Dopkins & Company, LLP
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

EMPLOYEE BENEFIT PLANS

AN UPDATE ON INDUSTRY DEVELOPMENTS

2019 Issue 1

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Changes to IRS Determination Letter Program

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Internal Revenue Service (IRS) Revenue Procedure 2019-20, which is effective September 1, 2019, most notably provides for a limited expansion of the determination letter program with respect to individually-designed benefit plans. Previously, Revenue Procedure 2016-37 eliminated the ability for these types of plans to obtain periodic determination letters from the IRS, and as a result, placed responsibility for ensuring that plan documents are updated to remain in compliance with revisions to the Internal Revenue Code (the Code) entirely on plan administrators. However, with the limited expansion provided by Revenue Procedure 2019-20, the IRS will now accept determination letter applications for individually-designed hybrid plans that combine features of both defined-contribution and defined-benefit plans during a 12-month period beginning September 1, 2019, as well as for individually-designed merged plans on an ongoing basis. Plan sponsors continue to be permitted to submit a determination letter application for initial plan qualification and for qualification upon plan termination.

To assist sponsors of individually-designed plans to ensure that all required amendments to plan documents are made, the IRS continues to publish a required amendments list on an annual basis (see https://www.irs.gov/retirement-plans/required-amendments-list). It is important that that administrators and fiduciaries of individually-designed plans monitor this list, as the IRS regularly issues notices requiring amendments to certain benefit plan documents.

The determination letter program remains available for pre-approved plans submitted for approval by providers or mass submitters. One way sponsors of individually-designed plans can mitigate the risk of noncompliance with the Code is to switch to using a pre-approved plan document. In an effort to encourage plans to use pre-approved plan documents, the IRS issued Revenue Procedure 2017-41 in June 2017. This revenue procedure increased the types of plans eligible for pre-approved status and allows greater flexibility in the design of pre-approved plans.

Changes to Hardship Withdrawal Restrictions

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Regulations issued by the IRS have clarified new hardship withdrawal rules for 401(k) and 403(b) plans under the Bipartisan Budget Act of 2018. Prior to these changes, participants were suspended from making salary deferrals following a hardship withdrawal for a period of time. With the new regulations, participants no longer are subject to this restriction. In addition, participants will no longer be required to first obtain a loan from the plan, prior to taking a hardship withdrawal. These changes are effective on or after January 1, 2020 with early adoption permitted as early as January 1, 2019. Another change is that Plan administrators may rely on an employee's written self-certification of insufficient assets to satisfy the financial need, unless the plan administrator has knowledge to the contrary.

For 401(k) plans, hardship withdrawals are permitted from elective deferrals, Qualified Non-Elective Contributions (QNEC), Qualified Matching Contributions (QMAC) and safe harbor contributions and earnings on these amounts. For 403(b) plans, hardship withdrawals are permitted from elective deferrals and earnings on amounts are ineligible for hardship withdrawals. Hardship withdrawals from QNEC and QMAC are limited to certain non-custodial 403b plans.

Changes to the safe harbor list of eligible hardship expenses include:

- Hardships for medical, educational or funeral expenses may be incurred by the 'primary beneficiary under the plan.'
- Casualty loss damage to a principal residence does not have to be due to federally declared disaster area.
- New category of hardship for expenses incurred as a result of federally declared disaster designated by FEMA.

Plan amendments will be needed for the hardship withdrawal changes. Individually designed plans will need to be amended no later than the end of the second calendar year following the issuance of the hardship changes on the required amendment list, while pre-approved plans will need interim amendments likely in the year following the issuance of the final regulations.

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Delinquent Participant Contributions

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As a general rule, Department of Labor (DOL) regulations specify that salary deferrals and loan repayments withheld from employee paychecks should be remitted to contributory employee benefit plans as of the earliest date on which such contributions can reasonably be segregated from the plan sponsor's general assets. While the regulations further state that in no event shall the deferrals be remitted later than the 15th business day of the month following the month in which the deferrals were withheld, it is important to note that the 15th business day rule does not represent a "safe harbor". The DOL expects that plan sponsors should be able to remit amounts withheld from employee paychecks to the plan on a payroll date frequency rather than a monthly frequency, and has repeatedly shown in its enforcement actions that it expects 1) the amount of time necessary to remit amounts withheld to be consistent from pay period to pay period and 2) the amount of time necessary to remit amounts withheld to be consistent with the amount of time necessary to remit income tax withholdings to the IRS. Failure to remit participant withholds to the plan in a timely fashion can result in fines and penalties in the event that the Plan is examined by the DOL.

In an effort to avoid late contributions, it is recommended that plan sponsors implement preventative processes, which may include:

- Establishing a procedure that requires participant contributions to be deposited coincident with each payroll date on a consistent basis;
- Training a backup employee to cover for vacations or unexpected disruptions in the process;
- Coordinating with their payroll provider to determine the earliest date they can submit deferral deposits; and
- Establishing a log of remittances including payroll dates and dates received by the plan. Log descriptions should include an explanation of why deposits are late and have the log reviewed by senior management to facilitate continuous improvement.

Late contributions continue to be one of the most prevalent prohibited transactions. As a result, the Employee Benefits Security Administration (EBSA) has designed the Voluntary Fiduciary Correction Program (VFCP) to assist plan sponsors in voluntarily correcting Employee Retirement Income Security Act of 1974 (ERISA) violations, which include delinquent participant contributions. Plan Sponsors can submit an application to EBSA demonstrating self-correction of the delinquent contributions, which may require corrective action including:

- Determining which deposits were late and calculating the related lost earnings;
- Depositing of the missed deferrals including lost earnings;
- An analysis of procedures and correction of the deficiency that facilitated the late deposit; and
- An attachment to the Form 5500 showing late deposits.

When the plan sponsor makes corrections under the VFCP the plan sponsor will receive a no action letter upon satisfactorily correcting the violation submitted in the application. As a result, participation in the VFCP allows the plan sponsor to avoid civil enforcement action, legal action and civil penalty.

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IRS Reopens Lump Sum Buyout Windows

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On March 6, 2019, the IRS issued Notice 2019-18, which reverses the IRS's previously stated intention to prohibit defined benefit plans from offering lump sum buyouts to retirees currently receiving benefits. Prior to the IRS's announcement in 2015 of its opposition to such arrangements, lump sum buyouts had become increasingly popular as a way for sponsors of defined benefit plans to "de-risk" those plans by reducing uncertainty regarding future obligations. Typically, plans offered a buyout "window", a specified period during which retirees receiving benefits could elect to forgo future annuity payments in exchange for a one-time lump sum payment.

The renewed availability of this de-risking option offers another option for sponsors of defined benefit plans to consider as they manage the obligations associated with such plans. However, there are a few items plan sponsors may wish to consider prior to implementing a course of action:

1) As compared to lump sum buyouts of terminated vested participants not yet receiving benefits, which have been and continue to be allowed by the IRS, lump sum buyouts for retirees may suffer from an "antiselection" effect. As retirees are generally more advanced in age, they may be able to be better assess their expected future life span. This could result in those expecting to live shorter than average lives electing to take the lump sum, while those expecting to live longer may not. Thus, the expected cost savings of the buyouts may be cancelled out by remaining participants living longer than expected.

2) There will be administrative costs associated with designing and executing a lump sum buyout window, including legal fees, costs of calculations of lump sum amounts, mailings and other publicity efforts, and so on. It will be important for Plan Sponsors to assess the number of retirees expected to take advantage of lump sum buyouts, and the associated savings on future benefit payments, prior to incurring these costs. It's worth noting, that while buyout windows for terminated vested employees typically see acceptance rates of 50% - 70%, retirees who are already receiving annuity payments may be less likely to give up those annuity payments.

3) Lump sum buyouts are not without controversy, as many in the pension plan industry have expressed concerns regarding the shifting of risk from Plan Sponsors back to retirees, who, in some cases, may now be responsible to manage their retirement income for the first time and may not have the sophistication to do so. Plan fiduciaries should consider the risk that lump sum buyouts may open the possibility of plan participants being exploited, or of ineffectively managing their assets and running out of their money prior to the end of their lives (such concerns, in fact, contributed to the IRS's initial 2015 decision to prohibit these buyouts).

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Expansion of the IRS Self-Correction Program

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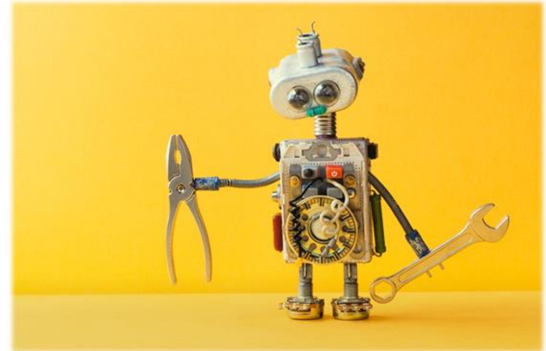
The IRS recently issued Rev. Proc. 2019-19, which went into effect April 19, 2019. This Rev. Proc. expanded the Self-Correction Program (SCP) of the IRS Employee Plans Compliance Resolution System (EPCRS) to make it easier to fix certain plan document and operational failures which were previously disallowed from self-correction. The expansion of the SCP is applicable only to Internal Revenue Code 401(a) plans (which includes 401(k) plans and 403(b) plans). These plans must have a favorable determination letter in order to be eligible for self-correction under the program.



Rev. Proc. 2019-19 also specifically expands the SCP to certain plan loan failures:

- Self-correction is now available for tax relief on deemed distributions of loans which were in default or met specified failures in the Rev. Proc.
- Self-correction is now available for loans which were in default, but for which the participant is willing to take actions to fix the defaulted loan in order to avoid a deemed distribution.
- If spousal consent is required for loan disbursements, but was not obtained, plans can now retroactively obtain spousal consent as a form of self-correction.
- If the number of plan loans is limited by the plan document and the plan sponsor erroneously allows participants to exceed that number of loans, plans can now be retroactively amended to expand the number of loans allowed. This option is only available if the ability to exceed the previous loan limit was offered to all participants in the plan (and not, for example, expanded intentionally for one specific person).

While the Rev. Proc. 2019-19 specifically discusses plan loan failures, there are many self-corrections which are now available under the SCP as long as they are corrected within a two-year window as spelled out in the Rev. Proc. Previously, these failures were required to be corrected under the Voluntary Correction Program (VCP) of EPCRS, which required written approval from the IRS to maintain tax-exempt status without paying penalty. It should also be noted that the IRS correction program under EPCRS pertains to plan document failures, but the DOL has a separate correction program that pertains to certain prohibited transactions, which was not discussed in this article. The DOL guidance is unaffected by this Rev. Proc. It is always recommended that plan sponsors consult with legal counsel regarding any errors which require correction to ensure that they are filing with the right agency (IRS vs. DOL) and under the correct program under Rev. Proc. 2019-19 (SCP vs. VCP).

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Trends in EBP Litigation and EBP Fiduciary Best Practices

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For several years we've witnessed a growing volume of litigation related to employee benefit plans. According to the Bloomberg Bureau of National Affairs, ERISA Litigation Tracker (2018), over 100 complaints were filed for the years 2016 and 2017. These lawsuits have gained mention in the news, the web, and even television commercials with attorneys seeking retirement plan participants whom believe they've been "harmed". Recently, the AICPA noted this trend in their 2018 Risk Alert for Employee Benefit Plans. They cite the subject of the lawsuits to include the following:

- Unreasonable fees charged;
- Failure to monitor fees charged to participant accounts;
- Improper investment options;
- Failure to monitor investment performance; and
- Plan oversight bodies have not operated for the exclusive benefit of the participants.

According to the IRS, a fiduciary is a person who owes a duty of care and trust to another and must act primarily for the benefit of the other in a particular activity. The IRS defines basic fiduciary responsibilities to include the following:

- Acting solely in the interest of the participants and their beneficiaries;
- Acting for the exclusive purpose of providing benefits to workers participating in the plan and their beneficiaries, and defraying reasonable expenses of the plan;
- Carrying out duties with the care, skill, prudence and diligence of a prudent person familiar with the matters;
- Following the plan documents; and
- Diversifying plan investments.

The responsibility to be prudent covers a wide range of functions needed to operate a plan. Since you must carry out these functions in the same manner as a prudent person, the IRS indicates it may be in your best interest to consult experts in such fields as investments and accounting. Hiring an expert can help reduce your liability but it does not completely eliminate all responsibilities and liability. The IRS provides the following list of items to consider in selecting a plan service provider:

- Information about the firm's affiliations, financial condition, experience with 401(k) plans, and assets under their control;
- A description of how the firm will invest plan assets or how it will handle participant investment directions, and its proposed fee structure;

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- Information about the identity, experience, and qualifications of the professionals who will be handling the plan's account such as:
    - Any recent litigation or enforcement action that has been taken against the firm;
    - The firm's experience or performance record;
    - Whether the firm plans to work with any of its affiliates in handling the plan's account; and
    - Whether the firm has fiduciary liability insurance.
- Once hired, these are additional actions you should take when monitoring a service provider:
    - Review the service provider's performance;
    - Read any reports they provide;
    - Check actual fees charged;
    - Ask about policies and practices (such as trading, investment turnover, and proxy voting); and
    - Follow up on participant complaints.

These recent trends in litigation highlight the importance of documenting your actions of fiduciary oversight. A documented investment policy can be used as a tool to prudently monitor the investment line-up. Plan fiduciaries should also document oversight by regularly meeting to discuss relevant matters and documenting the minutes from these meetings. We recommend this documentation to include matters such as the following:

- Date, time and location of the meeting;
- Identification of the people present at the meeting;
- Reference to any investment reports used during the meeting;
- Participation issues such as education, goals for increasing the number of participants, or deferral rates;
- Plan fee matters including benchmarking for reasonableness and 408(b)(2) service provider notice compliance;
- Fund performance matters including benchmarking, decisions to place a fund on a formal or informal "watch list", and decisions to replace/add a fund to the line-up;
- Consideration and approval of amendments to the plan document;
- Evaluation of service providers, including a review of SOC 1 reports obtained from service providers and considerations of end-user controls;
- Employee/participant complaints or concerns, if known;
- Compliance with ERISA regulations; and
- Party-in-interest transactions and considerations

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New Auditing Standard for Employee Benefit Plans

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In response to a request from the Chief Accountant of the Department of Labor, the Auditing Standards Board (ASB) recently issued Statement on Auditing Standards (SAS) 136, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA*, which specifically addresses audits of financial statements of employee benefit plans subject to the Employee Retirement Income Security Act of 1974 (ERISA). This new audit standard has the goal of improving audit quality over employee benefit plans.

SAS 136 provides more specific guidance in audit requirements of employee benefit plans. Specifically, the audit requirements cover the following topics:

- Client acceptance;
- Audit risk assessment and responses, including consideration of the plan's provisions;
- Communication of reportable findings to those charged with governance; and
- Auditor's responsibility regarding the ERISA required supplemental schedules.

A new audit report format from SAS 136 provides more information on the scope of the audit, responsibilities of the auditor as well as management's responsibilities, and enhanced reporting relating to going concern. The limited scope audit report is also modified and referred as the "ERISA section 103(a)(3)(C) audit" and will have a two-pronged opinion that is based on the audit and on the procedures performed relating to the certified investment information. The final version of the SAS 136 does not include the requirement for including compliance findings from the audit in the auditor's report that was proposed in the exposure draft. However, certain compliance findings are required to be communicated to those charged with governance. The effective date of SAS 136 is for periods ending on or after December 15, 2020.

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