at all. I can say without any hesitation or equivocation that the American Retirement Association would not be where it is today without Judy Miller.

Yes, Judy, you were totally worth it! **PC**

Brian H. Graff, Esq., APM, is the Executive Director of ASPPA and the CEO of the American Retirement Association.



Governmental Plans: What's in a Name?

What does it mean to be a governmental retirement plan?

Here's a 10,000-foot view.

BY ALLISON M. GRIMM AND MELISSA H. WEAVER

W

hat's in a name? Sponsors of so-called "church plans" may tell you that it means if your plan is identified in a certain way, your plan has a bull's eye painted on it by litigation attorneys for plaintiffs.

Retirement plans for both governmental entities and churches are exempt from the protections and requirements of ERISA and have, in the past, been largely unregulated in their operations. However, in recent years, church plans have been the object

of interest by the plaintiffs' bar in lawsuits challenging the status of plans as church plans and the associated exemptions and privileges that go along with that status.¹ Some wonder if governmental plans will soon receive the same scrutiny.²

Congress enacted ERISA primarily to stop abuses in the administration of private pension systems.³ Governmental plans were exempted due to federalism considerations.⁴ The federal government did not want to tell states what to do with regard to retirement plans for state and local government employees.⁵

As a result, retirement plans sponsored by governmental entities are exempt from ERISA and from many requirements of the Internal Revenue Code that are applicable to qualified retirement plans sponsored by private employers. This affords sponsors of governmental retirement plans a great deal of flexibility in plan design. However, as has happened with church plans, some participants may begin to question the status of their employer's plan as a governmental plan and the loss the ERISA protections for the participant that go along with that status.

So how do you know if an employer is a governmental entity that can sponsor a governmental plan? If the plan sponsor is governmental, what type of plan can it sponsor? If the plan is a governmental plan, which rules still apply and which are

“It appears that while the IRS regulatory project is open, the DOL and PBGC plan to defer to the proposed draft regulations.”

exempted?⁶ This article attempts to give the reader a 10,000-foot view of the issues surrounding what it means to be a governmental retirement plan. Unfortunately, in many cases the answers to these questions are far from clear, and will require further research by plans sponsors and their advisors.

WHAT IS A GOVERNMENTAL PLAN?

The term “governmental plan” is defined in the Code and in two titles of ERISA (Titles I and IV) with similar, but not identical, language. The Code and Title IV of ERISA define a governmental plan as “a plan established *and* maintained for its employees by the government of the United States, by the

government of any state or political subdivision thereof, or by any agency or instrumentality of any of the foregoing.”⁷ Title I of ERISA uses the word “or” instead of “and,” providing that the plan must be “established *or* maintained.”⁸

Neither the Code nor ERISA defines key terms and phrases in the definition of governmental plans, however, including “established and maintained,” “political subdivision,” “agency,” and “instrumentality.” For almost 30 years, there were no regulations defining those terms either. Over the years, the different agencies with retirement plan oversight have interpreted their respective definitions of governmental plans slightly differently, and the result has been confusion among plan sponsors. For example, the Department of Labor (DOL) has ruled that if a plan covers a *de minimis* (insignificant) number of private sector employees, it can still be considered governmental.⁹ The PBGC has ruled that governmental plans may not cover *any* private sector employees.¹⁰ The IRS has not clearly ruled, however.¹¹

Mindful of the confusion created by different agencies and court decisions concerning what constitutes a governmental plan, the IRS let the retirement plans community in on its thinking in this area in November 2011. The IRS, in consultation with the DOL and the PBGC, issued an Advanced Notice of Proposed

1 The 7th Circuit U.S. Court of Appeals ruled earlier this year that a plan maintained by a church-affiliated organization was not an exempt church plan in *Stapleton v. Advocate Health Care Network*, No. 15-1368 (7th Cir. Mar. 7, 2016).

2 Rosenburg, Stephen D., “Will Church Plan Litigation Lead to an Attack on Governmental Plan Exemptions?,” 5/4/2015, <http://www.bostonerisalaw.com/archives/398548-print.html>.

3 *Rose v. Long Island Railroad Pension Plan*, 828 F.2d 910 (2d Cir. 1987), cert. denied, 485 U.S. 936 (1988).

4 *Roy v. Teachers Ins. & Annuity Ass'n*, 878 F.2d 47, 49 (2d Cir. 1989).

5 See, e.g., H.R. Rep. No. 533, 93rd Cong., (1st Sess. 1973).

6 A church plan may waive its ERISA exemption if it makes a special election by filing a statement with the IRS, and if applicable, the Pension Benefit Guaranty Corporation (PBGC). Code §410(d) and Treas. Reg. §1.410(d)-1(a); ERISA §4021(b)(3). Governmental plans do not have the same waiver option, however. So what are the implications if a governmental plan contains ERISA language (whether by design, or by accident) that does not otherwise apply due to the governmental plan exemption? The answer to this question is not clear.

7 Code §414(d) and ERISA §4021(b)(2). The term “governmental plan” also includes certain plans governed by the Railroad Retirement Acts of 1935 or 1937, and certain plans of Indian tribal governments and related entities. See Code §414(d).

8 ERISA §3(32).

9 See, e.g. DOL Adv. Op. 2000-01A (Feb. 18, 2000); DOL Adv. Ops. 95-15A (June 26, 1995) and 95-27A (Nov. 8, 1995).

10 PBGC Op. Ltr. 77-169.

11 Powell, 372-4th: T.M., *Church and Governmental Plans* at Section II.A.2 and footnotes 57-58. The IRS will not issue a ruling as to whether a plan is a governmental plan under Code §414(d). Rev. Proc. 2016-3, 2016-1 I.R.B. 126, §3.01(60).

Rulemaking containing guidance in the form of a draft of proposed regulations that included definitions of the key terms listed above.¹²

This article only discusses the definition of governmental plans found in the draft proposed regulations, because a complete discussion of the various opinion letters of the three governing agencies on the topic, as well as applicable federal and state court cases, would exceed the page limit and the reader's attention span. Furthermore, it appears that while the IRS regulatory project is open, the DOL and PBGC plan to defer to the proposed draft regulations. While the DOL continues to use its *de minimis* approach in the interim, the PBGC has declined to address the issue further until the IRS regulations go into effect.¹³ Thus, it makes sense to focus attention on the definitions set forth in the draft proposed regulations, which define the key terms for making a governmental plan determination as follows.

'Established and Maintained'

A plan is "established and maintained" if: (i) it is established and maintained for employees by an employer; (ii) the employer is a governmental entity; and (iii) the participants covered by the plan are employees of that governmental entity.¹⁴ There is no *de minimis* rule for participation by a small number of private sector employees.

'Political Subdivision'

A political subdivision of a state means: (i) a regional, territorial, or local authority, such as a county or municipality that is created or recognized by state statute to exercise

sovereign powers (taxation, eminent domain, police powers); and (ii) the governing officers are either appointed by state officials or publicly elected.¹⁵

'Agency or Instrumentality of the United States'

An agency or instrumentality of the United States is determined using a facts and circumstances test that considers whether:

- i. the entity performs or assists in the performance of a governmental function;
- ii. there are no private interests involved, or the government of the United States has all of the powers and interests of an owner;
- iii. the control and supervision of the entity is vested in the United States government (must be more than extensive federal regulation of an industry);
- iv. the entity is exempt from federal, state and local tax by an Act of Congress;
- v. the entity is created by the United States government pursuant to a specific enabling statute that prescribes the purposes, powers, and manner in which the entity is to be established and operated;
- vi. the entity receives financial assistance from the government of the United States (but not just due to a contract to provide a governmental service);
- vii. the entity is determined to be an agency or instrumentality of the United States by a federal court;
- viii. other governmental entities recognize and rely on the entity as an arm of the United States government; and

ix. the entity's employees are treated in the same manner as federal employees for purposes other than providing employee benefits (*e.g.*, granted civil service protection).¹⁶

'Agency or Instrumentality of a State'

An agency or instrumentality of a state is determined using a two-part facts and circumstances test, which considers both main factors and other factors. The "main factors" are whether:

- i. the entity's governing board or body is controlled by a state (or political subdivision thereof);
- ii. the members of the governing board or body are publicly nominated and elected;
- iii. a state (or political subdivision thereof) has fiscal responsibility for the general debts and other liabilities of the entity, including responsibility for funding of benefits under the entity's employee benefit plans;
- iv. the entity's employees are treated in the same manner as employees of the state (or political subdivision thereof) for purposes other than providing employee benefits (*e.g.*, employees are granted civil service protection); and

v. in the case of an entity that is not a political subdivision, the entity is delegated the authority to exercise sovereign powers (power of taxation, eminent domain, police powers) of the state (or political subdivision thereof) and the delegation of authority is pursuant to a statute of a state (or political subdivision thereof).¹⁷

The "other factors" considered are whether:

12 REG-157714-06, 76 Fed. Reg. 69172 (11/8/11), as corrected at 76 Fed. Reg. 76633 (12/8/11). See Announcement 2011-78, 2011-51 I.R.B. 874. The IRS subsequently issued Notice 2015-7 to specifically address whether a plan sponsored by a state or local government is a governmental plan if employees of public charter schools are covered.

13 See DOL Adv. Op. 2012-01A (2012); 2011 "Enrolled Actuaries Meeting, Questions to the PBGC and Summary of Their Responses," Mar. 2011, Q&A 22, available at <http://www.pbgc.gov/Documents/2011bluebook.pdf>.

14 Draft Proposed Reg. §1.414(d)-1(k).

15 Draft Proposed Reg. §1.414(d)-1(e).

16 Draft Proposed Reg. §1.414(d)-1(c).

17 Draft Proposed Reg. §1.414(d)-1(f)(2)(i).

“Governmental plan sponsors have been provided with an exemption from many of the rules that apply to private employers when it comes to sponsoring retirement plans.”

- i. the entity’s operations are controlled by a state (or political subdivision thereof);
- ii. the entity is directly funded through tax revenues or other public sources (Note: This factor is not satisfied if an entity that is not otherwise an agency or instrumentality is paid from public funds under a contract to provide governmental services or is funded through grants by the state or federal government);
- iii. the entity is created by a state government or political subdivision of a state pursuant to a specific enabling statute that prescribes the purposes, powers, and manners in which the entity is to be established and operated (Note: A nonprofit corporation that is incorporated under a state’s general corporation laws is *not* created under a specific enabling statute);
- iv. the entity is treated as a governmental entity for federal employment tax or income tax purposes (such as the authority to issue tax-exempt bonds under Code §103(a) or under other federal laws);
- v. the entity is determined to be an agency or instrumentality of a state (or political subdivision

- thereof) for purposes of state laws (e.g., the entity is subject to open meetings laws);
- vi. the entity is determined to be an agency or instrumentality of a state (or political subdivision thereof) by a state or federal court;
 - vii. a state (or political subdivision thereof) has the ownership interest in the entity and no private interests are involved; and
 - viii. the entity serves a governmental purpose.¹⁸

WHICH RETIREMENT PLANS CAN BE SPONSORED BY GOVERNMENTAL EMPLOYERS?

If a plan sponsor *is* a governmental employer, what types of plans can it sponsor? The following types of retirement plans may be sponsored by governmental employers:

- 401(a) plan (other than 401(k), such as profit sharing, money purchase, defined benefit, etc.)
- 401(k) plan if *grandfathered* (the plan must have been adopted by the governmental entity prior to May 6, 1986 and continuously maintained since)¹⁹
- 403(b) plan
- 457(b) plan (nonqualified, eligible deferred compensation plan)

- 457(f) plan (nonqualified, ineligible deferred compensation plan)

WHAT TESTS OR RULES ARE INAPPLICABLE TO GOVERNMENTAL PLANS BECAUSE OF THEIR STATUS?

- If a retirement plan is a governmental plan because the plan sponsor is a governmental employer, it is exempt from many rules under the Code and/or ERISA.²⁰ The following is a list of the provisions of the Code and of ERISA that do not apply to governmental plans:²¹
- Minimum age and service rules of Code §410(a)
- Minimum coverage requirements of Code §§ 401(a)(3), 401(a)(26), and 410(b)
- Minimum vesting requirements of Code §411 including minimum vesting schedules, minimum accrual requirements for defined plans, consent requirements for plan distributions, and the anti-cutback rule of Code §411(d)(6)
- Nondiscrimination rules of Code §§401(a)(4) and 401(a)(5)
- Top heavy requirements of Code §§401(a)(10) and 416
- Joint and Survivor Annuity requirements of Code §401(a)(11)
- Merger and consolidation rules of Code §414(l) (See Code §401(a)(12))

¹⁸ Draft Proposed Reg. §1.414(d)-1(f)(2)(ii).

¹⁹ Nongrandfathered governmental employers cannot sponsor 401(k) plans; however, Indian Tribal governments and rural cooperatives can sponsor 401(k) plans. Code §401(k)(4)(B)(ii) and (iii); Treas. Reg. §1.401(k)-1(e)(4)(ii).

²⁰ Some 403(b) plans are governed by ERISA and some are not, depending upon actions and elections by the plan sponsor and its level of involvement with the plan.

²¹ Calhoun, “Checklist of Federal Tax Rules Applicable to Public Retirement Systems,” <http://benefitsattorney.com/charts/appfa/>; Jones, Fox & Bloom, Chapter 4, *Church Governmental and Collectively Bargained Plans*, pp. 4–45, <https://www.irs.gov/pub/irs-tege/epchd403.pdf>.

- Anti-assignment and alienation rules of Code §401(a)(13)
- Commencement of benefits requirements of Code §401(a)(14)
- Requirement that plan not decrease benefits due to increases in Social Security benefits (See Code §401(a)(15))
- Protections under Code §401(a)(19) regarding the forfeiture of benefits when a participant withdraws mandatory contributions from the plan
- Requirements with respect to PBGC notices of qualified total distributions under Code §401(a)(20)
- Minimum funding rules for a defined benefit plan under Code §§ 430-432
- ERISA requirement to file Form 5500, 29 U.S.C. §1024
- ERISA requirement to have compliant claims procedures, 29 U.S.C. §1133 and 29 C.F.R. §2560.503-1
- Requirement to provide participants with a Summary Plan Description under ERISA, 29 U.S.C. §1024 and 29 C.F.R. §2520.102-3

WHAT RULES DO APPLY TO GOVERNMENTAL RETIREMENT PLANS?

If a plan is a governmental plan, what rules *do* apply to such plans? The following is a list of the rules applicable to governmental plans established under Code §401(a) (e.g., profit sharing plans, money purchase plans, and defined benefit plans).²²

- Requirement that plan benefit “employees” (and not independent contractors) under Code §401(a)(1)
- Exclusive benefit requirements of Code §401(a)(2)
- Pre-ERISA vesting rules

(governmental plan must meet the vesting requirements resulting from the application of Code §§401(a)(4) and 401(a)(7) as in effect on Sept. 1, 1974;²³ participants must fully vest upon attainment of normal retirement age²⁴ and upon plan termination)

- Prohibition on using forfeitures under a defined benefit plan to increase benefits under Code §401(a)(8)
- Minimum distribution rules of Code §401(a)(9)
- Compensation limit for purposes of contributions or benefit accruals under Code §401(a)(17)
- Actuarial assumptions required by Code §401(a)(25)
- Direct rollover requirements of Code §401(a)(31)(A) and Treas. Reg. §1.401(a)(31)-1
- Death benefits under USERRA qualified active military service under Code §401(a)(37)
- Retiree health benefit rules of Code §401(h)
- Certain QDRO rules of Code §401(n)
- Notification of direct rollover rights of Code §402(f)(1)
- Pick up rules of Code §414(h)
- Limitations on contributions and benefits under Code §415 (some special rules apply)
- Definitely determinable benefits/written plan document (Treas. Reg. §1.401-1(a)(2) and §1.401-1(b)(1)(i))
- Operation in accordance with plan terms

CONCLUSION

Governmental plan sponsors have been provided with an exemption from many of the rules that apply to private employers when it comes to sponsoring retirement plans. However, history has shown that

labeling an entity a governmental employer is easier than proving that the label applies, especially in recent years. Sponsors of church plans have found their exempt status challenged repeatedly in the courts and by the regulators. Many expect the litigation focus to shift to governmental plans next. Before that happens, sponsors of governmental plans should revisit their right to claim exemption from ERISA and certain Code provisions to satisfy themselves that the governmental plan label still fits and that the plan is in fact exempt from those provisions. **PC**



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²² Calhoun, “Checklist of Federal Tax Rules Applicable to Public Retirement Systems,” <http://benefitsattorney.com/charts/appfa/>; Jones, Fox & Bloom, Chapter 4, *Church Governmental and Collectively Bargained Plans*, pp. 4-46, <https://www.irs.gov/pub/irs-tege/epchd403.pdf>. Other governmental plans, including 403(b) plans, 457(b) plans, and 457(f) plans have their own unique sets of rules that must be followed, and those rules are beyond the scope of this article.

²³ The three safe harbor vesting schedules are 15-year cliff vesting, 20-year graded vesting (based on a graded vesting schedule of 5 to 20 years), and 20-year cliff vesting schedule for public safety employees. More favorable vesting schedules (e.g., 5-year cliff or 6-year graded) will also satisfy the pre-ERISA vesting rules. See <http://www.irs.gov/Retirement-Plans/Plan-Participant,-Employee/Governmental-Plan-Determination-Letters>.

²⁴ In January 2016, the IRS issued proposed regulations that contain safe harbors for defining “normal retirement age” in governmental defined benefit plans (age 62, age 60 with 5 years of service, age 55 with 10 years of service, rule of 80 (where age plus years of service = 80), and 25 years of service). 81 FR 4599 (Jan. 27, 2016) (REG-147310-12).



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REGULATORY



DOL Unveils its Final Fiduciary Rule

The wait is over. Now the work begins.

BY NEVIN E. ADAMS

A

fter a five-month comment period, four days of public hearings, more than 3,000 comment letters, some 300,000 petitions, and more than 100 meetings with stakeholders — and nearly a year to the day after the Department of Labor (DOL) issued its proposed rule — the final fiduciary regulation was unveiled April 6.

THE ‘NEW’ FIDUCIARY

Under the rule, any individual receiving compensation for making investment recommendations that are individualized or specifically directed to a particular plan sponsor running a retirement plan, plan participant, or IRA owner for consideration in making a retirement investment decision is a fiduciary. Being a fiduciary under the final regulation means that an advisor must provide impartial advice in the client’s best interest and cannot accept any payments creating conflicts of interest unless the advisor qualifies for an exemption intended to ensure that the customer’s interests are protected.

The rule clarifies what does and does not constitute fiduciary advice, and includes examples of communications that would not rise to the level of a recommendation and thus would not be considered advice. It specifies that education is not included in the definition of retirement investment advice so advisors and plan sponsors can continue to provide general education on retirement saving without triggering fiduciary duties.

TPAs LOOK TO BE OKAY

The final rule included some good news and some much-needed clarity for third-party administrators.

While producing TPAs that act as a plan’s investment advisor would, of course, need to keep in mind the provisions of the new regulations that focus on the advisor role, the regulations made clear that a TPA’s recommendation of a recordkeeper would not constitute a “recommendation” under the rule and thus would not result in fiduciary status for the TPA, even if there was a differential in compensation as a result.

Additionally, the platform exception was simplified and broadened in the final regulation, addressing ambiguities that had caused concern. The final regulation clarifies that there are:

“The final rule included some good news and some much-needed clarity for third-party administrators.”

- no restrictions on proprietary investments on the fund platform; and
- no requirement or limit as to the number of investments.

The final rule also spells out that so-called “segmented” platforms are permitted. This would include differentials in, for example, the menu of funds offered to plans in a certain size segment. As long as the segmentation isn’t to a specific plan, these segmented platforms are allowed under the final regulation.

Of course, that doesn’t mean that there are no considerations for TPAs. Activities such as helping plan sponsors choose investments, making a recommendation as to the selection of an advisor (and receiving compensation for that advice) would constitute recommendations, and thus establish fiduciary responsibility. Similarly, if a TPA were to make a recommendation regarding a rollover transaction and receive a referral fee for that service, it would probably be considered advice.

One item that wasn’t included in the final regulation, though it was acknowledged, is a platform exception for IRAs. As stated in the regulation, the lack of an intervening, independent fiduciary in reviewing the funds (as there is in ERISA plans) concerned DOL officials. While the regulation acknowledges that in the presence of such an entity could provide the desired shield, the particulars of that situation are not yet clear, and will require additional research.

INVESTMENT EDUCATION

The final rule defines a variety of investment education activities that fall short of fiduciary conduct, and makes clear that advisors do not act as fiduciaries merely by recommending that a customer hire them to render advisory or asset management services. It also expressly provides that investment advice does not include communications that a reasonable person would not view as an investment recommendation. This includes general circulation newsletters, television, radio, and public media talk show commentary, remarks in widely attended speeches and conferences, research reports prepared for general circulation, general marketing materials, and general market data.

Significantly, the final regulation explains that education to plan participants including naming specific funds would be permitted “if certain conditions are met.” The proposed rule would have restricted plan advisors from being able to mention specific funds in the plan menu in asset allocation education materials.

However, in the context of IRAs, the DOL notes that there is no independent fiduciary to review and select investment options, and so references to specific investment alternatives will not be considered education.

Additionally, under the final rule, all appraisals (as opposed to just ESOP appraisals in the proposal) will *not* be considered advice for purposes of this rule but will be reserved for a future rulemaking.

SELLER’S EXCEPTION

Under the final rule, recommendations to plan sponsors managing more than \$50 million in assets (vs. \$100 million in the proposed rule) will not be considered investment advice if certain conditions are met and hence will not require an exemption.

“The rule and exemptions ensure that advisors are held accountable if they provide advice that is not in their clients’ best interest.”

NO CONTRACT REQUIREMENTS FOR ERISA PLANS

The new rule eliminates the contract requirement for ERISA plans and their participants and beneficiaries. Firms must acknowledge in writing that they, and their advisors, are acting as fiduciaries when providing investment advice to the plan, participant, or beneficiary, but no formal contract is required.

While the proposed rule required the firm, advisors and the client to be parties to the contract, in the final rule the DOL acknowledges that could be difficult in situations like call centers where the customer speaks to multiple advisors at a firm. The exemption in the final rule simplifies the contract requirement so that it is only between the firm and the client, and notes that there does not have to be a new contract for each interaction with a different employee of the same firm.

LITIGATION

The rule and exemptions ensure that advisors are held accountable if they provide advice that is not in their clients’ best interest. If advisors do not adhere to the standards established in the exemption, investors will be able to hold them accountable, either through a breach of contract claim (for IRAs and other non-ERISA plans) or under the provisions of ERISA for ERISA plans.

TRANSITION TIMING

There will be more time to implement the final rule — but not a lot. The broader definition of fiduciary will take effect in April 2017, and the other requirements of the exemption will go into full effect on Jan. 1, 2018. **PC**



Nevin E. Adams, JD, is the American Retirement Association's Chief of Marketing and Communication.

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ACTUARIAL



FASB Best Practices: Are Your ASC 715 and 960 Disclosures to Code?

Suggestions for selecting actuarial assumptions and preparing accounting disclosures in accordance with the applicable FASB standard.

BY NICHOLAS R. OSTEN
AND RAYMOND D. BERRY

If you have ever read through or prepared accounting disclosures under a Financial Accounting Standards Board (FASB) codification for defined benefit pension plans or postretirement health care plans, then you know that the accounting disclosures are anything but intuitive.

However, the FASB is very explicit when it comes to the methodology for calculating benefit obligations and how to prepare accounting disclosures. Therefore, it is critical for plan sponsors, actuaries, and other consultants to understand the requirements specified in the codifications to ensure that their accounting disclosures have been prepared in accordance with the applicable standard.

This article will provide an overview of the FASB codifications that are applicable to pension plans with several comments regarding postretirement health care plans and detail the best practices for selecting actuarial assumptions and developing the accounting disclosures, as well as identifying some common places where errors occur.

WHAT CODIFICATIONS ARE APPLICABLE TO MY PLAN?

The FASB has published codifications that vary based on the type of benefit plan and the associated accounting disclosures. Specifically, there are two codifications that are applicable to pension plans or postretirement health care plans, which are detailed below. Note that these codifications are only applicable to publicly traded and privately owned entities, not to governmental entities, which are regulated by the Governmental Accounting Standards Board codifications.

- **ASC 715** (formerly SFAS 158) — This codification is applicable to both pension plans and postretirement health care plans. It is used for developing accounting disclosures for the financial statements of the plan sponsor.
- **ASC 960** (formerly FAS 35) — This codification is only applicable to qualified pension plans. It is used for developing accounting disclosures for the plan itself.

ASC 715 OVERVIEW AND BEST PRACTICES

There are several key exhibits that must be included in all ASC 715 disclosures. These include the reconciliation of the Projected Benefit Obligation (PBO) for pension plans, the development of the Net Periodic Benefit Cost (NPBC), Accumulated Other Comprehensive Income (AOCI), and projected benefit payments.

- **PBO** — This is the liability of the benefit plan based on the participants' assumed salaries at retirement. The changes that occurred during the year must be disclosed. These typically include service cost, interest cost, actuarial gains/losses, benefit payments, and plan amendments, among others.
- **NPBC** — This is the annual expense for the benefit plan. The components of the annual expense must be disclosed. These typically include service cost, interest cost, expected return on assets,

“Retirement decrements are preferred unless all early retirement benefits are actuarial equivalent to the normal retirement benefits.”

amortizations of prior service costs/credits (resulting from plan amendments) and any gains/losses in excess of a certain threshold.

- **AOCI** — Typically, not all changes in the PBO are immediately recognized in the NPBC. ASC 715 allows for partial recognition of actuarial gains/losses and prior service costs/credits through amortization.
- **Projected benefit payments** — The projected benefit payments of the plan for each of the 5 years after the valuation date and the sum of the benefit payments for years 6-10 must be disclosed.

There are several key actuarial assumptions that must be used to develop the ASC 715 figures. Technically, the actuarial assumptions are the responsibility of the plan sponsor. However, the actuary will usually provide significant input regarding the assumptions; particularly for the demographic assumptions. The auditor is responsible for ensuring the assumptions and disclosures are in accordance with the standards.

The following discusses some key actuarial assumptions in more detail.

Discount Rate

There are two major requirements for the discount rate used to develop the PBO under ASC 715:

1. The rate must be based on the yield of high quality corporate bonds.
2. The rate must reflect the economic environment as of the measurement date.

Typically, the plan sponsor uses a cash flow matching process to develop the discount rate. This process involves matching the plan's specific expected benefit payments to spot rates from an appropriate yield curve to solve for the single equivalent discount rate which results in the same present value of benefits. This is the most common and preferred method for developing an ASC 715 discount rate.

Expected Long-Term Rate of Return

The expected long-term rate of return is used to develop the expected return on plan assets component of the annual NPBC. It is *not* used in the development of the PBO. This rate should be based on appropriate expectations of returns by the asset classes held in the plan trust. There are no prescribed requirements or methodologies for developing this rate like there are for determining the discount rate. However, a building block approach is typically used which applies capital market rate of return assumptions to the specific asset classes held in the trust in order to develop a single expected rate of return for the entire trust. A greater percentage of equity investments typically results in a higher expected long-term rate of return. This assumption is less common for postretirement health care plans and nonqualified plans since they are typically funded on a “pay as you go” basis.

“The most important actuarial assumption used in the development of the PVAB is the discount rate.”

Mortality Rates

As with all assumptions, the mortality assumption should be the best estimate and should reflect past plan experience to the extent credible. Most plans are not large enough to have the required mortality experience necessary in order to develop a credible plan specific mortality assumption. Therefore, most plan sponsors rely on generic mortality tables published by the Society of Actuaries (SOA) which are developed based on large mortality studies. The SOA has recently published the RP-2014 Mortality Table and the associated projection scale MP-2015. There are several forms of the RP-2014 such as the white collar and blue collar mortality tables that can be used to better model the mortality incidence of the plan's specific demographic.

The preferred mortality assumption is some form of the RP-2014 Mortality Table with generational mortality improvement projections using Scale MP-2015. If an older table or projection scale is being used, then there should generally be substantial empirical data indicating that the selected table or projection scale accurately models the plan's experience. It should be noted that this assumption is applicable to ASC 960 disclosures as well.

Retirement Rates

In general, retirement decrements are preferred unless all early retirement benefits are actuarial equivalent to the normal retirement benefits. This assumption is often far more critical for postretirement health care plans as benefits payable before Medicare eligibility are usually significantly higher than those after Medicare eligibility. Most postretirement health care plans provide for a Medicare offset to claim costs.

Special Accounting

There are certain events that trigger special accounting under ASC 715. These events have become more common and they are a common place for errors to occur. The two most common types of special accounting are curtailments and settlements, which are discussed in more detail below.

- **Curtailments** — A curtailment is an event that significantly reduces the expected years of future service of active plan participants or eliminates, for a significant number of active plan participants, future accrual of benefits. Common examples of curtailments are benefit plan freezes, factories closing, or downsizing. Curtailments may result in immediate recognition of deferred items in the AOCI in the NPBC.
- **Settlements** — A settlement is a transaction that meets all the

following criteria: the transaction is an action that is irrevocable, the plan sponsor no longer has the responsibility for the benefit obligation and any major risk relative to the pension assets or obligation used in the settlement has been eliminated.

When the total cash lump sum payments in a fiscal year exceed the sum of the service cost and interest cost components of the NPBC for that fiscal year, settlement accounting is triggered. A common example is a lump sum window for deferred vested terminated participants, particularly for a frozen plan. As a result of the settlement, the PBO and plan assets will decrease, and a portion of the gain/loss in the AOCI (dependent on the size of the settlement) is immediately recognized in the NPBC.

ASC 960 OVERVIEW AND BEST PRACTICES

The key exhibit that must be included in all disclosures is the Reconciliation of the Present Value of Accumulated Benefits (PVAB). The PVAB is the liability that represents the present value of the accumulated benefits under the plan. The exhibit shows the changes that occurred during the fiscal year in order to reconcile the beginning of year PVAB to the end of year PVAB. Common changes that are disclosed include benefits accumulated, actuarial gains/

The actuary will usually provide significant input regarding the assumptions; particularly for the demographic assumptions.”

losses, decreases in the discount period, benefit payments, actuarial assumption changes, and plan amendments.

The most important actuarial assumption used in the development of the PVAB is the discount rate. ASC 960 allows the PVAB to be calculated on one of two discount rate bases: a long-term rate of return and a settlement basis, which are discussed below.

- **Long-term rate of return** — This is an ongoing assumption determined on a continuing plan basis and does not represent the PVAB of the plan if it was to terminate. This rate should be based on appropriate expectations of returns by the asset classes held in the plan trust, and is typically equal to the long-term rate of return assumed in the NPBC calculation under ASC 715 as the rates are similarly defined in the accounting standards.
- **Settlement rate** — This rate is determined on a terminating basis and represents the PVAB if the plan was to be terminated. The settlement rate should reflect an insurance entity's interest basis for

determining annuity purchase rates as of the benefit information date. This rate is typically set equal to the ASC 715 discount rate. However, the ASC 715 discount rate tends to be less conservative than an annuity rate due to margins for profit that the insurer will build into their rate. So, a true settlement rate will generally be lower than the ASC 715 rate, but the ASC 715 rate may be an appropriate approximation.

It is not appropriate to use any other discount rate setting methodology for ASC 960 disclosure purposes. Sometimes segment rates published by the IRS for pension plan funding purposes are used to develop the PVAB. However, this is not acceptable under ASC 960. If the PVAB has been developed using funding segment rates, then the disclosures should be updated to utilize either a long-term rate of return or a settlement rate.

POSTRETIREMENT HEALTH CARE PLANS

There are additional assumptions required for postretirement plans which are less common or not required for pension plans, including the following:

- **Retirement decrements** — Age-based retirement decrements, as opposed to a single age, are almost always required.
- **Participation rate at retirement** — This is the percentage of participants electing coverage at retirement which should reflect the extent that benefits are subsidized by the plan sponsor.
- **Persistency of coverage** — This is the rate at which retirees are assumed to continue to elect coverage under the health care plan. This assumption is often set to 100%, but may be less if retiree contributions increase over time.
- **Medical trend** — This is the rate of medical cost inflation which should reflect general and long-term economic trends as well as plan expectations to the extent possible.

CONCLUSION

As one can see, there are many requirements that must be considered for plan and corporate accounting. There are additional items of concern that this article does not cover. Although accounting disclosures for pension plans and postretirement health care plans can be complicated, many problems and errors can be avoided by being familiar with the FASB codifications.

While this article provides a brief overview of the ASC 715 and ASC 960 accounting standards, the actual FASB codification should be reviewed prior to developing the applicable accounting figures or including them in financial statements. Conveniently for actuaries and plan sponsors, ASC 715 and ASC 960 accounting standards are available on the FASB's website in their entirety for your knowledge and reading pleasure. **PC**



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LEGAL



Church Plan Litigation May Be Headed to Supreme Court

We may know by late fall whether the high court will decide to resolve a 30-year-old conflict affecting church plans.

BY THOMAS E. CLARK JR.

By the end of the year, the U.S. Supreme Court will decide whether to hear at least two lawsuits related to the definition of a church plan exemption found in ERISA.

Ever since the first one was filed in 2013 challenging whether Catholic Church-related hospital pension plans are eligible for the exemption, these cases seemed destined for ultimate resolution by the Supreme Court. At issue is how narrow or how expansive the church plan exemption is, and whether these church-affiliated entities are eligible to use it so that their plans do not have to satisfy the myriad funding

and vesting requirements of ERISA.

Surprisingly, most of the courts which have addressed the issue threw out the IRS's expansive definition that allowed the hospitals to claim the exemption. Instead, the courts have adopted a far narrower definition. With more than a dozen similar cases filed in the last three years, two have reached appellate decisions by U.S. Circuit Courts, the appellate courts just below the Supreme Court. The plaintiffs, as participants in the pension plans at issue, successfully won their appeals in the 3rd Circuit in *Stapleton v. Advocate Healthcare Network* and in the 7th Circuit in *Kaplan v. Saint Peter's Healthcare System*. In both cases the courts ruled that the

hospitals are not eligible to use the church plan exemption because only churches can establish "church plans" as that term is defined in ERISA.

Before we jump into the legalese, however, it is worth considering the ramifications of these decisions.

UNDERFUNDING ISSUE

Stated simply, these rulings hold that the pension plans should have been complying with ERISA for as long as they have existed. The consequences are staggering considering that state laws, which applied in the absence of ERISA, usually have few if any requirements related to funding. As such, the primary motivation behind these

lawsuits is the fact that every single pension plan at issue is severely underfunded compared with ERISA's funding standard — many of them by hundreds of millions of dollars.

In addition to the underfunding issue, for the first time these plans would have to pay insurance premiums to the Pension Benefit Guaranty Corporation (PBGC) and put into place strict adherence to the many Title 1 fiduciary provisions of ERISA. Such tasks would require Herculean effort, and in fact may be downright impossible.

CONFUSION DATING BACK 36 YEARS

There are hundreds if not thousands of plans that would be affected by an ultimate resolution by the Supreme Court. For more than 30 years, the IRS has been issuing private letter rulings allowing church-affiliated entities to claim the church plan exemption. ERISA as passed in 1974 exempted “church plans” from its major provisions, including the minimum funding and fiduciary rules.

The rule was amended in 1980, and that amendment has caused much of the confusion. The IRS has interpreted the 1980 amendment to say that any plan that is maintained by a committee and that is sufficiently associated with a church is eligible for the exemption. However, both the 3rd and 7th Circuits have rejected that interpretation. According to the circuit courts, to meet the church plan exemption, the plan must be established and maintained by a church. Given that there typically is no argument that the hospitals themselves are churches, this had disqualified the plans from meeting the requirements of the exemption. The courts have based their decisions on the plain reading of the statute and the remedial purposes of the ERISA statute to provide protection to plan participants rather than exclude them from protection. In so deciding, the court rejected the hospitals'

arguments that the 1980 amendment to the church plan exemption allows any plan maintained, even if not established, by a church agency to be exempt.

WILL THE HIGH COURT ACT?

The defendant hospitals in *Stapleton* and *Kaplan*, facing hundreds of millions in funding requirements if they can't reverse the decisions, have both filed pleadings in court stating that they intend to file writs of certiorari with the Supreme Court looking to have the Circuit Court decisions overturned. However, the Supreme Court does not have to agree to hear every writ filed with it. The high court can be selective, and there is no guarantee they will take it.

If the Supreme Court grants the writs, the cases will likely be combined; they wouldn't be heard until 2017 or possibly even 2018, depending on how long it takes for briefing to be completed. If the high court declines to take the cases, then the law will be dramatically different depending on where these kinds of plans are sponsored. The 7th Circuit decision will only be law for plans established in Illinois, Wisconsin and Indiana; the 3rd Circuit decisions will only be law for plans established in New Jersey, Pennsylvania and Delaware.

But many of the lower court decisions may also continue to play a role, depending on how long it takes for the Supreme Court to decide to hear the cases. Currently, *Rollins v. Dignity Health* is on appeal to the 9th Circuit. Like the *Stapleton* and *Kaplan* cases, the plaintiffs in *Rollins* were successful in the district court by winning arguments that the plans were not church plans and could not use the exemption. A decision by the 9th Circuit in *Rollins* is expected any day now, and having one more circuit court decision could persuade the Supreme Court that the issue is ripe for hearing.

Alternatively, that impetus that could come from the 10th Circuit

in the case *Medina v. Catholic Health Initiatives*, where the court found instead in favor of the defendant hospital that the plan at issue was eligible for the church plan exemption. If the 10th Circuit agrees with the lower district court, that would provide the Supreme Court with a “circuit split,” where different circuit courts come to different conclusions about what the law is and the Supreme Court is often obligated to resolve the differences.

If briefs are filed sometime this summer, we may know by late fall or early winter whether the Supreme Court will decide to hear these cases. In the meantime, we shouldn't be surprised to see simultaneous efforts on Capitol Hill to pass legislation in favor of a more expansive definition of a church plan that would align with the 30-year-old interpretation of the IRS.

MEANWHILE...

For those who might sponsor or advise church plans that were not established by a church but are maintained by a church affiliated entity, there is little to do at this point but watch the litigation closely, and possibly review the status of your plan to see if changes can be made that would conform with the decisions of the 3rd and 7th Circuits. Even if you previously received a private letter ruling, your church plan status is in limbo until these cases are resolved. If you sponsor or advise a plan that was established by a church, then hopefully you have little to worry about unless the church entity has non-church affiliates with their own plans. Ultimately, concerned parties should seek out competent counsel to assist in addressing these issues. **PC**



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RECORD
KEEPING



Finding FDIC Insurance Within a Qualified Plan

In the wake of the impending SEC money market rules, FDIC-insured accounts can serve as a capital preservation option.

BY LENORA KEMP AND BRIAN KALLBACK

Over the last few months, many articles and white papers have been written about the upcoming changes to the SEC's revised money market regulations. The theme is similar in most of them: record keepers, TPAs, plan sponsors and advisors will need to review their fund options within the capital preservation investment category to ensure the funds offered fit within the objectives of the particular plan. Articles discuss institutional, retail and government money market funds, and stable value offerings — yet many fail to mention the potential benefits of an FDIC-insured investment account.

The SEC regulations will go into effect in October 2016. In response, fund companies and financial institutions have created new products or enhanced current service offerings. Like ducks wading carefully into murky pond water, TPAs and record keepers are working with their plan investment advisors to conduct due diligence as to which option is in the best interest of plan participants and beneficiaries. Fund performance, liquidity, gates and fees, and provider stability have been among the more commonly considered characteristics in selecting a money market investment option.

However, recent litigation concerning the relatively low performance of money market funds compared with stable value funds, as well as the appropriateness of using certain stable value funds, has caused consternation as to which one to use. ERISA requires a prudent, reasonable due diligence process that keeps at the forefront the best interests of plan participants and their beneficiaries.

Many record keepers or TPAs face a decision as to which route you want to take. In some cases, you may be able to offer multiple strategies and allow your advisor group to decide. Others will focus resources on a single strategy to centralize messaging and efficiencies.

“There is a demand for investments that are easy to understand, fully liquid, and result in the safety and security that is usually found within an FDIC-backed product.”

One overlooked investment option available to qualified plans is an FDIC-insured account. There is a demand for investments that are easy to understand, fully liquid, and result in the safety and security that is usually found within an FDIC-backed product. Unfortunately, many of these products do not show up on fund screens, since they may not be available across the landscape of platforms or because the category isn’t included within the search parameters.

When aligned side-by-side within the money market investment category, FDIC insured accounts compare quite favorably to other options. (See Table 1.)

Similar to a bank account, the standard deposit insurance amount is \$250,000 per depositor, per FDIC-insured bank, per ownership category. Whether the FDIC deposit insurance coverage is available within a qualified plan depends on whether the chosen financial product is a financial product (for example, mutual funds) or a deposit product (bank deposit account) and whether the bank is FDIC insured.

“For us, the decision to offer an FDIC-insured investment account was based, in part, on feedback we heard from our customers and advisor network that work with employee benefit plans,” says Karen Olson, V.P. of Treasury Management Solutions at Dubuque (Iowa) Bank and Trust, an FDIC Member. “Certain employers were asking if they could find security and safety within their qualified plan. They felt other options had too many strings attached and they weren’t comfortable offering capital preservation product where the NAV could potentially float.”

Generally, three traits of an FDIC-insured account separate the strategy from other money market or cash instruments: FDIC insurance protection, full liquidity, and accessibility/ease of use.

TABLE 1: MONEY MARKET INVESTMENT ALTERNATIVES

	Government MM	Prime (Retail) MM	Prime (Institutional) MM	FDIC insured investment account
Net Asset Value (NAV):	Constant	Constant	Floating	Constant
FDIC Insurance Coverage	No	No	No	Yes — Up to \$250,000 per participant.
Liquidity Fees	No	Yes	Yes	No
Gates	No	Yes	Yes	No

FDIC INSURANCE PROTECTION

“FDIC insurance is so easy to communicate to the end clients — whether from a record keeping or advisor perspective,” says Beth Pillsbury, senior director of capital preservation for the Banc of California’s Master Deposit Account. In a world where many employees desire the safety and security of a “known” commodity in a potentially intimidating and complex financial world, an FDIC-insured product brings the well-understood comfort of the full faith and credit of the United States government. “Everyone in America knows what FDIC insurance is no matter their investment experience and the gravity of what that protection represents is well understood by employees,” says Pillsbury.

Olson feels that the “FDIC insurance protection was the differentiator from other money market products,” she says. When TPAs and record keepers are educating their advisor groups and plan sponsors, the message of FDIC insurance resonates — audiences fully understand the included safety.

LIQUIDITY

While FDIC insurance protection is often cause for initial curiosity and interest, the full liquidity of the accounts leads to accessibility no matter the market environment. The ability to move money at the time and amount desired is easily understood and expected by many employees. Both gates and fees are possible for both retail and institutional prime money market funds. Should either of these be put into effect by the particular fund company, confusion could arise from employees who feel these accounts are otherwise fully liquid.

“We understand the frustration that TPAs and record keepers feel when they either cannot transition a particular fund to a new provider or when they have to hear from angry employees who are locked into an old

“The complexity of a guaranteed interest account often dilutes the marketed promise of a high rate of return.”

or poor investment,” says Olson. “It seems pretty straightforward to offer higher or guaranteed returns, but the equity wash, put option, market adjustment and other restrictions tend to offset the attractiveness of potential future gains. The employee is paying quite a bit in soft costs for that stated guarantee.”

The complexity of a guaranteed interest account often dilutes the marketed promise of a high rate of return. “When you start to review the fine print associated with an insurance product, you can see the many layers of legal protection the company places in front of that guarantee,” says Pillsbury.

ACCESSIBILITY

From the perspective of a plan provider, record keeper or TPA, can an FDIC-insured account be traded like a mutual fund? What are some administrative considerations should a record keeper or TPA want to add this to clients’ investment menus?

“[These accounts] look, act, feel, taste and smell like a traditional money market fund,” says Pillsbury. “[Record keepers, TPAs, or advisors] don’t have to change anything that they did in the past. Everything about these products — from the employee’s to the record keeper’s to the TPA’s perspectives — is very seamless to all parties involved.”

The decision whether to include a deposit account that includes FDIC

insurance within a qualified plan needs to carry the same prudent due diligence as any other investment decision. For many record keepers and TPAs, one characteristic — whether performance, liquidity, fees, manager tenure, etc. — generally does not influence the decision more than the collective characteristics of the whole. When analyzing which type of fund to use for a plan’s capital preservation options, plan demographics and other factors may very well conclude that selecting an FDIC-insured account product is a prudent choice.

“I’m delighted this topic is getting more attention,” says Pillsbury. “[We work in an industry] where we process things when they become a problem or an opportunity. An FDIC-insured investment is a worthwhile addition to any capital preservation section within a qualified plan.” **PC**



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HRPS is a business unit of Dubuque Bank and Trust Company, a subsidiary of Heartland Financial USA, Inc. Products offered through Heartland Retirement Plan Services are not FDIC insured, are not bank guaranteed and may lose value. Dubuque Bank and Trust Company is a Member of FDIC.

UPCOMING CONFERENCES

JULY 2016

ASPPA Regional Conference: Boston

Boston, MA
July 14–15

Western Benefits Conference

Seattle, WA
July 10–22

AUGUST 2016

ACOPA Actuarial Symposium

Chicago, IL
August 5–6

OCTOBER 2016

ASPPA Annual Conference

National Harbor, MD
Oct. 23–26

NOVEMBER 2016

ASPPA Regional Conference: Cincinnati

Covington, KY
Nov. 16–17

The ASPPA History Site is Now Online

A new website dedicated to ASPPA's rich history at the forefront of the retirement industry is now online!

asppa50.org

Featuring videos, photos from the ASPPA archives and documents from past presidents, members and other sources, the ASPPA history website celebrates our contributions to the pension and retirement industry and the actuarial profession – and the people who made it all happen. It's designed to complement the ASPPA history book currently in progress, and includes photos and documents uncovered in the course of researching, writing and editing the book.



Photos from ASPPA Annual Conferences going back to the 1974 conference, held a month after ERISA was signed into law, and more.



Documents from the ASPPA archives and other sources, including the 1966 certificate of incorporation, ASPPA Presidents' speeches, scripts of tributes to Chet Salkind and Ed Burrows, articles from *The Pension Actuary* by prominent leaders of the past, and more.



Videos starting with ones marking ASPPA's 25th anniversary in 1991 (and featuring founder Harry T. Eidson) and previewing this year's 50th anniversary celebration.

You'll also find a little background on the work-in-progress ASPPA history book, *Leading the Evolution: ASPPA's 50 Years at the Forefront of the Retirement Industry*, coming in October.

Check it all out at asppa50.org/, or click on "ASPPA History" in the "About" section of the ASPPA Net nav bar.



What's SUP? Form 5500 Changes for 2015 Filings



There are numerous changes affecting 2015 Form 5500 Series filings. Here's a helpful roundup.

BY MONIQUE ELLIOTT

Back in October 2014, the IRS published proposed changes to the Form 5500 series, announcing that it would start collecting some additional information on qualified plans. The purpose of these additional questions was to monitor plan compliance and check for red flags that might suggest potential disqualification errors. These proposed changes were published in draft on Form 5500-SUP in the *Federal Register* at that time.

A second draft was posted to the IRS website in March 2015 and submitted to the Office of Management and Budget for approval. Many groups came forward, arguing that the changes were burdensome and requesting that at a minimum, they be made optional for 2015.

Consequently, in December 2015 the DOL published advance copies of the 2015 Form 5500 and related schedules without a Form 5500-SUP. The DOL noted that the IRS compliance questions are now found in Schedules H, I and R, and that they are optional for the 2015 plan year. The IRS has published frequently asked

questions on their new compliance questions.

Additionally, in summer 2015 we saw some changes to the automatic extension period for many tax forms. This would have affected the Form 5500 by adding an additional month to the extension period. Congress has since repealed the change with respect to Form 5500 only.

THE DETAILS

The IRS and DOL are renewing their efforts to obtain plan compliance information. One mechanism available to them is the Form 5500. In October 2014 the IRS released a first draft of Form 5500-SUP. The second draft was issued in March 2015.

The draft Form 5500-SUP concerned many practitioners since it not only created additional work, but also necessitated communicating with plan sponsors about their compliance issues and updating their procedures and systems to be able to gather this data effectively and efficiently. Many groups wrote expressing their concerns, and requested the compliance reporting be withdrawn or, at the very least, made optional for 2015.

In December 2015, the draft 2015 Form 5500s were published on the DOL website with no Form 5500-SUP, possibly as a result of the feedback. However, the DOL news release and 5500 instructions stated that there were new IRS compliance questions included in Schedules H, I and R. The questions that were added to these schedules are identical to what was proposed for the Form 5500-SUP. The compliance information requested includes the following:

- Form 5500, page 1: Preparer's name, address, telephone number
- Schedule H/I, lines 4o-p: Whether there is unrelated business taxable income; Whether there are in-service distributions
- Schedule H/I, lines 6a-d: Trust name, EIN, trustee/custodian name, telephone number
- Schedule R—new section VII:
 - Whether the plan is a 401(k) plan
 - Whether the plan is a safe-harbor plan or uses ADP/ACP testing
 - Whether the current year methodology is used for ADP/ACP testing
 - Whether coverage testing is satisfied by the ratio percentage or average benefits test
 - Whether permissive aggregation with other plans is used to satisfy coverage and non-discrimination tests
 - If the plan has been timely amended for all required tax law changes
 - Date of the last amendment/restatement
 - Date of determination letter
 - If the plan is maintained in a U.S. territory

After publication of the draft 2015 Form 5500, the IRS retreated slightly by announcing that because OMB had not approved the new compliance questions, the IRS decided not to require plan sponsors to complete these questions in 2015 and that plan sponsors should skip these questions for this year. This is good news for

plan sponsors and practitioners. It is yet to be seen whether additional efforts from advocacy groups will result in the removal, or at the least the revision of these questions for future years.

EXTENSIONS

Last year the Highway and Transportation Funding Act of 2015 (HATFA) changed the filing deadlines for a number of tax returns, including the Form 5500. This provided for a 3½-month automatic extension on the return. While it is often assumed that extensions are always a good thing, many practitioners immediately commented that this extension was not a welcomed change and would add complexity to the retirement plan reporting system. Several groups voiced these concerns, and Congress subsequently passed an extension of the transportation funding measure that repealed the change in the automatic extension period for Form 5500 filers. Therefore, there has effectively been no change to the Form 5500 filing deadline.

WHAT'S REALLY SUP?

Many 5500 preparers have already been working diligently to adapt their systems to capture the compliance data being requested by the IRS. To the extent possible, preparers should avoid requesting information regarding the new compliance questions. However, not all preparers may be able to avoid doing so, for instance because of automatically generated information requests. Therefore, plan sponsors should be aware that their service providers may be requesting this information this year and that the information is not required. Plan sponsors should be diligent in reviewing their draft Form 5500s carefully, and deciding whether they do or do not want these *optional* questions answered on their filing. It is expected that anyone who files fewer than 250 returns will be able to file a paper Form 5500-SUP in future years, if they prefer to send a paper

filing and not include the information on their Form 5500, which is publicly available on EFAST.

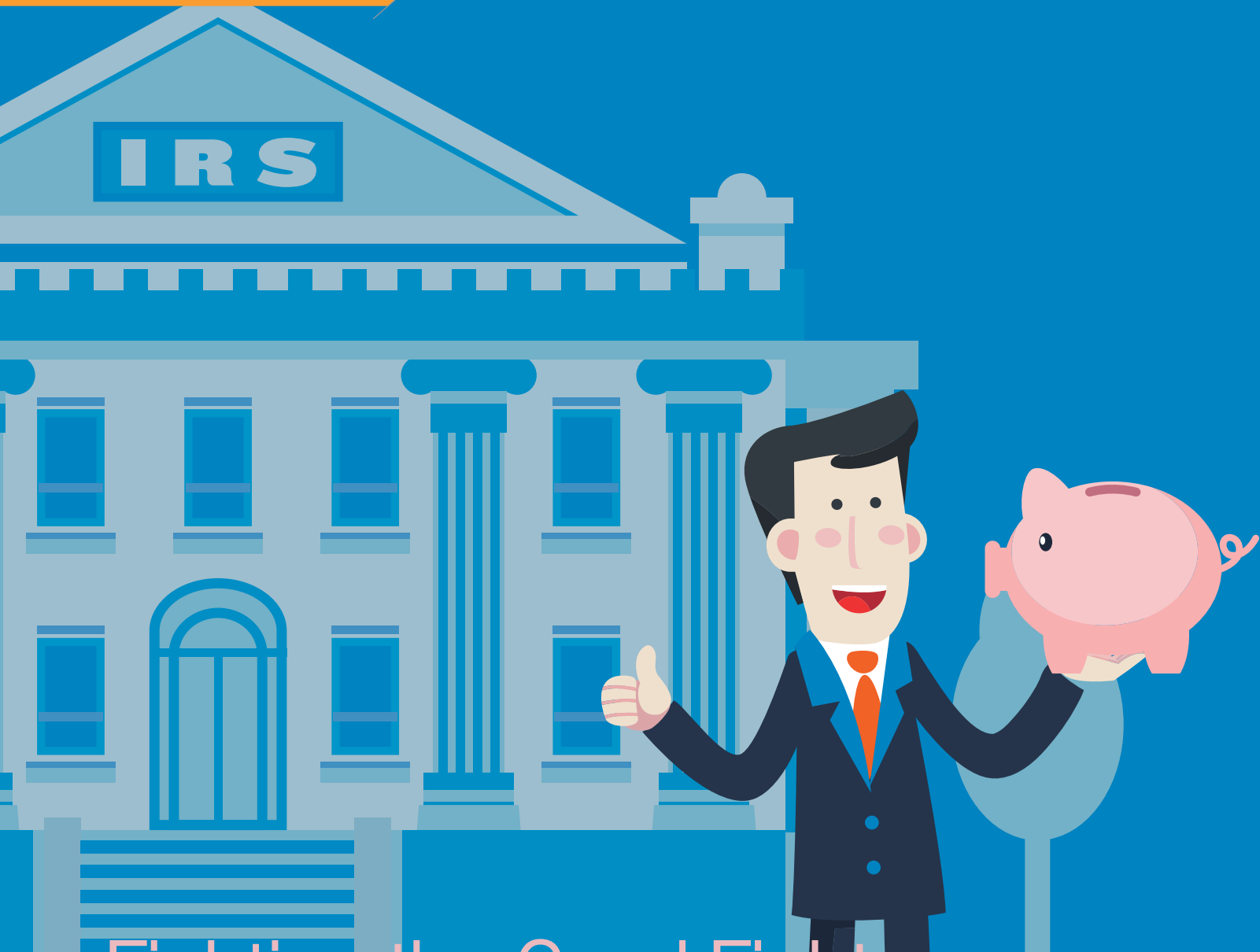
AFTER WORDS...

It will be interesting to see what happens with these IRS compliance questions and whether EFAST 3's release in 2020 brings additional compliance questions and other complexities to future returns. The challenge is that in their audits and investigations, the IRS and DOL continue to see numerous issues with plans. These issues relate to how the plans operate, proper sponsor oversight of plan and parties in interest, retention of competent service providers (auditors, advisors, TPAs, for example), and various other fiduciary matters.

What is the most effective, budget friendly, and automated approach that can be used to foreshadow whether there are potential issues with a plan? While modifying the Form 5500 to query known or typical issues sounds like a great idea, the big risk with this is that plan sponsors really do not know how to answer these types of questions, to know if they are answered incorrectly, or to understand the ramifications of incorrect answers. In many cases, especially the smaller unsophisticated plans, they already rely heavily on their auditors and record keepers to assist with ERISA compliance matters. These changes will certainly take it up a large notch. Additionally, plans filing Schedule I do not typically require an annual audit, so this will present an even bigger challenge for them.



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Fighting the Good Fight: The IRS Small-Plan Audit Program

In the early 1990s, ASPPA prevailed over a serious regulatory threat to small businesses and the pension actuarial profession — and laid the groundwork for an era of fruitful cooperation with the IRS.

BY JACK EL-HAI

This article was excerpted from Leading the Evolution: ASPPA's 50 Years at the Forefront of the Retirement Industry, coming in October. It tells one of the most dynamic stories in the history of the Society — the conflict between ASPPA and the IRS over the IRS actuarial audit program in the early 1990s and the productive resolution of that conflict.

For more about ASPPA's history and Leading the Evolution, please visit the ASPPA history website at asppa50.org/.

For years, starting long before the regulatory and legislative changes of the early 1980s, pension professionals and the IRS had been in agreement on the ground rules for establishing and operating defined benefit plans. “The pension community had been regulated by the Internal Revenue Service on the basis of negotiated logic between the practitioners and the IRS,” observed ASPPA historian Arnold F. Shapiro, the author of ASPPA’s 25th anniversary book. “There had not been a tremendous amount of law, except for general guidelines that were used to negotiate solutions to problems.”

Following the passage of TEFRA in 1982 and other tax legislation, ASPPA members had to contend with mass terminations of defined benefit plans and other substantive changes in their businesses. Then another cataclysmic event occurred in 1989, when the IRS started to attack the actuarial assumptions the profession had been using since ERISA was enacted in 1974. This move shook the organization to its core.

BLANKET MANDATE FOR PENSION PLANS

That year, the IRS began to change its approach to small-business defined benefit pension plans. “An IRS Assistant Commissioner and several others in the agency decided that some small defined benefit plans were inappropriately sheltering income and that they were taking

“The IRS took a very arbitrary and heavy-handed position, stating that certain assumptions used in funding these plans were wrong.”

deductions that were far too large,” explains ERISA attorney Bruce Ashton, ASPPA’s 2004 President.

The IRS believed that the deduction levels were based on the use of actuarial assumptions that were too conservative. ERISA required that Enrolled Actuaries use their best estimate, in view of all pertinent circumstances, in selecting assumptions. In response, the IRS took a very arbitrary and heavy-handed position, stating that certain assumptions used in funding these plans were wrong. Instead of pursuing presumed abuses on a case-by-case basis, as would have been indicated under ERISA, the IRS issued a blanket mandate for the use of IRS specified assumptions.

To enforce its mandate, the IRS started a massive audit program around the country. The IRS auditors aimed at very large law firms that had multiple defined benefit plans, as well as many small professional corporation plans in Arizona and other states. When the auditors reported that they had found irregularities in a plan, they imposed retroactive penalties, and ASPPA members would sometimes be sued by their clients “for having got them into a messy situation,” Ashton says.

ASPPA Executive Director Chet Salkind first heard about the audit program when he received “about 50 phone calls in one day saying, ‘The IRS is calling me in for an audit and what they are insisting upon is a projected rate of investment return of 8 percent per annum, and an assumed retirement age of 65,’” he recalls. This very heavy-handed approach was completely in conflict with ERISA and the regulations governing the practices of Enrolled Actuaries. Nevertheless, the IRS persisted.

ACTUARIAL ASSUMPTIONS AT ISSUE

Under the Enrolled Actuaries’ Code of Professional Conduct, contained in Treasury regulations, selected assumptions needed to be based on the actual circumstances of each plan. If long-term investment return experience showed a net return of 8 percent a year, such an assumption would be deemed reasonable. If, in a particular industry, people typically retired at age 55, that would also be considered reasonable. Economic assumptions dealt with anticipated salary growth as well as investment rates. Those assumptions needed to be internally consistent, in a statistical modeling sense. Demographic assumptions, such as expected retirement age, expected rates of termination of employment and incidence of disability, should be related to anticipated experience, based on available data.

However, in the case of small employers, there was also a very practical issue that made such demographic assumptions questionable under almost any circumstance. First, with very small populations, any assumption is almost certain to be proven wrong. Second, where plans were designed to project maximum allowable benefits under the law, predictions of changes in compensation would often be immaterial.



The 1991 ASPA Annual Conference featured a gala 25th anniversary celebration.

Interestingly, the data collected by ASPPA in 1979 for the President's Commission on Pension Policy showed that fewer than 5 percent of all small plans were, in fact, designed or funded with these types of aggressive assumptions.

"For many years the IRS had accepted assumptions of retirement ages as low as 55 and investment returns of 5 percent per year," Salkind noted. "It was an extremely difficult situation because not only did the IRS want to impose those new assumptions, but they also wanted the assumptions to apply retroactively. It would have been less serious — although still a problem — if they would apply the new rules going forward. But the IRS was determined to upset past returns."

ASPPA RESPONDS

Salkind immediately perceived the audit program not only as an attack upon the small business

pension plan system, but also an assault on the membership of ASPPA, especially the pension actuaries for the plans that were being audited. He conferred with the chair of ASPPA's Government Affairs Committee, attorney Fred Reish, and Reish's partner Bruce Ashton. Together they determined to do something to prevent this overreaching abuse of authority by the IRS.

"Fred and I started finding out everything we could about the actuarial audit program," Ashton recalls, "and we wrote a pamphlet designed to help members understand what the issues were. After that, we wrote a booklet that discussed what the IRS was doing, the legal issues involved, the practical issues involved, how to handle an audit, and how to deal with the cases that members' clients were involved in." The booklet, which explained "why the IRS was wrong, where they were wrong, and how to fight the audit

program," as Reish remembers, sold about 1,000 copies, so they knew members were seeking it out and finding it useful.

At the same time, Salkind went into action, filing requests through the Freedom of Information Act (FOIA) to obtain audit-related documents from the IRS. "All government agencies tend to be protective of their paperwork," Salkind says. "The Freedom of Information Act puts the burden on the government to disclose." Salkind sometimes made use of his first-hand knowledge of IRS recordkeeping gained during his time as an IRS employee. After one FOIA document request, "somehow the IRS said they couldn't find the document. I replied, 'Well, it's in the third cabinet to the right,' and then they found it."

Several of the documents that Salkind obtained told a damning story. "One indicated that they wanted to raise \$666 million

“In the case of small employers, there was also a very practical issue that made such demographic assumptions questionable under almost any circumstance.”

in revenues from the small plan audits, and when you worked out the numbers, that assumed they were going to reject the interest and retirement age assumptions in about 90 percent of the plans. The document indicated they weren't dealing with the audits on an individual basis but were grossly imposing the new assumptions and doing it retroactively. It would have done serious harm to our members involved in small plans, and their clients.”

As the court cases wound through the system, ASPPA produced *amicus* (“friend-of-the-court”) briefs to submit to various courts. These briefs unquestionably influenced the ultimate outcome of the cases.

A NEW RELATIONSHIP WITH THE IRS

While the court cases proceeded, ASPPA also took the approach of meeting with IRS officials in person to find a solution to the crisis. Fred Reish and 1991 President Pat Byrnes met with IRS Assistant Commissioner John Burke to discuss the poor relations between the agency and the private sector, especially in the small-plan defined benefit pension plan market. “There was enormous animosity,” Ashton says. “And that was not good for the system. That had to change.” Even when there was distrust between the opposing sides, ASPPA often invited IRS officials to speak at conferences and other programs. There were definite disagreements, but these invitations resulted in a continuing exchange

of ideas. “I always tried to maintain good relations with the people in the regulatory agencies, and I treated them with a good deal of respect,” Salkind said.

ASPPA's discussions with the IRS led to a settlement program for the actuarial audits that many ASPPA members were able to take advantage of in order to close small cases inexpensively. Perhaps more importantly, the discussions marked the beginning of a long process in which ASPPA was able to form mutually beneficial good relations with the IRS and other government agencies. “You would have thought that this conflict would have made ASPPA and the IRS enemies,” observes 2006 President Sarah Simoneaux. “In fact, it brought us together. We came together and realized that we shared common objectives. We both want small businesses to adopt pension plans and we want Americans to save for retirement. And the IRS came to realize that ASPPA was never in support of abusive practices. That's really the result of this crisis. It turned out to have very positive consequences.”

RESOLUTION LEADS TO REMEDIAL CORRECTION PROGRAM

Ultimately, in 1995, the courts vindicated ASPPA's members and the private sector by ruling that the IRS had been wrong in its approach. The IRS gave up on pursuing plans that had operated under the earlier assumptions, and most plans had no

penalties imposed upon them. “So the apocalypse that we saw coming didn't happen,” Ashton notes. “But at the same time, the IRS actions had created an opportunity for us to start the dialogue with the folks at the IRS and the Department of Labor about other problems that arose in qualified pension plans and the need for some way to fix those problems voluntarily. That led to the creation of what has now become a robust remedial correction program that the IRS has. It also then led to the Department of Labor adopting a voluntary fiduciary correction program. All of those

“Salkind immediately perceived the audit program not only as an attack upon the small business pension plan system, but also an assault on the membership of ASPPA.”



1996 President Mike Callahan honors Rep. Nancy L. Johnson (R-Conn.) for her role in combating the IRS small-plan audit program.

“While the court cases proceeded, ASPPA also took the approach of meeting with IRS officials in person to find a solution to the crisis.”

were pushed, at least initially, by and through ASPPA’s Government Affairs Committee.”

A HIGHER PROFILE FOR ASPPA

Several years later, 1990 President Alan Stonewall looked back and called the IRS audit program “an all-consuming issue” for ASPPA. Yet ASPPA’s hard-fought battle against it “thrust ASPPA onto the national stage and made ASPPA better known,” Reish says. “It became a symbol of what ASPPA was capable of doing. It was a period of great excitement and great energy.”

Member Alex Brucker sees other benefits that came to ASPPA from the conclusion of the audit program controversy. “ASPPA started a period of growth from that moment,” he says. “We were able to persuade the IRS to start a voluntary correction program. We got the IRS to collaborate with us on benefits conferences all over the country in which IRS speakers meet with the community. We built a

relationship with the IRS that still is very strong, so that we have a great communication base with everyone at the government level. We saw the power of being able to speak with and have a relationship with the IRS, and they started to respect our opinions instead of thinking that we were just out to be advocates against them. The audit program was the turning point that built ASPPA to what it is today and what it will be tomorrow.”

ASPPA and the IRS forged ahead in their relationship and tried not to let the legacy of the audit program sour their interactions. “You know, sometimes you have to let these things pass,” former IRS Chief Actuary Jim Holland says. “It’s better to just let the emotions die, let the feelings die, let the thoughts about it die, and maybe 20 years later you can bring it up again.”

“So ASPPA has helped to fight the good fight through all of the



PBGC Communications Director Chet Salkind addressed the 1975 ASPA Annual Conference at the Mayflower Hotel in Washington, D.C. He became ASPA's Executive Director in 1979.

Behind the Scenes: ASPPA's Response to the Small-Plan Audit Program

“The audit program had been developed in the tax audit part of the IRS, without much input from the IRS’ actuarial branch. The program unfolded unexpectedly. We found that the methods used by Enrolled Actuaries were much broader than we had the ability to train agents to examine, because we couldn’t turn IRS Agents into actuaries. Unfortunately, the approach taken was to try to impose ‘one-size-fits-all’ assumptions that couldn’t be supported with evidence and effectively rode roughshod on the authority of the Director of Practice to enforce the Enrollment Regulations.”

— *Jim Holland, former IRS Chief Actuary*

“I realized you could accomplish more than you thought you could if you just put your head down and bulled ahead. You often succeeded. And I became more optimistic about the possibility of success in what we were trying to overcome. I saw that if we exerted enough effort, we had a good chance of winning.”

— *Chet Salkind, ASPPA Executive Director*

“If the IRS had prevailed, it would have created a tremendous amount of liability for the actuarial profession to a lot of taxpayers. We were very concerned about it. And we were prepared to go all the way. Had we lost this case, I don’t know where ASPPA would be today, because I think that it would have put a crimp on the whole actuarial profession, which would have changed the profession dramatically. The liabilities could have put a lot of people out of business.”

— *Alex Brucker, ASPPA member*

“Fighting the Actuarial Audit Program was rewarding because we were right, and we were dealing with something that was definitely wrong.”

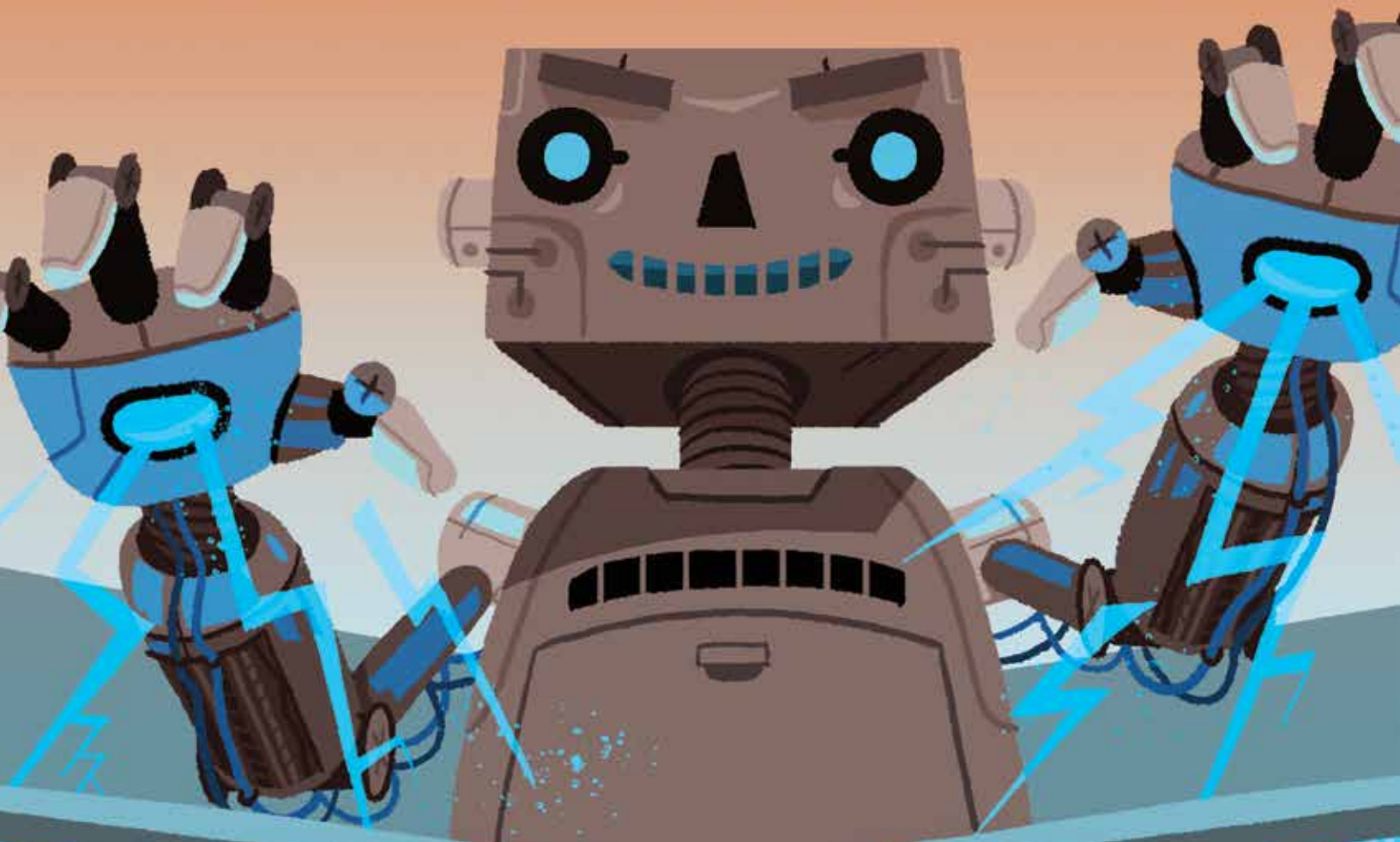
— *Andrew Fair, ASPPA member*

“The discussions marked the beginning of a long process in which ASPPA was able to form mutually beneficial good relations with the IRS and other government agencies.”

legislation and regulation that has gone past,” says member Marcy Supovitz. “Each and every one of those battles was a milestone in how ASPPA has protected plan formation, particularly in the smaller employer market. I’m not sure everybody in this industry realizes how much ASPPA has done in those areas.”

“I could see that ASPPA was an organization that really related to the work I was doing in the small-plan area,” says member Norman Levinrad, “and I felt it was the right organization for me because it represented the interests of the company I worked for and the kind of small business clients that we served.” **PC**

Jack El-Hai, the author of Leading the Evolution, is a professional writer and the author of numerous works, including The Nazi and the Psychiatrist and Non-Stop: A Turbulent History of Northwest Airlines.



THE RISE OF ROBO

An illustration of a computer workstation with multiple monitors. The central monitor displays the title 'RECORD KEEPING' in large, bold, white letters with a black outline. To the right, another monitor displays the author's name 'BY BRUCE SHUTAN' in white text. The background shows several other monitors, some displaying binary code (0s and 1s) on a blue background. A stylized character is visible on the left side, and a blue lightning bolt-like graphic is on the left. The overall color scheme is orange and blue.

RECORD KEEPING

BY
BRUCE
SHUTAN

A NEW LEVEL OF AUTOMATION IS DEVELOPING. BUT DO TODAY'S TECH-BASED STARTUPS CONSTITUTE AN OPPORTUNITY OR A THREAT TO TRADITIONAL PLAYERS?

The 401(k) landscape appears increasingly mechanized, most notably with robo-advisors reshaping the way plan sponsors and participants receive and pay for advice. The “robo” trend is now spilling into the recordkeeping world. But will so-called “robo-recordkeepers” slay established players with unbeatable digital solutions, ascend slowly, or simply fail to compete?

Many industry insiders still aren't quite sure what to make of robo-advisors like Betterment for Business or high-tech startups offering their own highly automated recordkeeping platforms. One source scoffs that advisory firms are masquerading as recordkeepers and outsourcing the technology, dismissing the involvement of “tech kids from Stanford with a fancy website who don't know anything about 401(k) plans.” However, some of the newcomers boast a surprisingly deep bench of experts to guide customers through gee-whiz technology.

SEEDS OF DISRUPTION

Robo-recordkeeping took root when auto enrollment and escalation features were encouraged by the Pension Protection Act to boost savings rates, observes Henry Yoshida, an industry thought leader who founded digital retirement savings platform Honest Dollar, which recently was acquired by Goldman Sachs' investment management division.

“It was only natural that at some point the recordkeeping portion was going to become automated, or that we would create a generation of people who would [be comfortable] with digitally driven advice, recordkeeping and decisions related to 401(k),” he says.

If anything, robo recordkeeping should obliterate any complacency in the market. Mary Patch, director of retirement plan solutions with Partners Wealth Management (and chair of ASPPA's *Plan Consultant* Committee), believes it will force the



“Who will calculate a new comparability design, review criteria for a hardship, scrub a census, and so many other tasks a recordkeeper provides that the robos have not to this point?”

— Mary Patch,
Partners Wealth Management

industry to reevaluate its technology and approach or face serious disruption. “Recordkeepers will be forced to find a more efficient way to do business,” she says. “Historically, if legislation changes forced them to raise their fees, they may not be able to going forward. They'll need to find a more effective way to implement changes to remain cost competitive.”

To stay competitive, Patch says they should be leveraging technology to contend with the industry push towards flat fee recordkeeping. “While many recordkeepers indicate their exposure to liability for the assets as a reason for implementing an asset-based fee, clients are uncomfortable with fees being tied

to assets,” she notes. Since assets in the plan tend to increase over time (due to contributions and positive market performance), “the plan recordkeeping fees exponentially increase without increasing the amount of work that is being provided to the same (or similar) number of employees.” Flat, per-head fees for recordkeeping are already a trend in the larger plan market, Patch notes, and the small plan market may experience the same trend.

Others suggest that buyers beware. The market needs to steer clear of “pop-up 401(k) providers” whose seemingly impressive front-end presence lacks solid back-end experience in plan administration, compliance testing, Form 5500s, compliance, etc., warns Chad Parks, a former RIA and certified financial planner who founded Ubiquity Retirement + Savings, formerly The Online 401(k).

“I think they're going to realize that this is a lot more technical and complicated” a market than anticipated, he says.

Robo-advisors and high-tech startups could bring tremendous value to the 401(k) recordkeeping space at a time when the entire business is becoming automated, but they may encounter an uphill battle for the hearts and minds of retirement plan sponsors.

Sophisticated algorithms can easily handle ERISA because it's rules-based, says columnist and educator Fred Barstein, founder and executive director of The Retirement Advisor University.

While recordkeeping is built on scale, Barstein says that's not the case for consulting. Emerging players will have a much harder time providing the handholding and consulting expertise of established companies — which, he says, involves nuances and intricacies — especially for smaller plans that lack resources. He doubts that a meaningful understanding of plan complexity can be programmed into an automated solution.



“We see ourselves as very complementary to the traditional recordkeepers and TPAs because we’re not attempting to reinvent the wheel.”

— Roger Lee, Captain401

BETTER MOUSETRAP?

But tell that to Betterment for Business, which built its own 401(k) recordkeeping system from scratch and is the only one in the industry that has done so in the past year, according to Cynthia Loh, the robo-advisor’s general manager.

Recordkeepers that have been around for 25 to 35 years must deal with clunky additions to legacy systems, while startups have the luxury of best-in-class platforms that are more malleable, explains Loh, whose firm recently raised \$100 million in new capital.

One example is handling exchange-traded fund (ETF) transactions, which none of the recordkeepers Betterment considered partnering with before developing its own solution could do. “In fact,” she reports, “they had to modify those ETFs into a mutual funds security that trades one time per day.” The same is true with regard to compliance software, with which she says Betterment is able to offer “more guardrails” and expansive automation.

Perhaps the larger value proposition is that recordkeeping is made available to plan sponsors

alongside various participant services that are in high demand — *i.e.*, an ability for participants to manage their 401(k)s in tandem with external accounts with the help of low-cost advice.

Betterment also points to 401(k) expertise within its ranks. “We didn’t do it with just a bunch of tech engineers,” Loh says. “We sought out people who we thought were the smartest in the industry.” The firm’s advisory board includes Raymond Kanner, IBM’s managing director and chief investment officer, and ERISA attorney Thomas E. Clark, Jr. of the Wagner Law Group.

If Betterment for Business is able to bring in 250 plans in 2016 following the January launch of its 401(k) platform, then Yoshida believes it would be considered “a massive success” for stakeholders of the nation’s largest independent robo-advisor, which serves more than 150,000 customers and manages more than \$4 billion in assets. Noting that the company employs only about 100 people, he says “they’re much more efficient scaling by having one person cover 100 Betterment plans than they are right now with their individual base.”

HUNDREDS OF MEASURES

The fact is that recordkeeping in the 401(k) space cannot be automated without human accountability, says Clark. Noting how everyone from the Department of Labor to FINRA agrees that foundational fiduciary principles must be applied to cookie-cutter algorithms used by robo-advisors, he says “the same is always going to be true for automating the recordkeeping side, but even more so.”

While there are only about a dozen critical metrics governing investments and a low barrier of entry into this market, he says there are hundreds of measures related to recordkeeping. The tricky part, of course, is complying with the myriad rules in the tax code.

Low-lying fruit seems to have been automated long ago, says Clark, citing as examples labor-intensive tasks involving daily valuation, account tracking and participant communications. But he notes that computer programmers cannot predetermine, for example, whether plan participants have adequately met hardship loan requirements or how to handle a qualified domestic relation order. “You need a human to actually do a legitimate cognitive analysis of the information being presented to the system about whether someone is eligible for any one of those plan features,” he says.

Considering how some of the industry’s big-box players can be challenged providing administration to more complex plan designs of plan administration, compliance and testing, Patch wonders whether robos will fare any better. “If the larger players struggle with complex plan designs, how will the robos handle them? Who will calculate a new comparability design, review criteria for a hardship, scrub a census, and so many other tasks a recordkeeper provides that the robos have not to this point?”



“My brethren who are independent TPA recordkeepers are all suffering from the same pain points of these legacy platforms that we’ve been having to work with.”

— Chad Parks,
Ubiquity Retirement + Savings

For robos to meet their profitability needs, they may implement vanilla plan designs and leverage safe harbors to simplify plan compliance, Patch believes. “This, coupled with housing the participant accounts in self directed brokerage windows, will naturally decrease recordkeeping costs and provide for a competitively priced plan solution,” she says.

Most digitally driven 401(k) providers have a different pricing model and offer inexpensive Vanguard ETFs or Vanguard index funds, according to Yoshida. “If you’re Guideline or Betterment for Business, you’re probably just charging anywhere from, let’s say, \$3 to \$10 per month per person just like what Honest Dollar was doing,” he says.

“So that model clearly isn’t going to work when you’re trying to capture 1,000-participant and larger plans because that becomes too expensive. You’d rather pay on a percentage basis.”

Barstein says the emerging crop of automated service providers will not work in an unbundled environment, citing as one exception Aspire Financial Services, LLC, whose technology platform is offered through TPAs. But they could give smaller recordkeeping TPAs a run for their money unless those TPAs infuse their services with more high-level technology.

“Whether you’re a compliance-only TPA or a recordkeeping TPA, if what a robo advisor does replaces the main part of what you do — your core competence — then you’re not really delivering anything very valuable,” he notes.

POWER OF PARTNERSHIPS

One could argue that recordkeeping is an opportunity for traditional players or their partners to distribute financial products to plan participants, Yoshida observes, while digital newcomers to the 401(k) space are simply starting from scratch and building a participant base. But he’s quick to point out that none of the robo 401(k) advisors have enough participants or clients to matter.

Any partnerships between the establishment and startups would need to address the misalignment of their business models. “Vanguard doesn’t need to partner with Betterment on an initial basis for Betterment for Business or even for Betterment traditional to be a distributor of their funds,” he says. “There’s going to be 25 RIAs within five miles of where we’re sitting that probably could send \$3 billion to Vanguard.”

Another consideration is that pairing digital providers with brick-and-mortar recordkeepers lacks the strategic value of, say, MassMutual acquiring the Hartford’s recordkeeping business. “They

were able to acquire 34,000 plans predominately in the emerging market space, plus gain a tax-exempt business that MassMutual didn’t have,” Yoshida explains.

“You’ve got a lot of components,” he continues. “You’ve got people. You’ve got assets under management, cash flow and revenue in two market sub-segments of the 401(k) recordkeeping space that you previously had no presence in. You don’t gain that if you look at partnering with or buying out one of these existing robo 401(k) advisors. In other words, it could be used as a tool to distribute if you’re an asset manager.”

In some cases, startups are teaming with established recordkeepers to expand their digital footprint. One example is ForUsAll, which three years ago sought to bring 401(k) capabilities in the large employer market within reach of small and midsize plans.

“We can sit on top of existing recordkeeping platforms, or potentially, TPA platforms,” explains David Ramirez, a Financial Engines alumnus who heads up investment management at ForUsAll, which he co-founded. He says the company has chosen to work with a select group of recordkeepers based on three key criteria: an ability to integrate with their systems, along with a commitment to delivering the highest quality 401(k), and at the lowest possible cost.

As part of its mission and role as a 3(16) fiduciary, ForUsAll uses fully integrated web-based and mobile technology to significantly cut those costs in half and vastly improve the user experience for plan participants. It also provides payroll integration with cloud-based payroll providers.

As this issue went to press, Ubiquity was nearly finished converting its entire book of business to a proprietary platform called Paradigm Record Keeping Systems that will be licensed to other TPAs and recordkeepers. The intention is

to work closely with early adopters to automate as much as possible for more complex plans as the company moves up-market.

Ubiquity's "secret sauce" may be in narrowing about 100 highly complex permutations of 401(k) plan design into a set of 20 parameters. Examples include eligibility, entry dates, deferral change frequency, vesting, hardships, loans, safe harbor and discretionary profit sharing.

Parks encourages scrappy startups to license his new platform rather than reinvent the process — only to find they're in way over their heads. His offer also extends to established players that won't be able to retool fast enough to anticipate the next generation of automated technology and systems interconnectivity.

"My brethren who are independent TPA recordkeepers are all suffering from the same pain points of these legacy platforms that we've been having to work with," Parks observes.

While applauding Betterment for attempting to duplicate its scalable success with robo-advising in the 401(k) recordkeeping space, he believes the move will underestimate or miscalculate all the moving parts that will need to fit. "Capturing expertise into an algorithm is always a real challenge," he says, "but when you have a string which is potentially 10 different outcomes within a regulatory framework, that becomes more difficult."

Another talked-about 401(k) entrant formed three years ago called bloom targets plan participants. "We have no desire to become the recordkeeper," says Chris Costello, the company's cofounder and CEO.

However, he reports that bloom is in talks with both employers and various recordkeepers, whom he considers "incredibly valuable," about bundling its services as a voluntary benefit or plan feature. The firm's automated solution was built to "work nimbly, agnostically with anyone, as long as they had a 401(k) and login credentials," Costello says.



You cannot automate out the expertise that an amazing, 30-year plan administrator on the TPA side brings to the table in understanding the nuances of how you meet the tax code and make the IRS gods happy."

— Thomas J. Clark, Jr.,
Wagner Law Group

Yet another notable newcomer to the 401(k) digital space is Roger Lee, founder and CEO of Captain401, which launched last year. "There are new advances in technology that can make administering a 401(k) plan from the company's perspective a lot easier and more frictionless," he explains.

His focus is on significantly raising plan sponsorship and participation among businesses with fewer than 100 employees, only 14% of which offer a retirement plan, according to the Government Accountability Office. In addition to baking automated investment advice

into a 401(k) plan, Captain401 uses technology to offload administrative work that customers have historically been expected to do with traditional recordkeepers. Other strategic objectives include improving the participant's overall experience and retirement-readiness outcomes.

"We see ourselves as very complementary to the traditional recordkeepers and TPAs because we're not attempting to reinvent the wheel," Lee explains. "We rely on them to provide expertise and consulting for the nuts and bolts of the 401(k) plans."

CONSOLIDATION FEARS

Patch recalls earlier in her career the practice of opening brokerage accounts at Charles Schwab with no account fee, along with hiring a TPA to perform compliance testing and prepare Forms 5500. This eliminated the need for a daily valuation recordkeeper and reduced the cost for administering the plan.

"That's kind of a similar service that Betterment is probably going to provide," she says. "It's hard as an advisor to competitively price daily valuation recordkeeping because most have a \$5,000 minimum. So now, if Betterment dramatically decreases that fee, there are no trading fees for the funds, similar to the OneSource at Schwab, and they're providing administration for a much lower fee, advisors may find themselves justifying the current recordkeeper fees to their clients."

Traditional independent recordkeepers that have long served the space could be "gobbled up by firms like Fidelity, Schwab and Empower that have critical mass and can drive down cost because of their pure volume," Patch predicts.

As an RIA working with individual, high net worth clients, Costello remembers how difficult it always was to sell an HR department on either starting a 401(k) or changing plans. He applauds Captain401 and Betterment for Business for



“We can sit on top of existing recordkeeping platforms, or potentially, TPA platforms.”

— David Ramirez, ForUsAll

swimming upstream amid these currents in hopes of targeting small businesses. About 60 million working Americans “don’t even get a crack at a 401(k),” he laments.

Reputation is expected to play a critical role in thinning the herd among new and old 401(k) recordkeepers. Plan sponsors know that Fidelity, Hancock, Transamerica or MassMutual offer the necessary technical expertise to administer 401(k) plans, Clark notes.

And while believing a newcomer like Betterment has an equally deep bench, he says other robo-advisors and high-tech startups will need to demonstrate competence when it comes to recordkeeping. In a nutshell, the issue is whether they have the intellect and manpower to custom design and administer a plan as well as established players.

“You cannot automate out the expertise that an amazing, 30-year plan administrator on the TPA side brings to the table in understanding the nuances of how you meet the tax code and make the IRS gods happy,” he explains.

Clark questions the distribution mechanism of emerging players in the 401(k) plan recordkeeping space. “Are they going to hire a nationwide group of 30 regional wholesalers like Fidelity or Transamerica or Principal or American Funds?” he wonders. “Or are they going to sell through advisors or TPAs?”

Whatever the case, it could be a steep climb for newcomers to start from scratch — especially at a time when, Clark observes, fees are falling to absurdly low levels because of the scale large that recordkeepers offer.

He remains highly skeptical of any game-changing technology that will reshape the 401(k) recordkeeping landscape for established industry players. “Do I believe that some third party that is not an already existing investment advisor or manager, recordkeeper or TPA can come in and majorly disrupt the recordkeeping world by offering some kind of technology that puts them all out of business?” he asks rhetorically.

“No, I don’t think that’s possible,” he continues. “Do I think that somebody in the industry, however, can build tools and technology and innovate and disrupt to the point that TPAs and advisors would want to work with their platform over others? Absolutely. That’s going to happen — it has been for a long time.” **PC**

Bruce Shutan is a Los Angeles freelance writer.





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What's Next for the Enrolled Retirement Plan Agent Program?

The ERPA program was rolled out by the IRS with much fanfare in 2009, yet it was abruptly curtailed with barely a last gasp in early 2016. Is there a future for the program?

BY MELISSA BAKER
AND PETER GOULD



Since the first ERPA exams were conducted in 2009, more than 1,300 retirement plan practitioners have earned this designation. With barely more than a terse news release in November 2015, IRS announced that the examination program would end in February 2016. In this article we'll briefly review the ERPA back story, consider the importance of the designation (from the perspectives of an ERPA and of a business owner) and ponder the uncertain future of the designation.

HISTORY

The ERPA program arose from the perceived need to have retirement plan practitioners who would be able to represent their clients in IRS matters. The ability to represent clients before the IRS is governed by Circular 230. Prior to 2004, it was possible for unenrolled preparers (*i.e.*, not CPAs, attorneys, Enrolled Agents or Enrolled Actuaries) to assist clients with IRS matters by filing Form 2848-D. The Internal Revenue Service Restructuring and Reform Act of 1998 led to the elimination of that ability for unenrolled preparers, a limitation that was put into practice in 2004.

As a result of these changes, there was concern among retirement plan practitioners (now “disenfranchised”), clients and the IRS about how to continue with normal IRS interaction and representation in our industry. (Note that this was during a time of rapid growth in the number of qualified plans.)

As if in a harmonic convergence, the stakeholders seemed to magically align in support of the concept of conferring IRS practice privileges to individuals servicing retirement plans (but not currently authorized to represent clients before IRS). The Advisory Committee on Tax Exempt and Government Entities (ACT) suggested that the IRS develop the ERPA program. The leadership of both ASPPA and NIPA were very strong proponents of the

“The ERPA designation provides a career development milestone for team members, and having multiple Circular 230 practitioners on staff provides a firm with a ‘deep bench.’”

program. Monika Templeman, the IRS Director of Employee Plans Examinations at the time, was a crucial “inside” booster — as evidenced by her enthusiasm in announcing the new ERPA program at the ASPPA Annual Conference. (More information about the evolution of the ERPA program is contained in the Fall 2011 issue of *The ASPPA Journal*.)

Now fast-forward to Nov. 9, 2015. Without any warning, the IRS announced that ERPA examinations would not be offered after Feb. 16, 2016. It was especially surprising because no mention of this impending change was made by IRS speakers at the ASPPA Annual Conference just weeks before.

Let's take a closer look at the viewpoints of the key players in the ERPA game: ERPAs, business owners, and the IRS.

“Monika Templeman, the IRS Director of Employee Plans Examinations at the time, was a crucial “inside” booster of the ERPA program.”

THE ERPA'S POINT OF VIEW

From the perspective of someone who's earned the ERPA designation, not only do ERPAs have the ability to represent taxpayers before the IRS, we are helping those taxpayers (often small employers who are plan sponsors) keep their plans in compliance. When we can practice before the IRS, we've expanded our ability to assist our plan sponsor clients.

Even though I may earn ASPPA, NIPA or other designations, they don't confer practitioner privileges before IRS. Under Circular 230, I was required to successfully demonstrate my expertise and proficiency by passing the ERPA exams. In addition, I had to pass the background check and be in good tax standing (also reviewed at renewal).

The IRS Office of Professional Responsibility can sanction me if I don't follow the rules of Circular 230. Despite these additional hurdles, earning my ERPA allows me to best serve my clients and also improves my marketability as a retirement plan practitioner.

BUSINESS OWNER'S POINT OF VIEW

As a business owner, having one or more team members who have the ability to represent clients before the IRS is a big plus. From a selfish perspective, it means that I don't have to handle every IRS matter, so employing an ERPA allows me to leverage my time.

In addition, having an ERPA on the team who can represent clients before the IRS provides additional peace of mind for the plan sponsor. This factor is often a marketing advantage when meeting with prospective clients.

As a “cost of doing business,” one might consider the ERPA to be a bargain compared with professional organization designations and dues — less than \$250 per test for two tests and a \$30 triennial renewal fee. Of course, the ERPA designation does not replace the importance and benefits of professional organization membership and credentials. Rather, they're complementary.

On the other hand, some business owners have taken the position that having only one ERPA on staff is sufficient. The authors don't subscribe to this point of view. Rather, the ERPA designation provides a career development milestone for team members, and having multiple Circular 230 practitioners on staff provides a firm with a “deep bench.”

THE IRS'S POINT OF VIEW

There has always been interest on the part of the IRS to work with taxpayer representatives who are competent. It makes interactions more efficient and usually results in speedier resolution of matters that come before IRS — a win-win situation. To that end, having practitioners subject to the requirements of Circular 230 gives the IRS some leverage (through OPR) that allows bad actors to be suspended or barred from representing clients before the agency.

Over the past 6 years, the IRS has brought more than 1,300 practitioners (formerly unenrolled preparers) into

The Importance of the ERPA Designation

In the words of the IRS:

“ERPAs can represent their clients before the IRS with respect to issues involving the following programs: Employee Plans Determination Letter program; Employee Plans Compliance Resolution System; and Employee Plans Master and Prototype and Volume Submitter program. In addition, ERPAs are generally permitted to represent taxpayers with respect to IRS forms under the 5500 series and can practice before Appeals, Collection, Counsel and other IRS offices with respect to the above listed matters.”

the fold of Circular 230 as ERPAs. It is notable that this was entirely *voluntary* and that every ERPA paid for this privilege. Since 2009 the IRS has probably engaged in thousands of taxpayer matter interactions with ERPAs, and has benefited by the competence and skill with which the ERPAs handle these matters.

In contrast, the IRS attempted to regulate all unenrolled tax preparers in 2011, by requiring *mandatory* competency testing and continuing education requirements. This was challenged in court, and the Court of Appeals for the DC Circuit ultimately upheld a lower court's ruling that the regulation program was invalid.

WHY KILL THE ERPA PROGRAM?

Since there was no dialogue between the IRS and other stakeholders prior to the announcement of the program's demise in November 2015, we can only make some educated guesses about the logic behind the decision to abandon the program.

“Earning my ERPA allows me to best serve my clients and also improves my marketability as a retirement plan practitioner.”

Did lower-than-expected participation lead to the abandonment? When the ERPA program was rolled out, it was originally estimated that from 3,000 to 6,000 practitioners could become ERPAs in the first 5 years of the program. With just over 1,300 ERPAs currently on the books, did the lower numbers lead to abandonment?

Was it about the money? The IRS is reeling from deep and prolonged cuts in funding. The agency has always been heavily involved in the subject matter (question-by-question) of the ERPA examinations. Was abandonment of the program seen as a cost-cutting move?

Was it because ERPAs didn't have a strong voice? Other categories of Circular 230 practitioners (attorneys, CPAs and Enrolled Agents) are well established and well represented by their professional organizations. These other practitioner categories have nurtured relationships with OPR and the IRS Return Preparer Office. While ASPPA and NIPA were instrumental in the development of the ERPA designation and they partnered to form AIRE (the contracted organization that developed and administered the ERPA examinations), neither organization served as the voice of ERPAs. An ERPA-centric organization dedicated solely to the needs and support of ERPAs never materialized.

WHAT'S NEXT?

If you're already an ERPA, preserve your hard-earned Circular 230 privileges. Be sure to satisfy your ERPA continuing education requirements — 72 hours per 3-year cycle (a minimum of 16 hours per year, two of which must be ethics credits). Pay your taxes and be sure to timely renew your ERPA.

If you aspired to become a Circular 230 practitioner by earning the ERPA designation, you could get involved in organizing and participating in a push to resurrect the ERPA examination program. Of course, we cannot predict the success of such an effort. Accordingly, you might want to pursue another path to becoming a Circular 230 practitioner. If so, be aware that no other avenue will focus on the specialized body of knowledge that retirement plan professionals use every day.

Making a unilateral decision to abandon the ERPA program without the benefit of input from partners and stakeholders was a poor choice. If the issue was cost cutting, couldn't examination and/or renewal fees have been increased to cover the actual costs of the program? If the issue was time, couldn't the IRS have relied more heavily on a combination of work experience plus existing examination programs from ASPPA and/or NIPA (in the same way that state CPA and bar examinations are not micro-managed by the IRS)?

ERPAs need an organization dedicated to supporting their needs and interests. It may be too late to resurrect the ERPA examination program, but today's ERPAs still need a voice.

And lastly, if the ERPA program is to be preserved and revived, it will need a champion within the IRS who will be as passionate an advocate as Monika Templeman was. **PC**

Melissa Baker, ERPA, QPA, QKA, is a retirement plan specialist at Indiana Benefits, Inc. in Bloomington, Ind. When this article is published, she hopes to be enjoying some summer sun on the tennis court.

Peter Gould, Enrolled Agent, CPC, QPA, QKA, is the president of Indiana Benefits. He'd rather be out in a field on his Kubota tractor than writing this article.





ESOPs: Something Old, Something New, Something Borrowed, Something for You?

On the occasion of the 60th anniversary of the first ESOP, here's an in-depth look at where ESOPs came from, what's new, and where they're going.

BY DAVID BENOIT

Employee Stock Ownership Plans (ESOPs) have been around for many years, and most practitioners in the field have at least a passing familiarity with them.

For the last 15 years or so, questions about ESOPs and use of an ESOP as an “exit strategy” for a business or as a way to finance another corporate priority have been relatively rare. Many are now seeing this relative rarity change. ESOPs are coming back into the discussion. This article hopes to help refresh the reader as to certain aspects of, change in, and uses of ESOPs.

Increasingly, business owners may seek to “tie the knot” with — to become essentially wed to — an ESOP as a business succession or advancement tool. Accordingly, and as a token of good luck and future prosperity, we discuss something old, some things new, something borrowed, and whether, in light of the above, an ESOP might be something for you.

SOMETHING OLD

Congratulations are in order in this, the 60th anniversary of first ESOP. Yes, ESOPs predate ERISA. The first ESOP was created in 1956 as the brainchild of attorney Louis Kelso in order to allow the employees of Peninsula Newspapers, Inc. of Palo Alto, Calif. to purchase the company from its retiring founders. Prior to that time, various formulations of stock ownership among employees had been tested, such as stock bonus plans, but ESOPs were fundamentally different in that an ESOP was conceived of not just as a benefit to employees, but also as a mechanism to finance transition of the plan sponsor from one owner to another — from a selling shareholder to the company’s employees.

Still, ESOPs were relatively exotic creations prior to their specific inclusion and authorization under ERISA in 1974. After that, their use

“As of 2015, the National Center for Employee Ownership estimates there are roughly 7,000 ESOPs covering about 13.5 million employees.”

exploded during the decades of the 1970s, ‘80s and ‘90s. Companies that have established an ESOP at one time or another include Avis, Exxon, Polaroid, United Airlines, Chrysler, Standard Oil of California and gasoline retailer Atlantic Richfield (ARCO). Top-10 supermarket chain Publix, which employs more than 180,000 employees and is the 35th largest retailer in the world, is currently wholly owned by an ESOP. As of 2015, the National Center for Employee Ownership (NCEO) estimates there were roughly 7,000 ESOPs covering about 13.5 million employees.¹ Of these, roughly 55% (covering over 90% of all ESOP participants in the United States) were created prior to 2000. However, due to a number of reasons, ESOPs somewhat fell out of favor since the beginning of the new millennium. It now appears that the tide is turning and ESOPs — something old — are resurfacing in many discussions. Certain tax friendly characteristics, as well as their utility as a business transition strategy, are currently being rediscovered by many companies and business owners.

¹ See, NCEO at <http://www.esop.org/> (as retrieved May 12, 2016).

ESOPs should not be confused with employee stock options plans or stock bonus plans, which are not retirement plans at all.”

What exactly is an ESOP? At its most basic level, an ESOP is a qualified retirement plan under which the sponsoring company contributes either stock or money to purchase stock from an existing owner, to a trust established in conjunction with the plan for the benefit of the company’s eligible employees.² ESOPs should not be confused with employee stock options plans or stock bonus plans, which are not retirement plans at all.³

The following is a basic overview of how an ESOP functions. Please note that there are many details and potential pitfalls not discussed in this article, and, if considering implementing or exploring an ESOP for your company, one is advised to consult with an expert familiar with the drafting and operation of an ESOP.

While the specific statutory authority for ESOPs can be found

under Code Section 4975(e)(7) (and to a lesser degree, ERISA §§ 407(b) and (d)), an ESOP is also subject to many of the other requirements of a qualified retirement plan under Code Section 401(a). It is designed and operated in accordance with the same basic qualification and tax benefit rules as any profit sharing or 401(k) plan. Generally, all full-time employees over age 21 will be participants under the plan, and their shares will be subject to similar vesting schedules as are other qualified retirement plans.

Although ESOPs share many of the characteristics and requirements of other qualified retirement plans, there are significant and important differences. First and foremost, an ESOP is designed to invest a significant portion, indeed often the majority,⁴ of its assets in employer securities.⁵ Importantly, it can also borrow money from the company, a third party (such as a bank), or even a selling shareholder in order to acquire the company stock without violating ERISA’s or the tax code’s rules against prohibited transactions. This type of an ESOP — one formed using a loan from any source — is generally called a “leveraged ESOP,” and the company making cash contributions to the plan to enable it to repay the loan.

Regardless of how an ESOP acquires the company securities held by the plan, there are certain rules regarding how those shares are held, who they benefit, and what happens to the shares when individual plan participants terminate, retire or otherwise are entitled to receive a distribution (or diversification, as we shall discuss) from the plan. The ESOP component of the plan

is often essentially the entire plan, but an ESOP component may also form a portion of a plan, the balance of which includes a 401(k) or other pension, profit-sharing, or stock bonus portion which is not invested in company stock.

In an ESOP, a company sets up a trust fund, into which it contributes new shares of its own stock or cash to buy existing shares. The plan maintains an account for each employee participating in the plan. An interest is allocated each year to individual employee accounts proportionate to that individual’s share of certain assets (generally company stock or cash) held in the trust. With an ESOP, you never buy or hold the stock directly while still employed with the company. Rather, the accounts are essentially bookkeeping entries. Allocations are made either on the basis of relative pay or some more equal formula. If an employee is terminated, retires, becomes disabled or dies, the plan will distribute the shares of stock in the employee’s account. ESOPs are also subject to the distribution provisions of Code Section 401(a)(14) and must further comply with the distribution and payment requirements of Code Section 409(o).

ESOPs are also generally required to provide participants with the right to demand distributions in the form of employer securities (albeit subject to significant exceptions and limitations) and to provide certain voting rights if the employer has a registration-type class of securities.

When employees leave the company, they receive their stock, which the company must buy back from them at its fair market value

2 For the more technically minded among us, an ESOP is an individually designed stock bonus plan, which is qualified under Internal Revenue Code Section 401(a), or a stock bonus and a money purchase plan, both of which are qualified under IRC Section 401(a), and which are designed to invest primarily in qualifying employer securities. An ESOP may form a portion of a plan the balance of which includes a tax-qualified pension, profit-sharing, or stock bonus plan which isn’t an ESOP. ESOPs generally have participation, vesting and allocation features common to all qualified plans. ESOPs are subject to the distribution provisions of IRC Section 401(a)(14), but must also comply with the distribution and payment requirements of IRC Section 409(o).

3 In addition to employee stock ownership through ESOPs, the NCEO estimates that there also are about 2,000 profit sharing and stock bonus plans that are substantially invested in company stock and that as many as 5 million employees participate in 401(k) plans that are primarily invested in employer stock. Up to another 11 million employees buy shares in their employer through employee stock purchase plans. See, NCEO at <http://www.esop.org/> (as retrieved May 12, 2016).

4 While it is not precisely clear what constitutes “primarily” invested in employer stock, most ESOPs are structured such that they invest more than 50% of plan assets in employer stock, and most practitioners believe that amounts above 50% would be considered as meeting the “primarily” invested requirement.

5 Most other retirement plans are prohibited from holding more than 10% of their assets in employer securities or real property.

“Congratulations are in order in this, the 60th anniversary of the first ESOP.”

(unless there is a public market for the shares). Private companies must have an annual outside valuation to determine the price of their shares. In an ESOP, just as in every other form of qualified pension plan, employees do not pay taxes on the contributions until they receive a distribution from the plan when they leave the company. ESOP distributions are qualified distributions that can be rolled into an IRA.

The law provides ESOPs with several special features that are either unavailable or available only on a limited basis to other plan types. One significant difference between an ESOP and most other qualified retirement plans is the ability of the ESOP to purchase employer securities from or sell employer securities to the company, a related company, current shareholders, plan fiduciaries, corporate officers or certain other “parties in interest” without having such transaction be considered a “prohibited transaction” under ERISA or the Internal Revenue Code.

Another significant difference is the ability to purchase the securities at issue with a loan either from the plan sponsor or from a third party. Again, but for a special exemption specific to ESOPs, this type of direct or indirect loan between the plan and the plan sponsor would be a prohibited transaction. One final important area of differentiation

from most retirement plans is the exemption enjoyed by ESOPs from certain limitations on the maximum contributions that may be allocated to any single participant’s account and the total amount of employer deductions found under Code Sections 415 and 404. Both of these sections allow leveraged ESOPs greater latitude than is permitted to most plans. This expands the ability of the ESOP to purchase larger amounts of employer stock than would otherwise be permitted in any single plan year.

A KSOP is a specific sub-set of ESOPs that combine a standard ESOP with a 401(k) plan. Under this type of retirement plan the company will often match employee contributions with stock rather than cash. KSOPs benefit companies by reducing expenses that would arise by separately operating an ESOP and 401(k) retirement plans.

SOME THINGS NEW

While ESOPs have been around for a while, there are some recent developments of which one should be aware, including the impact of the DOL’s final fiduciary rule, the impact of recent Supreme Court cases on the presumption of prudence in investment in plan sponsor stock, and certain administrative changes.

When the DOL finalized its final fiduciary regulation in April,

it consciously omitted a previously set forth rule specifically excluding those who provide appraisals, fairness opinions, or similar statements from the definition of a fiduciary.⁶ Instead, the final rule did not address appraisals, fairness opinions or similar statements concerning the value of ESOP securities or other property in any way. In its comments section, the DOL noted that it will be reviewing certain issues related to valuations as part of a separate regulatory initiative. As a result, one should expect further guidance and perhaps further regulation in the areas of appropriate and arm’s length appraisals, fairness opinions and other similar statements issued in conjunction with the purchase and sale of stock to or from an ESOP.

Another recent development has been the decisions by certain courts, and confirmed by the United States Supreme Court in the unanimous 2014 decision under *Fifth Third Bancorp v. Dudenhoeffer*,⁷ revising what was previously thought to be a relatively settled area of law. In the past, courts often recognized a special status for the purchase of employer securities under an ESOP — a presumption that since an ESOP is required to invest primarily in employer securities, the purchase was automatically prudent provided that adequate steps were taken, and that the decision to purchase employer securities would be reviewed under an

⁶ 81 FR 20969 (April 8, 2016), § IV.A.(5).

⁷ *Fifth Third Bancorp v. Dudenhoeffer*, 573 U.S. ____, 134 S. Ct. 2459, 189 L. Ed. 2d 457 (2014) (ERISA fiduciaries are not entitled to a presumption of prudence but are “subject to the same duty of prudence that applies to ERISA fiduciaries in general, except that they need not diversify the fund’s assets.”) 573 U. S., at ____ (slip op., at 1–2)

abuse of discretion standard and only invalidated by the courts if the action was found to be unreasonable given the circumstances. In *Dudenhoeffer*, the Supreme Court found that while an ESOP is exempted from ERISA's diversification standards, it is still under an obligation of prudence and fidelity to the best interests of plan participants and beneficiaries. This new line of authority has been further extended in the recent 2016 case of *Amgen Inc. v. Harris*.⁸

In addition, there are other areas that are being studied by the IRS, such as whether it is permissible under the Code and related regulations for an ESOP to provide that the plan sponsor may transfer S-Corporation stock from a non-ESOP plan (or non-ESOP portion of a plan) back to the ESOP (or ESOP portion of the plan) if a non-allocation year would not occur, as well as certain issues regarding timing of stock repurchase and diversification rights.

SOMETHING BORROWED

Perhaps the most important recent development, however, is not intrinsically ESOP-related, but rather a concept that has and been prevalent with regard to, is in essence borrowed from, other types of defined contribution plans for many years: the concept of pre-approved plan document language. In Revenue Procedure 2015-36, published July 6, 2015, the IRS expanded its procedures for issuing opinion and advisory letters regarding the acceptability of pre-approved master and prototype and volume submitter plans under Code Sections 401, 403(a) and 4975(e)(7).

In past, ESOPs and the attorneys drafting the ESOP plan documents have often faced long waits and lengthy negotiations in the process of obtaining a determination letter with regard to the plans. In addition, there are multiple areas of disagreement between the IRS and certain practitioners based on varying

ESOP Pros and Cons

Pros

- Provides a ready-market for a privately-held company as an alternative to a third-party sale.
- Flexible succession or estate planning tool. It allows owner(s) the flexibility of liquidating whatever portion of ownership desired over any chosen period of time.
- Preserves jobs for loyal employees and preserves legacies that are typically lost in third-party mergers and acquisitions.
- ESOP can borrow funds if needed to fully or partially liquidate an owner and both the principal and interest paid on the loan are tax deductible through employer contributions to a qualified retirement plan.
- In a C-Corporation, the capital gains tax on the proceeds of a sale to an ESOP can be deferred if 30% or more of the company's outstanding stock has been sold to the ESOP at the completion of a transaction and the proceeds are invested in "qualified replacement property" (QRP).
- In an S-Corporation, the ESOP is a tax-exempt owner, so in a 100% ESOP owned company, the corporation is entirely tax exempt.
- ESOP companies outperform. An ESOP establishes an incentive-based retirement plan for company employees, allowing them to share in the growth of the company. Independent national studies show that ESOP companies out-perform non-ESOP companies in annual growth and revenue. Projected out over 10 years, an ESOP company is typically one-third larger than a comparable non-ESOP company, and the overall profits equate to an average of 8% to 11% higher than non-ESOP counterparts.
- Dividends on company stock that are used to repay an ESOP loan, or paid directly to participants are deductible under IRC 404.

Cons

- Cost. The costs to design and implement an ESOP can often top \$50,000.
- Complication. ESOPs have a number of intricate tax rules (as can be seen above), and therefore expert advice from advisors, experts, attorneys and recordkeepers who regularly practice in this field is often the best protection against inadvertent, yet significant, mistakes.
- Ownership dilution. Sale of shares to an ESOP to finance the company's growth will result in dilution of the current owners' interests. Therefore, any expected gains must be weighed against this loss of ownership.
- Valuation concerns. An annual independent appraisal of the company is required to aid the plan trustee in establishing fair market value (FMV) of the stock. Most ESOP fiduciary issues revolve around the valuation procedure and methods used to establish FMV. The ESOP is prohibited by law from purchasing stock at a price greater than FMV.
- Claims against company liquidity. An ESOP is required to repurchase shares in certain occasions and at certain times. This repurchase obligation does not provide much flexibility, and can have a significant impact on cash flow. Careful planning is required to analyze and plan sufficiently to meet liquidity needs for repurchase obligation.

⁸ *Amgen Inc. v. Harris*, No. 15-278 (U.S. Jan. 25, 2016).

interpretations of statutory language and requirements as such relates to ESOPs. By allowing for and advisory letters with regard to certain ESOP language, the IRS hopes to both speed up the approval process as well as reduce misunderstandings. This could be a significant turning point regarding the drafting of ESOP plan documents.

Drafters will be able to include the specified ESOP provisions in the round after the current PPA restatements. This next round opens on Feb. 1, 2017, with newly drafted documents to be submitted to the IRS for review by Jan. 31, 2018. Given this timing, the first preapproved ESOP plan documents will likely not be available for adoption until sometime early in 2020.

In order to receive a favorable opinion letters under Rev. Proc. 2015-36, the plan document must include a statement that the plan is an employee stock ownership plan within the meaning of Code Section 4975(e)(7) and is designed to invest primarily in employer stock and that identifies the plan sponsor as being either a C-Corporation or an S-Corporation, as well as provisions addressing and adequately meeting each of the following items:

- Defining employer stock in accordance with Sections 409(l)(1) or -(2)
- Appropriate diversification requirements
- Appropriate valuation, independent appraiser, and allocation of earnings requirements
- Voting requirements
- The right to demand upon distribution that the plan buy back stock for which there is no public market
- Multiple distribution requirements
- Exempt loan requirements
- ESOP annual addition requirements
- Certain other requirements enumerated in the Revenue Procedure

Sections 6.03(4) and -(5) of Rev. Proc. 2015-36 set forth the specific areas for which opinion letters will and will not be issued for ESOPs. For purposes of Rev. Proc. 2015-36, ESOPs are considered to be “nonstandardized” plans.

For a more thorough discussion of the scope of Rev. Proc. 2015-36, as well as its many limitations, please see *ASPPA asap*, No. 15-11, June 14, 2015 (“IRS Expands Pre-Approved Plan Program to Include Cash Balance Plans and ESOPs”).

IS AN ESOP FOR YOU?

As discussed, ESOPs can be strong tools for business succession planning. In addition, multiple studies have pointed to productivity gains and increased employee involvement and job satisfaction in conjunction with establishment of an ESOP.

Some of the uses identified by the NCEO for an ESOP include:

1. *To buy the shares of a departing owner.* Owners of privately held companies can use an ESOP to create a ready market for their shares. Under this approach, the company can make tax-deductible cash contributions to the ESOP to buy out an owner's shares, or it can have the ESOP borrow money to buy the shares (see below).
2. *To borrow money at a lower after-tax cost.* ESOPs are unique among benefit plans in their ability to borrow money. The ESOP borrows cash, which it uses to buy company shares or shares of existing owners. The company then makes tax-deductible contributions to the ESOP to repay the loan, meaning both principal and interest are deductible.
3. *To create an additional employee benefit.* A company can simply issue new or treasury shares to an ESOP, deducting their value (for up to 25% of covered pay) from taxable income. Or a company can contribute cash, buying shares from

Certain tax friendly characteristics, as well as their utility as a business transition strategy, are currently being rediscovered by many companies and business owners.”

existing public or private owners. In public companies, which account for about 5% of the plans and about 40% of the plan participants, ESOPs are often used in conjunction with employee savings plans. Rather than matching employee savings with cash, the company will match them with stock from an ESOP, often at a higher matching level.⁹ **PC**



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⁹ <http://www.nceo.org/articles/esop-employee-stock-ownership-plan> (as accessed May 12, 2016).



Making Participants Out of Employees Via Eligibility

A strategic approach to defining eligibility provisions in 401(k) plans can boost take-up rates.

BY NOAH BUCK

As consultants to our plan sponsor clients, we are often asked for guidance on plan design. In the last decade, plan design discussions on 401(k) plans have often centered on automatic plan features, which is due to the higher participation and savings rates they create for our clients' workforces. But beyond the hype of automatic plan features, there are other topics within plan design — sometimes overlooked — that are meaningful and impactful to participants and plan sponsors. One of those topics is plan eligibility.

The eligibility rules of a 401(k) plan have significant implications for plan sponsors. These rules can affect benefit costs, talent recruitment and retention, administrative complexity and plan compliance. As consultants, we can help plan sponsors take a strategic approach to defining eligibility provisions in their 401(k) plans, with consideration given to various plan objectives and statutory requirements.

THE PARAMETERS

It's typical for plan sponsors to define the eligible population as their common law workforces, with specific provisions to exclude certain employees such as nonresident aliens with no U.S.-source income, union or nonunion employees, commissioned employees or leased employees. Plan sponsors may also exclude certain job categories as long as these provisions are not a means to sidestep the minimum statutory age and service requirements outlined below. A plan's eligibility rules are subject to coverage testing under Code Section 410(b) to ensure they are not discriminatory against non-highly compensated employees.

In general, a qualified 401(k) plan's eligibility rules cannot be stricter than the minimum statutory requirements in the Code, which are age 21 and one year of service. A plan can always be more liberal than these minimum statutory requirements. For example, a plan can set eligibility requirements at age 18 and no service requirement.

The year-of-service requirement can be based on elapsed time or it can be hours-based. If hours-based, the plan sponsor can require an employee to work as many as 1,000 hours in a 12-month period in order to satisfy eligibility. Section 410(a)(4) mandates that plan sponsors allow these employees to enter the plan no later than the earlier of: (1) the first day of the plan year following the satisfaction of eligibility; or (2) six months following the satisfaction of eligibility.

Under the aforementioned parameters, the longest a plan sponsor can typically make an eligible employee wait to satisfy eligibility and enter a plan is between 12 and 18 months. Consider the following extreme example: John Doe works for a company that requires a year with 1,000 hours of service before entering on the first day of the subsequent plan year in January or six months later in July. He is hired in January 2015 and works 1,000 hours in his first 12 months. John enters the plan in July 2016, or approximately 18 months after he was hired.

STRATEGY

To what degree is the plan used to attract and retain talent?

A law firm does not want highly sought-after recruits joining a competing law firm down the road because they can enter the competing firm's retirement plan sooner.

Employers relying partially on their 401(k) plans for recruitment should consider that quicker and easier access to the plan will be more attractive to those in their prospective talent pools.

Are eligibility and entry date provisions cost-efficient with respect to turnover and vesting?

An organization's turnover rate and average employee tenure are important to consider. A restaurant chain employing high-turnover wait staff will save cost and administrative energy by requiring employees to work six months before entering the plan instead of requiring one month.

It's also important to consider the plan's vesting provisions. If the plan has immediate vesting, the employer matching contributions — meant to supplement long-term retirement savings — could be going right out the door to short-term employees who are allowed to enter the plan too quickly. Employers should consider structuring eligibility and plan entry provisions so employer contributions are more likely to stay in-house with longer-term employees.

What's the best enrollment experience for employees?

Aside from the actual benefit provided to employees, an organization can also be strategic with its enrollment experience. It can be difficult to engage employees on their benefits. An organization may want to take advantage of the employee engagement that exists when new employees are signing up for other benefits, and align the 401(k) eligibility provisions accordingly. If newly hired employees sign up for medical, dental, life insurance and other benefits within the first few

weeks of employment, it may be easier for them to elect a savings rate in the 401(k) plan at the same time. Employees asked to satisfy a longer 401(k) eligibility requirement may no longer have benefits at the front of their minds a few months down the road.

The enrollment experience needs to be carefully considered by organizations using automatic enrollment. Specifically, your clients may find it prudent to enroll employees after at least one to three months of service. This cushion of time allows plan communications and education to take hold with employees, and it affords them a reasonable opt-out period. Employees being automatically enrolled too quickly may feel rushed, and — if it's an eligible automatic contribution arrangement (EACA) plan — may request refunds.

How easy is the administration?

Administrative errors in a 401(k) plan can be costly to our clients, and for that reason there's value in keeping the rules clear and simple. Plan sponsors should avoid gray areas or knowledge gaps with respect to the administration of eligible employees. For example, if hourly employees are excluded from the plan, can the organization's recordkeeper or payroll team clearly identify the hourly employees? Automated processes to assign eligibility based on clear and consistent data are preferable to manual processes that are prone to oversight.

Are dual eligibility provisions a good fit?

An organization may want to let some employees enter the plan right away, but require others to meet a more stringent eligibility requirement (assuming coverage testing will pass). For example, an organization with both salaried and hourly employees might require hourly employees to fulfill a longer eligibility period if this category of employees has a higher turnover rate or shorter average tenure.

Similarly, a plan sponsor may allow immediate plan entry with respect to 401(k) deferrals, but assign a longer eligible period for employer matching contributions. Some plans with immediate vesting can extend the eligibility period for employer contributions for as long as two years.

Will the plan pass coverage testing?

Some exclusions do not affect coverage testing, such as the exclusion of those not meeting the age and service requirements, nonresident aliens, union employees and some newly terminated employees. However, it's important for our clients to tread carefully when venturing outside of these standard exclusions or when setting up dual eligibility provisions. For example, an exclusion of a certain job category (e.g., "hourly employees," or "employees working in the Atlanta office") can cause the plan to fail coverage testing, resulting in corrective contributions to the plan. Nondiscrimination testing should be completed each year to validate a plan's eligibility provisions, and projected testing is recommended ahead of significant plan design changes.

CONCLUSION

Plan eligibility provisions within 401(k) plans can have a significant impact on our clients and their employees. Injecting strategy into this area can help our clients contain benefit costs, recruit and retain talent, simplify administration, and stay in compliance with the law. **PC**



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Tech Solutions the Key to TPAs' Future

It's up to TPAs to invest in technology that will increase margins by creating the solutions advisors want and need to be successful.

BY DAVID J WITZ

Historically, recordkeepers, not TPAs, have held a leadership position in technology deliverables that are provided to plan sponsors, participants and advisors. The expectation, especially from advisors, for new disruptive and/or sustaining innovation has not changed despite continuing fee compression, litigation risks, and now the new conflict-of-interest rules from the Labor Department.

Today, however, there is a growing reliance on TPAs to deliver more technology-driven solutions that enhance an advisor's ability to win new clients and keep existing ones. This is a high-cost proposition that squeezes profit margins for small TPAs at a time when fee compression has already cannibalized revenues.

Fortunately, large bundled service providers, which in many cases also collaborate with TPAs, have invested significant capital in technology solutions that help their small TPA partners. But those solutions also enhance their ability to win direct business, giving them an unfair competitive advantage with advisors that sell retirement plan solutions. Bundled providers benefit from economies of scale that enable them to spread their technology costs

over a larger base of participants. This results in a cost per participant that no bundled daily valuation recordkeeper can match.

In addition to this competitive advantage, consider that many bundled providers are also product manufacturers that draw additional revenue from proprietary or sub-advised investment options — revenue that may be deployed for technology enhancements. Although TPAs are not product manufacturers, they have enjoyed the benefits of receiving a portion of the asset-based fees charged by recordkeepers in the past. But this is quickly disappearing as the market demands pricing that is not linked to plan assets for administrative services.

DATA THE KEY

The critical question for TPAs to address today is: "What action must I take now to remain relevant five years from now?" The bundled providers with whom they collaborate and compete are taking action today that reveals what they believe they must do to stay relevant in the future. Their action plan includes:

- acquisition;

- heavy investment in new proprietary and non-proprietary technology; and
- dedication to a multi-revenue solution platform that includes proprietary and sub-advised investment options.

In today's ever-changing retirement industry, the strong will survive and flourish. However, survival is dependent on distribution, and distribution is dependent on unfair competitive advantages in the mind of the advisor — advantages created with substantial capital resources that TPAs do not have.

However, there is a silver lining: data. A local TPA has data on plans that others don't have — data that is valuable and that can be monetized to create reports that provide documentation to support procedural prudence and fiduciary governance, impact outcomes, assist with plan design — and that, when monetized, encourages advisors to stay loyal.

BUYING CONSORTIUM

Of course, few TPAs can afford the price tag of building the technology for proprietary purposes. Instead, a TPA's survival is dependent on "co-opetition," a neologism coined to describe cooperative competition (sometimes called "coopertition" or "co-opertition"). In other words, a TPA with a small technology budget can create an equally impactful result if the budget of multiple TPAs is combined into a buying consortium.

A buying consortium provides a TPA with the ability to build a suite of technology solutions it could not afford to build or support on its own. Bottom line: The current environment of fee compression that squeezes margins, combined with the high cost of innovative cutting edge technology solutions, encourages collaboration between competitors who wish to protect their business valuation and remain relevant in the future. It also provides a TPA a way to monetize its storehouse of information and knowledge.

Of course, as with any technology initiative, early adopters that embrace the initiative to stay relevant will profit the most. Late adopters will either pay a premium to jump on board after the fact or be locked out altogether due to limitations on the number of participating TPAs established by the consortium.

An integrated technology platform of multiple solutions will assist the consortium with winning the loyalties of their distribution channel by supporting their consulting engagements with clients and prospects. Technology that wins distribution loyalty is technology that adds value and improves margins.

GENERATIONAL COMMUNICATION ISSUES

TPAs that embrace this new paradigm will need to be mindful of how they roll out the new technology solution. The communication approach must be structured to address what remains of the Baby Boomer generation while appealing to the predominant Gen X and Gen Y workforce — the generations that are today's emerging decision makers and fiduciaries. Failure to consider the generational differences is a quick way to lose opportunities. If you are willing to invest in technology with the intent of capitalizing on new, cutting edge deliverables that win distribution and customer loyalty, you cannot ignore the messaging. It must resonate with the preferences of each generation as both customers and distributors of your services.

While the future is yet to be written, certain trends are undeniable. The big are getting bigger and the small are not growing (or their growth is marginal). And while advisors are a distribution channel to be coveted, they don't want to spend their money. (This is especially true for dabblers.) It will be up to a TPA to take a leadership position and invest in technology that will increase margins by creating solutions advisors want and need to be successful.

More importantly, it will be the technology solutions that build loyalty with advisors. The solutions that have been identified as especially important to advisors include data integration, prospecting tools, proposal generators, plan features analysis, plan design tools, benchmarking, investment monitoring, fiduciary and participant online education, and model creation and monitoring.

Developing new technology that will support the advisor's ability to stay focused on business development, client relationships and vendor management will give TPAs a shot at more opportunities to build their business valuation and achieve the success they covet. But the clock is ticking, and the door of opportunity is closing.

The DOL's conflict-of-interest rule has created a clear path to writing IRA rollover business while also being a plan-level fiduciary. That is an impetus for new technology to support what could be an army of dabblers that become fee-based Series 65 RIAs now that the rule has been finalized. A TPA that has tools in place to support this new paradigm is in the best position to build scale quickly. Time will tell which TPAs are left behind, but my tea leaves say it is the late adopters of new technology. **PC**



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Believe it, or Not

Just about every ASPPA member has a favorite client story. Some are funny; others are heartwarming. And some just make you scratch your head and wonder. Back in April we set up a secure web form and asked members in an *ASPPA Connect* post to share their favorite — anonymously, of course. Here are the results. Enjoy!

THE SHOEMAKER'S CHILDREN

I was attempting to guide my client (via the phone) through logging into our sponsor website. He kept insisting the button I was telling him to click on wasn't on his screen. I asked him to send me a screenshot so I could assist him better.

He took a picture of his computer screen with his cell phone and texted it to me. When I looked at the picture, his mouse was pointed to the button he insisted wasn't there.

This man owns a tech company.

COOKIES!

Many years ago, I received a box of homemade cookies in conjunction with a request for benefits. The terminated participant assumed the withdrawal process would be time-consuming and she wanted to speed it up by enticing our office with her delicious oatmeal cookies!

ISN'T CATCH-UP A CONDIMENT?

Reconciling a takeover plan and discovered a discrepancy between reported contributions and plan assets. Further investigation revealed that although the catch-up contributions were withheld and labeled in the payroll reports as “catch-up,” the client only deposited the amounts

reported as “salary deferral.” This occurred over a period of five years! The good news: It only involved two employees, and the total correction with interest was approximately \$42,000.

Thank goodness for VFCP.

THE MR. MAGOO WORKFORCE

I once had a sponsor request all documentation be in 12 point type or larger because “our employees are old and probably can't see worth a darn!”

DULY NOTED

Back in the days when handwritten notes and paper were the norm, a client sent in an end-of-year census and indicated a participant was deceased. The client apparently felt the need to write in the margin that the former participant had been decapitated — by a shovel. The plan sponsor was a hardware store.

DOES THAT HURT?

Cause of death listed on a death certificate sent by a client: “metabolic derangement.”

CHARGE IT!

Once had a fellow TPA crowing to me at a vendor dinner about how he had this great idea to offer a no-annual-fee credit card to employees who enrolled in “his” 401(k) plans. When I told him that he would disqualify every plan he worked on with his great idea, he actually remained quiet for the rest of the dinner.

BAD PENNY

Had an “opportunity” offered to my company to work on a plan with an investment that seemed

ASPPA members share some of their favorite client stories.

BY JOHN ORTMAN

(to me, at least) to be a prohibited transaction — a complex web of poorly-documented/shady loans and withdrawals that involved an investment in a church in Africa. Over the salesman's strenuous objections, we passed on the case. Two years later it was submitted for review again — this time with a fresh DOL penalty letter for the prohibited transaction.

KEEP OUT: THIS MEANS YOU

Our business is located in North Carolina, where we don't get much snow. However, when it does snow we usually close all businesses for a day or two, stay off the roads and buy all the milk, bread and water at the grocery store! A few years back we had an epic snowstorm that left us with about two feet of snow. Needless to say, the entire state was under a state of emergency. I live just a few miles from my office, so I drove over just to make sure everything was buttoned up, change the phone message, etc. While sitting at the reception desk, I see a client of ours walking up to the door. So I went to greet him at the door and joked, “You can't possibly have a pension emergency?!” Well, he felt he did. He wanted to be sure to hand deliver his and his son's beneficiary forms to our office. They were very important, he informed me, as they named each other as the other's beneficiary in order to “keep the outsiders out” of their retirement assets. “Outsiders?” I asked. He stated that would be their wives! **PC**

Welcome



New & Recently Credentialed Members!

MSPA

John Bury
Frank Svrcek

CPC

Jeremy Lackey

QPA

Scott Adams
Cindy Banta
Carolyn Hawks Bates
Jeremiah Bolinsky
Tami Bowder
Marianne Fanning
Sherry Gengler
David Gossett
Jason Grant
Theresa Greco
Constance Haugen
Stefanie Hensler Ring
Joel Howell
Glendon Hughes
Amanda Johnston
Kirstyn Jones
Jennifer Keller
Drew Kreigline
Karen Kurtzke
Michael J. Lee

Jone Liuzza

Edith Lopez

H. Lyons

Joshua Martin

Kristi Morhidge

Tracy Novak

Morgan Paige

Beth Pearce

Christina Poteet

Whitney Rader

Dianna Ray

Timothy Sanborn

Mindy Santan

Michelle Siewell

William Walther

Jeremy Yang

Jacqueline Zerbey

QKA

Scott Adams

Michaela Bauza

Jeremiah Bolinsky

Chris Ciminera

Gail Cowlin

Shawna Della

Tara Farmer

Danielle Hoppman-Koch

Michael Jageler

Rich Johnson

Kirstyn Jones

Drew Kreigline

Philip Miley

Michael Montchyk

Kristi Morhidge

Peter Padilla

Anthony Petri

Caryn Potere

Evan Rentschler

Gavin Saine

Bert Saveriano

Jonathan Schmeidler

Michael Spear

Maureen Verzi

Robert Vick

Brian Ward

Dawn Wesley

Linda Widger



R P F

ASPPA Education: What Does It Mean to You?

In their own words, here are the perspectives of two members who completed the RPF Modules recently.

BY JOHN T. WEBB

One of the goals of ASPPA has always been to provide extensive education opportunities. For me, ASPPA credential programs are a sense of personal accomplishment. When I started in the industry, I did not know anything about pension plans, not to mention “401(k).” Little did I know, this would be my career path for more than 19 years.

ASPPA played a key role in my understanding of retirement plans. I remember that one of my first managers encouraged me to take the Pension Administrator (PA) program, now known as “Retirement Plan Fundamentals.” From there I continued further by passing the DC-1 and DC-2 exams, then gaining the QKA, ERPA and TGPC credentials.

I had no clue at that time the doors it would open for me, not just of personal knowledge and growth but also my career. Reflecting back on my early years, I continue to follow in the footsteps of my manager and encourage others to continue their professional growth by obtaining an ASPPA certificate or credential.

As ASPPA celebrates 50 years, we wanted to take a look at how ASPPA education has served those in the industry at different stages of their careers. We asked Deborah Aboudara, CPC, QPA, and Beth Parker, who recently completed the new RPF Modules, to share their ASPPA education experiences.

DEBORAH ABOUDARA

Tell us a little bit about yourself and how you arrived at your current position.

I was a stay-at-home mom in my late 30s, and decided to go back to work in the accounting field. Stumbling into our field quite by accident, I worked for several small administration firms scattered throughout the country — they supported my desire to learn more. I now own my own pension administration firm in North Carolina.

How did you first hear about ASPPA?

My ASPPA education started with my mentor, who told me that ASPPA credentials would be perfect for me, particularly since I wanted to continue in the field after moving my family from Chicago to Southern California. Our family moved around a lot and I also saw the benefits of owning portable credentials. ASPPA credentials belong to you. You own your credentials. But take it one credential at a time.

What was your experience like studying for ASPPA's credentials?

Having a mentor is advantageous, because otherwise, it's very lonely studying for the exams. Rising early in the morning before the family was up, I read and studied (from the syllabus) one hour each morning at the kitchen table. I even took *The ERISA Outline Book* and had a printer slice the books up into manageable pieces. I put the "Outline" in slim, 3-ring binders, and read from them on the treadmill at the gym.

I embraced the possibility of an ASPPA weekend crash course. I saved my money to travel to the venue of the weekend crash course, say, for the QPA exam, after which I could return home to focus on my identified weak spots. I will never forget the weekend course in Philadelphia, where instructor Chuck Klose, on his knees, pleaded in earnest that each of his pupils understand cross-testing. ASPPA instructors dearly want you to succeed.

How do you see yourself involved in ASPPA education in the future?

The learning never stops. I have volunteered to help edit workbooks, edit exam questions, and grade exams. I have worked with people from all over the country, and each person I have met through ASPPA is as invaluable as a gold thread connected through a finely woven piece of cloth. How could I not learn more?

What advice would you give someone new to ASPPA education?

Your time and resources are valuable and it's up to you to manage your unique road to reach your goal. It takes some careful planning, much time, energy and dedication, but you can do it!

BETH PARKER

Tell us a little bit about yourself and how you arrived at your current position.

It has been said of our industry, that no one takes a direct route into becoming a retirement plan professional. With a marketing degree and diverse accounting experience,

I began my career in the pension industry on the operations side with Pentegra Retirement Services. My current position is as an internal sales consultant.

How did you first hear about ASPPA?

In my first week of work, I asked my co-worker, "What does 'QKA' mean after your name?" I quickly learned that ASPPA is the foremost education platform for the pension industry. It is hard to explain how complex and all-encompassing the pension business is to someone outside of the pension world. The task to acquire the vast amount of required knowledge can seem disconcerting. I was assured that ASPPA had a myriad of resource materials to help me achieve the needed level of mastery.

Describe your educational experience.

This past fall, I was extremely privileged to have been selected to take part in a beta testing program for the RPF Certificate. This newly redesigned certificate program, replacing RPF-1 and RPF-2, is the gateway to obtaining QKA credentials. I was beyond elated to discover the depth of resources made available online as I worked my way through the six modules. Each module had a pretest that gave you your results and an explanation of any question that was missed. After the pretest there were sections of reading followed by quizzes that mirrored the data and included helpful hints.

What impact did ASPPA education have on your career?

The Girl Scouts have the motto: Be Prepared. In all facets of business, to be effective in your job, it is essential that you be prepared. What I have experienced thus far with ASPPA education has helped to prepare me to do a better job every day. As a woman in a predominantly male profession, it is important for my success to know all I can, and ASPPA provides that critical support. With the additional confidence and my acquired knowledge through my ASPPA education, the future is limitless.

How do you see yourself involved in ASPPA education in the future?

Since my experience with ASPPA education has been so positive, I am excited about my future as I strive to obtain my QKA credential. The extensive knowledge I will accumulate as I progress through the credential programs will drive my success in my chosen career field in the pension industry.

WHAT ABOUT YOU?

Most of you have a story about ASPPA educational opportunities and how they have affected your career. ASPPA is always reviewing its programs, making them more accessible and reacting to government and industry changes. While the programs evolve, ASPPA's commitment to education has not changed over the past 50 years.

There are many opportunities for volunteering with ASPPA education. These programs exist because of you and your support. I will never forget that manager who encouraged me to pursue a credential — it was transformational! By encouraging someone to pursue a credential, you may never know how it will affect their career growth in the retirement industry.

To find out about more ASPPA education offerings, visit asppa-net.org/education. And for volunteer opportunities, check out asppa-net.org/membership/volunteer. **PC**



John T. Webb, ERPA, QPA, QKA, CPFA, TGPC, is the manager of the ERISA Technical Team at

Nationwide. He serves on ASPPA's Academy Advisory Group and was the past vice co-chair of the membership committee. At Nationwide, John is the coordinator of the QKA program with 34 Nationwide associates successfully meeting the requirement for the QKA during 2015.



ETHICS



Courtesy and Professional Conduct

The ARA code of professional conduct recognizes that clients are best served when ARA members conduct themselves like the courteous professionals they are.

BY LAUREN BLOOM

The election season is upon us. For the past several months, voters nationwide have been treated to the spectacle of politicians vying to secure their parties' nominations for offices at every level from the presidency to local government. In an effort to distinguish themselves from their opponents, some candidates initially took the "high road," touting their own accomplishments and plans to address a wide variety of pressing issues rather than attacking their opponents. But as the months ticked by, the fields narrowed and convention delegate counts began to solidify, the tone of debates, town meetings and candidate rallies became increasingly rancorous. Names were called, accusations were made, candidates' integrity and judgment were questioned, and unflattering photos were tweeted. Eventually, enough mud was slung that hardly any of the would-be nominees could emerge entirely unsullied from the primary process.

Pundits from both sides of the aisle have warned repeatedly that negative campaigning has serious consequences. It generates bad feeling, tempting voters whose first-choice candidates didn't win the primaries to stay home when the

time comes to vote in the general election. Candidates who indulge in name-calling and mudslinging look far from statesmanlike. Worst, negative comments from opponents in one's own party during the primaries can be used to devastating effect by the other side in a general election. But despite these obvious drawbacks, candidates continued to slam their opponents, apparently believing that the benefits of negative campaigning outweigh potential consequences.

What if those candidates were employee benefit plan professionals?

The similarities between ambitious politicians and American Retirement Association members may not be immediately obvious. However, the two groups have important traits in common. Politicians running for office are trying to persuade their constituents — *i.e.*, their customers — to elect or reelect them as public employees. ARA members, if they want to continue working in the employee benefits field, are constantly seeking to persuade their clients — *i.e.*, their customers — to retain their professional services. Both groups face fierce competition that can quickly turn ugly if not thoughtfully managed. And ARA members, like political candidates, can harm their professional standing if they indulge in slurs against their competition.

The ARA's Code of Professional Conduct speaks briefly but compellingly to this point. Precept 8 of the Code requires ARA members to provide professional services "with courtesy," and to "cooperate with others" in the interests of their clients. The specific parameters of these requirements depend on the circumstances around a particular engagement. Still, Precept 8 states that ARA members have an obligation to behave politely when providing professional services.

The ARA member's duty of courtesy can arise in several contexts. For one, ARA members are rarely a plan's sole consultant. Let's say, for

An ARA member who represents clients before federal agencies may be tempted to fly off the handle from time to time."

example, that an ARA member who is an investment advisor believes that a client is getting inaccurate or incomplete information from its outside legal counsel. The ARA member can, and probably should, express that belief to the client. Under Precept 8 of the Code, however, the ARA member is wise to state that opinion without becoming accusatory, hostile or sarcastic.

Similarly, an ARA member may believe that a plan sponsor or administrator is about to engage in a foolish or risky action with respect to a plan. The ARA member is wise to call the proposed action into question, and to recommend a better alternative. Again, though, Precept 8 urges the ARA member to maintain a civil demeanor when doing so.

Additionally, an ARA member who represents clients before federal agencies may be tempted to fly off the handle from time to time. An interpretation of ERISA and its regulations that seems perfectly reasonable to the ARA member may meet with unyielding opposition from government representatives. In such a situation, Precept 8 recognizes that the client is ill served if the ARA member gets into an ugly argument with the authorities.

Another situation that can severely test an ARA member's civility is being replaced by another employee benefits professional. As Precept 8 recognizes, a client has

an "indisputable right to choose a professional advisor," which means that the client has an indisputable right (subject to legal and contractual limitations, of course) to replace an ARA member with a competitor. When that happens, the ARA member is likely to be hurt, angry and inclined to argue. Nonetheless, Precept 8 calls upon the ARA member to accept the termination like an adult, without lashing out at the client or the new advisor. (Precept 8 also addresses transition of work papers and plan documents when an ARA member is replaced, but that's a subject for a separate article.)

ARA members may also be tempted to behave discourteously when striving to win a plum assignment or a new client. Just like an ambitious politician, the ARA member may get so caught up in the competition that the impulse to criticize other employee benefits professionals becomes overwhelming. In such a situation, however, Precept 8 urges the ARA member to focus on touting his or her own professional strengths and services, rather than disparaging the competition.

Precept 8 doesn't require ARA members to bite their tongues or decline engagements just because another consultant expressed a differing opinion or previously served a client. Rather, Precept 8 recognizes that clients are best served when ARA members conduct themselves like the courteous professionals they are.

In this heated election season, political candidates might be smart to adopt Precept 8 themselves. A civil candidate is likely to make a better leader. **PC**



Lauren Bloom is the general counsel & director of professionalism, Elegant Solutions Consulting, LLC, in Springfield, VA. She is an attorney who speaks, writes and consults on business ethics and litigation risk management.



Retirement Plan Education, In-House Style

Good ideas can start with just one dedicated and creative person — and employer buy-in.

BY JOHN IEKEL

“Physician, heal thyself.” That Biblical maxim can be applied in other contexts as well. How about, “Teacher, instruct thy peers”? One teacher in Baltimore is following that advice by teaching his colleagues about retirement saving through a program of his own genesis.

It’s a success story that exemplifies how good ideas — and the initiative and drive to take a positive action to increase understanding of, and participation in, retirement saving programs — can start with just one dedicated and creative person. And it all shows what can happen when an employer not only buys in, but also creates and sustains an environment where such a thing can happen.

The employee retirement plan education program at Gilman School, a private K-12 institution in Baltimore, Md., is the brainchild of Sean Furlong, its director of finance and administration. The idea occurred to him while he was presenting material to students about budgeting and handling finances, including retirement plans.

Furlong pitched the idea of providing Gillman faculty with in-house education about retirement plans and saving to the school’s administrators, whom he says were very receptive. “Retirement education is part of the school benefits program now,” Furlong notes.

“Our goal from the presentation is to help our employees become aware of what they need to put aside for retirement (via education and presentations), then encourage them to put that away prior to signing up for annual benefit renewal,” says Furlong. “Then once invested, make sure our employees have solid investing options at the lowest cost possible.” Finally, he says, they seek “to educate our employees on overall financial planning, above and beyond retirement planning.”

“I absolutely feel education of employees on retirement is critical,” Furlong asserts.

NUTS AND BOLTS

So what does the program entail?

Participation in Gilman's retirement plan is mandatory. "We make it mandatory that all employees put aside 5% of their pay, which will receive a 6% match from Gilman. Then we offer 1:1 contribution for, and dollar put in above, 5% up to 7%. So if an employee puts in 7%, they get an 8% match," Furlong says. The materials presented to Gilman employees through the program report that Gilman School's average contribution to retirement plans is 4.1% higher than those of employers with plans of similar size.

The program has many facets, including:

- presentations to all employees at once (done at least once a year for the last 5 years);
- ongoing online opportunities to learn through Financial Finesse — access to tools, articles and presentations on any financial topic of interest or concern;
- articles sent to all employees on current topics relevant to retirement readiness;
- seminars once a year on various topics; and
- once-a-year presentations to employees before annual benefits elections on the benefits and importance of saving more.

The materials presented to employees use graphics to reinforce the premise that it is beneficial to start saving as early as possible. For instance, assuming a \$3,000 annual investment with 6% annual growth and reinvestment of all plan earnings with no taxes imposed, it tells participants that their retirement accounts would amount to the following by age 67, based on when they start saving:

- age 20: \$679,500;
- age 35: \$254,000; and
- age 45: \$120,000.

The materials also use examples to illustrate the difference a seemingly small increase in the deferral rate can make for a participant. For instance:

- Age: 45
- \$50,000 annual salary
- Defers 5% into the retirement plan
- Assume a 7% annual rate of return
- At age 65 (20 years) has \$102,488 in his retirement account

Same participant with one small change:

- Age: 45
- \$50,000 annual salary
- Defers 6% into the retirement plan (only \$19.23/paycheck)
- Assume a 7% annual rate of return
- At age 65 (20 years) has \$122,986 in his retirement account — a difference of \$20,498 for just a small tweak to the deferral rate

The materials also use illustrations to convey:

- suggested retirement savings targets as a multiple of annual income, by age from 35 to 67;
- how investments can grow over 25 years at a salary of \$30,000, \$50,000 and \$75,000;
- the benefits of investing retirement funds as early as possible;
- the consequences of not saving enough and not starting retirement saving early enough;
- advice older workers give to younger workers about saving for retirement; and
- how one can spend less in order to save more.

Attending an initial one-on-one session is mandatory, too. But while all employees are required to attend those initial sessions, participation in the education program is not mandatory.

The seminars offer employees flexibility; Furlong notes that employees have a choice of different seminars. For instance, he says, Gilman offered one last year for employees getting close to retirement on Social Security claiming options and the potential impact of those decisions.

RESULTS

Has the program motivated participants to change how they save for retirement?

"We feel we have had an impact," says Furlong. "Our overall savings rate has gone in 5 years from approximately 16% to approximately 22%."

The program materials back Furlong's assessment. They say that the overall average retirement plan contribution rate increased by almost 1 percentage point to nearly 10.2% from 2012 to 2013, and that among the employees who changed their contribution rate, the average increase was 2.03%. The Gilman School's average deferral is 13%, with a match of 8%.

Gilman's plan compares well against other plans, too, with an average contribution 4.1% higher than similarly sized plans.

The Gilman plan argues in favor of investing in target date funds. Says Furlong, "the number of participants in target date funds is close to 85%, which we prefer to individual choices folks used to make in past (for instance, they could invest their retirement funds wholly in stocks, bonds, commodities, etc.). We were merely providing options without education. Through education, we feel the target date funds are perfect for our employees who tend to not look at their portfolios much and who are not in the investing business (so concepts of rebalancing, asset allocation, reducing risk as you approach retirement are not as prevalent in our culture)," he adds.

Employees paid attention: investments in TDFs amounted to 2.3% of the assets in the plan before the program was instituted; now they stand at 87.15%.

So what do employees say about it?

"We have found that our employees close to retirement are very appreciative of the work we have done. In fact, when we present to other employees we occasionally have a teacher close to retirement who will choose to provide additional comments about the importance of what we are doing and the terrific benefit it is," says Furlong. **PC**



GAC Update

BY CRAIG P. HOFFMAN



Cross-Testing Proposal Withdrawn

April action by the IRS marked a significant victory for ASPPA.

On April 14, the IRS and Treasury Department withdrew a regulatory proposal that would have been very detrimental to the formation and maintenance of retirement plans by small businesses. ASPPA’s Government Affairs Committee and the ASPPA members who participated in our campaign to quash the proposal were the primary reason the regulation was withdrawn. This was a significant victory for ASPPA, its members and the plan sponsors with whom they work.

To better understand how important this issue was to our membership, a review is in order. On January 29, the Treasury Department and IRS proposed a regulatory change to the general nondiscrimination test used by most cross-tested defined contribution plans. The proposal immediately caused alarm bells to go off within the ranks of ASPPA’s Government Affairs Committee. This was due to the fact that it had the potential to significantly increase the employee costs of some of the most popular DC plan designs being used today. This, in turn, could have led some employers to terminate their plans and caused other employers to forgo adopting a plan.

The proposed regulation would have added a new requirement to “rate group testing” under the general test for nondiscrimination. Specifically, a rate group would not have been able to pass the average benefit test unless “The formula that [was] used to determine the allocation for the HCE with respect to whom

the rate group [was] established applie[d] to a group of employees that satisfie[d] the reasonable classification requirement of §1.410(b)-4(b).”

Many plans, as currently structured, would not have been able to satisfy this requirement. This is because it is *per se* an “unreasonable” classification if the criteria used to determine the allocation group to which the formula applies is based on a person’s name or criteria having substantially the same effect. For example, a plan which places each employee in a separate allocation classification or group would not have been able to satisfy the requirement.

The ASPPA Government Affairs Committee, on behalf of the ASPPA membership, raised serious concerns about the proposal:

- The proposal introduced a “facts and circumstances” test, with related uncertainty, into a nondiscrimination system that has been purely numerical for over 20 years. Is a classification that describes just one employee equivalent to enumeration by name? What about two employees? There is no way to know before the plan is under IRS audit.
- The proposal unfairly burdened small employers, who face added uncertainty because of the likelihood of having very small groups.
- To the extent an employer would be forced to use the ratio percentage test, rather than the average benefit test, this would raise costs to cover employees. For over a decade cross-tested plans have provided minimum gateway contributions,

a systematic approach which over time can give an employee generous retirement benefits.

ASPPA GAC raised these concerns in several meetings with IRS and Treasury Department officials. We also reached out to members of Congress to explain how detrimental the proposal would be for small businesses. And we set up a website so that our members and their plan sponsor clients could easily express their views on the harm this proposal would have caused to the formation and maintenance of qualified retirement plans.

This multi-faceted campaign paid off. IRS Announcement 2016-16 formally announced the withdrawal of the offending portion of the proposed regulation. According to the Announcement, the Treasury and IRS “have given additional consideration to the potential effects of the proposal ... on the adoption and continued maintenance of qualified retirement plans ... and have concluded that further consideration will be needed with respect to issues relating to those provisions.”

The Announcement affirms that ASPPA’s message was heard and resulted in the proposal being withdrawn. It remains to be seen if it may return in some different form. If so, ASPPA GAC will continue to advocate for a private retirement system that encourages the formation and maintenance of qualified retirement plans. **PC**



Craig P. Hoffman, APM, is General Counsel for the American Retirement Association.

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