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FALL 2019

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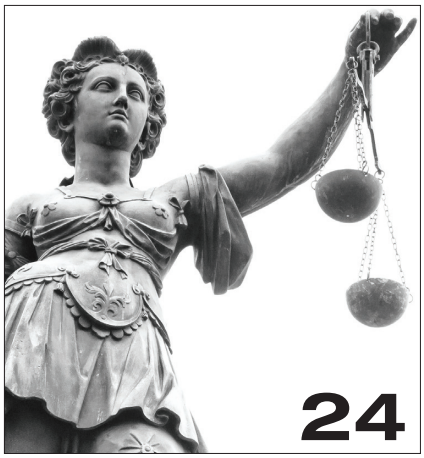

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Plug This Leak!

Solutions to the problem of leakage due to plan loan defaults are more readily available than you think.

A generation after the first 401(k) plans were introduced, plan leakage remains a recalcitrant problem affecting participants and plan sponsors alike.

Of the three-headed leakage monster, cashouts at termination (responsible for about two-thirds of the total, according to the Employee Benefit Research Institute) is the top factor driving leakage, followed by early withdrawals and plan loan defaults. Of the three, cashouts and early withdrawals share two important aspects in common. First, in most cases, the root cause is the kind of simple misfortune that we all face at some point in our lives, such as involuntary termination of employment, medical emergencies, or student loan or other debt.

Second, the plan design and compliance factors governing cashouts and hardship distributions are not exactly fungible. Both features boost participation rates, and so are essentially invaluable to plan health, and the ERISA and Code rules governing them are generally permissive. So absent changes in the rules, the impact of any efforts to attack the leakage problem via plan design is bound to be limited.

Which brings us to leakage from plan loan defaults.

First of all, if you haven't made a point of looking into the extent of leakage from defaults, things may be worse than you think:

- A 2018 report by Deloitte estimated $7.3 billion in loan defaults, with subsequent withdrawal of voluntary cashouts at $48 billion.
- Deloitte found that the cumulative effect of loan defaults – including taxes, early withdrawal penalties, lost earnings and early cashouts of defaulting participants' balances – represents approximately $300,000 in lost retirement savings over the career of a typical defaulting borrower.
- The Deloitte study estimated the impact of loan leakage over a 10-year period at nearly $2.5 trillion in projected leakage at retirement.
- A 2017 Wharton/Vanguard Pension Research Council study found that nearly 40% of participants have taken advantage of a loan offering, and that 86% of participants with plan loans defaulted on their loans after leaving employment.

The good news is that solutions to the problem of plan loan defaults are more readily available than for cashouts and early withdrawals. Today, most plans require participants to pay off their plan loans within 60 or 90 days after separation. Add taxes and a 10% early withdrawal penalty for those under 59½, and you're looking at a major expense. Sadly, many participants choose to cash out some or all of their 401(k) balance to pay the loan off. In many cases, it's their only viable choice.

Instead of requiring a lump sum repayment in full within 90 days, allowing participants to repay the loan over time, in installments, would go a long way toward plugging this leak. While this installment plan approach is spreading, the growth is slow. That's due largely to the fact that there is a limited number of plan sponsors with the paternalistic approach (especially toward ex-employees) that's essential to taking this kind of step. Also, administering it is cumbersome.

In time, advances in recordkeeping technology will ease the administrative difficulties, allowing recordkeepers to more readily accept monies from sources outside the payroll feed – in this case, former employees.

In the realm of plan design and non-retirement benefits, here are four other ideas that can address the default problem:

- 401(k) plan loan insurance to prevent loan defaults and the punitive consequences of involuntary job loss;
- preapproved emergency loan options that allow automatic payroll deductions for current employees;
- rainy-day savings plans funded via payroll deductions; and
- mandatory financial education and loan risk awareness programs as part of the loan approval process.

In other words, the right balance of product innovation, technology, plan design and education can help plug the loan default leak.

Questions, comments, bright ideas? Email me at jortman@usaretirement.org.

JOHN ORTMAN
EDITOR-IN-CHIEF

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BY JIM NOLAN

My Last Literary Hoorah!

And one last call to be a committee volunteer. . . we need you!

It's hard to believe, but this is my fourth and final column for *Plan Consultant* magazine as President of ASPPA.

I want to thank President-Elect Missy Matrangola for her tireless work during the last year. I also want to thank Vice President Frank Porter for his assistance during the last year as both VP and GAC Chair. Finally, but by no means least, I want to thank Brian Graff and all of the staff of ARA for their leadership, vision and tireless energy during the year.

As I write this, it is a hot July day in Kansas, and I am about to join two meetings of volunteers and staff (the ASPPA Annual Conference Committee and the Legislative Relations Committee). This is just one example of our tireless volunteers working with ARA staff to educate our members and our government partners.

This will also be my last column reiterating our call for all members to look into volunteering to serve on an ASPPA committee (see the nearby sidebar for the committee roster). We need you in order to continue accomplishing the mission of educating the government, our members and our clients regarding retirement plan issues!

In May, the Leadership Council met to review the affairs of ASPPA – including our new education efforts, which will be released late this year or early next year. We discussed the potential effects of open MEPs on ASPPA members. Brian Graff informed the Leadership Council that we would like to proactively address some of the concerns that are arising from the membership at large around the prospects that the SECURE Act will be enacted. That legislation passed the House of Representative with overwhelming bipartisan support in June and now heads to the Senate.

This year's ASPPA Annual Conference was discussed as well, with President-Elect Missy Matrangola noting that the TPA Growth Summit is a complement to ASPPA Annual's technical agenda, and was created for TPA business owners and staff who focus on business development.

Thanks to all for a very interesting year. I look forward to seeing you at ASPPA Annual, Oct. 20-23, 2019! You are in great hands with Missy and Frank going forward. PC

> "We need you in order to continue accomplishing the mission of educating the government, our members and our clients regarding retirement plan issues."

James R. Nolan, QPA, is the CEO of The Nolan Company, a division of T Bank, N.A., a TPA providing recordkeeping, administration, actuarial and plan design services serving clients in 50 states. This is his last column as ASPPA's 2019 President.

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BY BRIAN H. GRAFF

Starting 'Blocks'

The impact of student loan debt on retirement savings has emerged as one of the most significant challenges of our time.

If your workforce includes recent college graduates – or even not-so-recent college graduates – it's likely that some of them have debt associated with their college years – and just as likely that it's hampering their retirement savings.

Any number of studies have chronicled the impact of this debt on retirement savings. A recent study by TIAA found that an estimated 84% of Americans say that outstanding student debt is hurting their ability to sock away money for their golden years, and roughly three-quarters (73%) say that they're putting off maximizing their retirement plan contributions, or don't plan to contribute to a retirement account at all, until their student debt is gone. Among those who haven't yet started, more than a quarter cite student debt as the reason why.

The non-partisan Employee Benefit Research Institute (EBRI) has found that though those with college degrees are more likely to have access to a defined contribution plan at work, and to participate at higher levels, they have smaller balances. For families with heads younger than 35 with a college degree, the median DC balance was $20,000 and the average balance was $53,638 for the families without a student loan, compared with $13,000 and $32,987, respectively, for the families with a student loan. Said another way, those without student loans had more than 50% more in their DC plan than those with student loans.

Now, it's always been a challenge encouraging younger workers to save for retirement – but the breadth and depth of the impact of student debt on retirement savings has emerged as one of the most significant challenges of our time. And it's keeping the next generation of retirement savers from enjoying one of the most significant benefits of a long investment horizon – the magic of compounding!

This has been a significant and growing concern for our members, both as employers and among the employers they support. In fact, calls to do something to mitigate its impact have only strengthened in the months since the 2018 IRS private letter ruling (PLR 131066-17) which permitted a specific 401(k) plan sponsor to contribute to the plan on behalf of plan participants who pay down student loan debt but do not necessarily contribute to the employer's 401(k) plan. Since then there have been calls for a revenue ruling that broadens the reach of this guidance.

A number of legislative proposals would go even further – bills have been introduced by Sens. Rob Portman (R-OH) and Ben Cardin (D-MD), as well as Senate Republican Whip John Thune (R-SD), along with Sen. Mark Warner (D-VA).

Perhaps the most notable – and one that we've been actively engaged on – is one by Sen. Ron Wyden (D-OR), Ranking Member of the Senate Finance Committee. Wyden's Retirement Parity for Student Loans Act – co-sponsored by Senate Finance Committee members Maria Cantwell (D-WA), Ben Cardin (D-MD), Sheldon Whitehouse (D-RI), Maggie Hassan (D-NH) and Sherrod Brown (D-OH) – would provide a voluntary option for plan sponsors, a benefit that must be made available to all workers eligible to make salary reduction contributions and receive matching contributions on those salary reduction contributions, applied to repayments of student loan debt that was incurred by a worker for higher education expenses, supported by evidence of their student loan debt payments. The legislation stipulates that the rate of matching for student loans and for salary reduction contributions must be the same, and special rules would apply if a worker makes both salary reduction contributions and student loan repayments, such that student loan repayments would only be taken into account to the extent a worker has not made the maximum annual contribution to the retirement plan.

Significantly, the legislation also provides clarification on certain nondiscrimination rules that apply to 401(k) plans, as well as safe harbors that deem the nondiscrimination rules to be satisfied if certain matching or other employer contributions are made to the plan. And how will potential errors in administration of these programs be addressed? These are important considerations for plan sponsors (and recordkeepers) alike.

The Rolling Stones once told another generation that "time was on their side." But without a retirement plan solution to the student debt issue, that won't be the case for millions. PC

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

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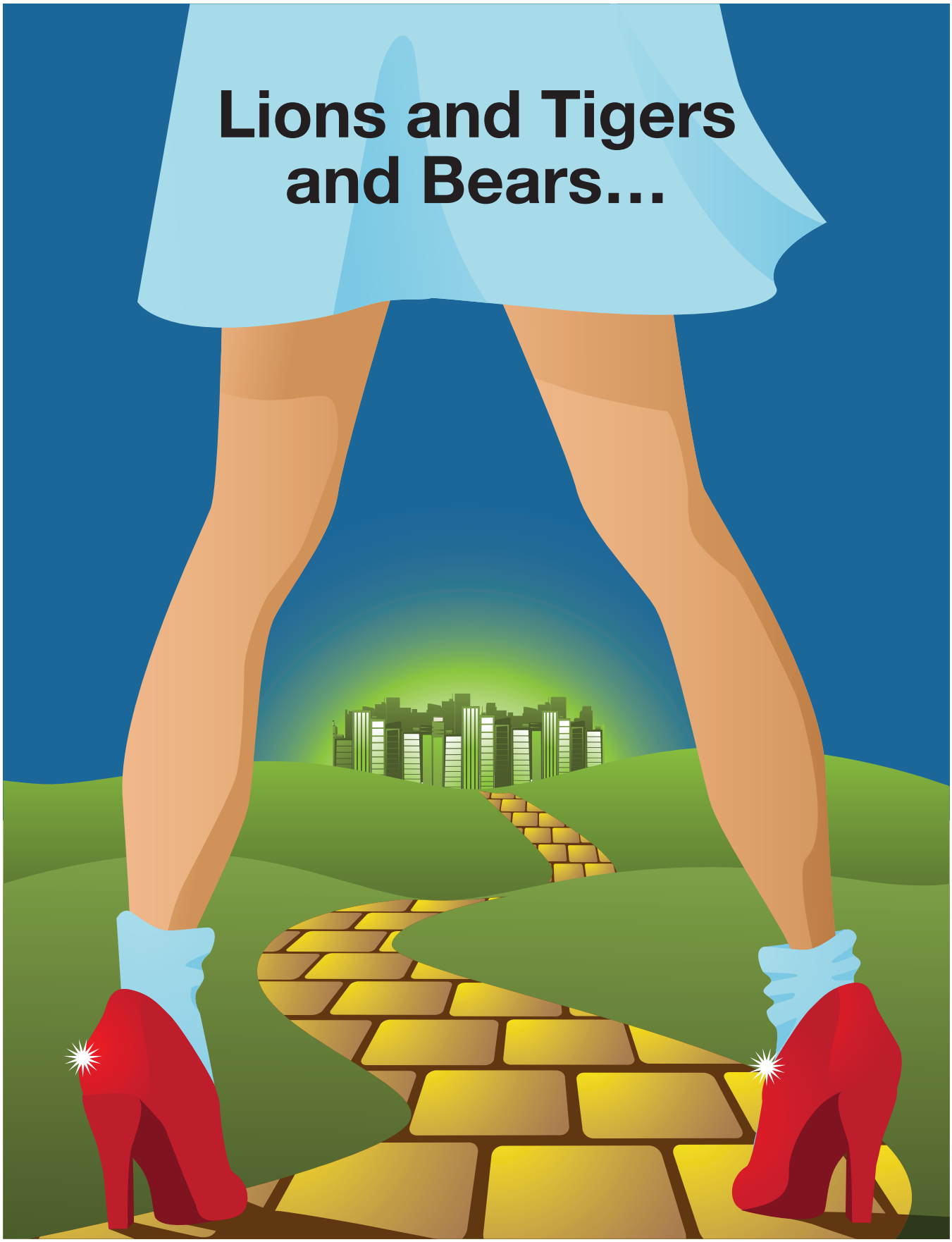

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Oh, my! And late deferrals, too – the TPA perspective.

BY TONY PANAGIOTU

On the way to Oz, Dorothy's journey was fraught with challenges because of her imperfect and often frightened companions. A journey not unlike a TPA's duty to provide competent and capable services to clients – one that is often a product of less-than-perfect information from clients and the threat of a Department of Labor or IRS audit.

Fear not: When it comes to late deferrals, unless you run into an egregious case of totally missed deferrals due to fraud or gross negligence, the remedies are simple. As Dorothy discovered when she unveiled the Wizard, there is not much bite and just a bit of bark.

That's enough movie trivia. Let's get down to the business of late deferrals. After 30 years of practice as an ERISA attorney, I can tell you: late deferrals happen. They just do. Late deferrals occur for any number of reasons, such as changing payroll companies, new payroll clerks or when Controllers or HR staffers take time off and just forget to make timely deposits.

So what's a TPA or recordkeeper to do?

First, let's get a handle on the basic rules and your obligations as a TPA or recordkeeper. The DOL has basically stated that participant contributions will be considered plan assets as soon as they can reasonably be segregated. So what does that mean?

One of my law school professors once said that "reasonable" can mean just about anything! Perhaps with that in mind, many years ago the DOL clarified what they mean by "reasonable," issuing final regulations which stated that for small plans with fewer than 100 participants at the beginning of the plan year, contributions are deemed timely if they are deposited not later than the seventh business day following the date on which the participant would have otherwise have been paid in cash. For plans larger than the small plan safe harbor, the regulations state that in no event will the date for reasonable segregation be later than the 15th business day of the month following the month in which such amount would have been payable to the employee.

So simply put, for small plans, deferrals are late unless they are deposited within seven business days. For large plans, I suggest using the seven-day standard as well. (By the way, under audit the DOL often invokes a *two-day* standard.)

One other set of rules that comes into play are the Prohibited Transaction rules under ERISA and the Code. Essentially, the IRS and DOL view the late deposit of deferrals as a prohibited short-term loan of participants' money to the plan sponsor for the amount of time in excess of what would be a reasonable time for segregating the assets. This is why for late deferrals, not only do you calculate lost earnings, but also must calculate the prohibited transaction penalty, no matter how small, and file Form 5330.

Of course, we all know the standards – so how should a recordkeeper respond when confronted with late deferrals? First, calm down; it's not the end of the world. Call the client; make them aware of the issue and perhaps suggest practices and procedures to prevent the problem from recurring. If the plan is a large one, amaze the auditors by telling them that you instructed the client to change their practices and procedures and watch them tear up.

The next step is to properly mark the correct box on the Form 5500, file Form 5330 and confess the client's sin. Also calculate lost earnings, no matter how small, and tell the client they should make a corrective deposit of lost earnings even if the amount is miniscule. (The DOL will make your client correct errors measured in pennies… no kidding.)

As a practical matter, you can spend hundreds of dollars calculating pennies in lost earnings – so, as the regulations state, be "reasonable." As a TPA or recordkeeper, your duty (depending upon your service agreement) is to assist your client with compliance. Late deferrals are a large part of compliance, so inform and educate your client and disclose late deferrals on Form 5500. If you are a recordkeeper, no doubt you have sophisticated systems to flag when contributions should be made, and you should be able to warn clients when deposits are late.

Taking your obligations further, do you have an ethical obligation to plan participants? Generally, unless you took on the title of fiduciary, your services don't rise to that level since you don't have discretionary authority over plan assets or management of the plan. That usually falls to the plan trustees. Only trustees can hire and fire service providers, and they have the fiduciary authority to oversee the proper operation of the plan. You are deemed a provider of ministerial functions and thus not a fiduciary.

Nevertheless, I believe you do have an obligation to provide high-quality service and advice, so don't turn a blind eye when this issue comes up – and make the client aware of its importance.

Both the DOL and IRS make late deferrals one of their favorite items to check on audit. So emphasize this with your clients, especially new ones. This is one of the most important things to get right. Even if a client makes a mistake and their deposits are late, know that the corrections are easy. Have your client make the corrective deposit as soon as possible and have them establish new practices and procedures, and everyone will sleep better at night. PC

Tony Panagiotu, CPA, JD, is the president of Panagiotu Pension Advisors, LLC, a Group RHI Company. An ERISA attorney for more than 30 years, he is a frequent lecturer to CPAs, attorneys and clients on the technical and practical aspects of qualified retirement plans.

SECURE Act Would Boost MEPs

The latest on developments and new opportunities regarding multiple employer plans.

BY FRED REISH, BRUCE ASHTON & JOSHUA WALDBESER

Multiple employer plans (MEPs) offer the potential of expanding retirement plan coverage, especially for smaller employers. This potential has led to new regulatory guidance and possible legislation that could open up opportunities for both employers and service providers. This article addresses recent legal developments and how they may affect the plan marketplace.

In simplest terms, MEPs are intended to allow multiple employers to offer retirement benefits through a single plan, without significant employer involvement and on a cost-efficient basis due to pooling of assets and services. Historically, MEP formation and participation has been mired in a confusing mashup of competing regulatory requirements. But positive steps are being taken to unwind these restrictions.

MEPs BACKGROUND

A major problem with MEPs has been the question of whether the arrangement is a single plan in which a number of employers participate or whether the MEP is a collection of individual plans that use common service providers and investments. Both of these scenarios exist; in the latter case, there are regulatory hurdles that have hampered the use of MEPs.

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Under the Internal Revenue Code, a plan in which unaffiliated employers participate is a single plan. But Department of Labor (DOL) guidance under ERISA looks at the matter differently, saying that employers must have significant relationships unrelated to benefits – referred to as "commonality" or a "nexus" – to constitute a *bona fide* group or association under the ERISA definition of employer.

The practical consequence is that, absent sufficient commonality, a MEP sponsored by unaffiliated employers constitutes a single tax-qualified plan under the Code, but multiple ERISA plans. (These are often referred to as "open MEPs.") Among other things, the DOL interpretation could require multiple Form 5500 filings, multiple fidelity bonds and multiple plan audits, and create confusion about roles and responsibilities.

REGULATORY DEVELOPMENTS

To expand plan coverage, federal regulators have been working to address potential compliance concerns for MEPs.

First, the Treasury Department has proposed regulations providing relief for MEPs from the risk of disqualification due to failures relating only to a particular participating employer – a concept referred to as the "one bad apple" rule. This concept is often cited as a reason why employers may be hesitant to join MEPs. In our view, this concern is more theoretical than practical, given the availability of IRS correction programs, including its "fee-free" self-correction program. Nonetheless, the regulation, once finalized, should help assuage these concerns.

Second, the DOL has finalized its "Association Retirement Plan" (ARP) regulation. The ARP regulation relaxes the "commonality" rule by requiring only that the employer-members of the group or association either (1) be in the same trade, industry, line of business or profession, or (2) have a principal place of business within a single state or metropolitan area. Subject to some conditions, the ARP regulation provides that the "primary purpose" of the group or association can be to offer the MEP to employer-members, provided there is at least one other substantial business purpose. A "substantial"

business purpose is deemed to exist if the group or association would be a viable organization in the absence of the MEP, and specifically includes the promotion of common business interests or employer community.

The ARP regulation also endorses the establishment of MEPs sponsored by professional employer organizations (PEOs) in situations where the PEO provides "substantial employment functions" on behalf of its employer-clients, and the PEO controls the MEP by serving as its sponsor, administrator and named fiduciary.

THE SECURE ACT

A key provision in the Setting Every Community Up for Retirement Enhancement (SECURE) Act would provide for the establishment of defined contribution MEPs, referred to as "pooled plans," without regard to any "commonality" whatsoever. The SECURE Act is not yet the law – it was approved by the House (and if passed by the Senate, would likely be signed by the President) – but has run into delays in the Senate. Still, it seems likely the SECURE Act will pass, which would pave the way for the establishment of MEPs regardless of any relationship among the participating employers.

As a result of the likelihood of enactment of the SECURE Act, the industry response to the ARP regulation has been more tepid than might be expected. Trade associations and similar groups that can comfortably satisfy its commonality requirements and other restrictions certainly could choose to proceed in establishing MEPs in reliance on the ARP regulation (as could many PEOs), but significant numbers of potential MEP sponsors may choose instead to adopt a "wait and see" approach in light of the SECURE Act.

OPPORTUNITIES FOR PROVIDERS

Greater availability of MEPs should be a beneficial development for small businesses that lack the time, resources and/or inclination to establish and maintain their own 401(k) plans. MEPs reduce administrative responsibilities (and attendant exposure to liabilities) and should result in lower investment and administrative costs. In the MEP model, participating employers generally have no direct responsibility for such tasks as selecting and monitoring investment funds, distributing information and disclosures

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> As a result of the liklihood of enactment of the SECURE Act, significant numbers of potential MEP sponsors may choose instead to adopt a "wait and see" approach.

to participants, processing withdrawal and loan requests, and other administrative duties, all of which are outsourced to the MEP sponsor and its suite of service providers.

If and when the SECURE Act becomes law, the open MEP market will undoubtedly become much larger. open MEPs currently exist and are available to small employers who wish to adopt them. But if the SECURE Act passes, many more vendors will establish them, and they will likely be more cost effective from a compliance perspective, but the larger market should be more competitive, which could result in further cost reductions.

Expansion of the MEP market also means new business opportunities for plan providers. For instance, more MEPs will mean more need for investment advisory services, from constructing fund lineups to participant-level advice. Similarly, insurers may offer MEP investment platforms via group annuity offerings, and non-insurance-affiliated recordkeepers may likewise offer plan services, such as the recordkeeping platform and plan documents.

The exact nature of the opportunities for providers will depend on the details of the law. Under current law – in particular the ARP regulation – financial and other service providers cannot act in the role of the "group or association" sponsoring the plan. Thus, until the SECURE Act is enacted, providers interested in exploring the MEP market will need to partner with industry groups and trade associations, and PEOs, who will actually sponsor the plans and select the vendors. While this is a potentially attractive business opportunity, it provides less control and stability from the perspective of the provider. For example, a typical Association MEP might have a committee of participating employers who are responsible for selecting and monitoring service providers, and which can hire and fire vendors as it sees fit.

If the SECURE Act passes, service providers will be able to offer open MEPs (called "pooled plans" in the Act) to a broader marketplace of employers, unconstrained by requirements such as association membership. In this model, each participating employer will be responsible for deciding if and when it should join (or leave) the pooled plan, the pooled plan provider and its suite of supporting providers. But in this case, it would be possible to structure the MEP such that the provider cannot be terminated "across the board" by a third-party sponsoring organization.

Contemporaneously with the ARP regulation, the DOL published an RFI seeking public comment on whether the open MEP model (i.e., a MEP with no commonality) should be authorized through DOL guidance. The RFI also asks about related issues such as provider compensation, potential prohibited transactions and other issues for additional guidance. If the SECURE Act is not enacted, the DOL could possibly provide an improved model for open MEPs.

CONCLUSION

There is significant interest in expanding plan coverage through MEPs and encouraging employers to adopt MEPS by reducing their fiduciary and administrative responsibility. Open MEPs provide an opportunity for service providers to "do well by doing good" – that is, to expand their business by helping employers sponsor plans and helping employees save for retirement. PC

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Joshua Waldbeser is a Partner in Drinker Biddle's Chicago office. He counsels plan sponsors and committees with respect to their fiduciary responsibilities under ERISA, as well as design and operational considerations for 401(k) plans, ESOPs and other DC plans, and cash balance and traditional DB plans.

IRS Issues Rules on Hardship Distributions

The proposed rules include several Jan. 1, 2020, effective dates.

BY NEVIN E. ADAMS, JD

Following up on provisions enacted in the Bipartisan Budget Act of 2018, late last year the IRS issued some much-anticipated proposed regulations on hardship distributions.

Generally speaking, the changes will make it easier for participants to get, and to get more, when requesting a hardship distribution – and many of the "penalties" associated with taking a hardship distribution are removed. Moreover, the criteria for determining what a hardship is have also been expanded.

HARDSHIP DEFINITION EXPANDED

The proposed regulations modify the safe harbor list of expenses for which distributions are deemed to be made on account of an immediate and heavy financial need by:

- adding "primary beneficiary under the plan" as an individual for whom qualifying medical, educational, and funeral expenses may be incurred (regulations had previously referenced only a spouse or dependent);
- clarifying that the home casualty reason for hardship does not have to be in a federally declared disaster area (an unintended consequence of the Tax Cuts and Jobs Act of 2017); and
- adding a new type of qualifying expense to the list – expenses incurred as a result of certain

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disasters that the IRS and Congress have traditionally, but separately, provided relief for in the past, such as hurricanes, floods, wildfires, etc. This, the IRS explains, is "intended to eliminate any delay or uncertainty concerning access to plan funds following a disaster that occurs in an area designated by the Federal Emergency Management Agency (FEMA) for individual assistance."

This updated list of safe harbor expenses may be applied retroactively to distributions made on or after Jan. 1, 2018.

EXPANDED ACCESS

The account balances that may be accessed for hardship have been expanded to include:

- elective deferrals *plus* earnings; and
- QNECs, QMACS, safe harbor contributions, QACAs – all of these plus earnings, "regardless of when contributed or earned."

Note that individual plans may decide to limit the sources for hardship availability.

HARDSHIP 'PENALTIES'

The proposed regulations eliminate the safe harbor under which a distribution is deemed necessary to satisfy the financial need only if elective contributions and employee contributions are suspended for at least 6 months after a hardship distribution is made and, if available, nontaxable plan loans are taken. However, the IRS, acknowledging the timing of the publication of these proposed regulations, says that the prohibition on suspending contributions would only apply for a distribution that is made on or after Jan. 1, 2020.

The regulations also eliminate the rules under which the determination of whether a distribution is necessary to satisfy a financial need is based on all the relevant facts and circumstances, replacing it with a general standard for determining whether a distribution is necessary. That general standard is that:

- the hardship may not exceed amount of need, adjusted for anticipated taxes and penalties;
- the participant must have obtained all other available distributions under the employer's plans (other than loans, as had been the case under the previous regulations);

- the participant must represent that he or she has insufficient cash or liquid assets to satisfy that financial need; and
- the plan administrator may rely on this representation, barring "actual knowledge" to the contrary.

The IRS notes that in light of the timing of the publication of the regulation, the requirement to obtain this representation would only apply for a distribution that is made on or after Jan. 1, 2020. The regulations note that plan generally may provide for additional conditions for distributions made before that date, "to demonstrate that a distribution is necessary to satisfy an immediate and heavy financial need of an employee."

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APPLICATION TO 403(b) PLANS

The IRS notes that income attributable to Section 403(b) elective deferrals continues to be ineligible for distribution on account of hardship and that QNECs and QMACs in a Section 403(b) plan that are not in a custodial account may be distributed on account of hardship, but QNECs and QMACs in a Section 403(b) plan that are in a custodial account continue to be ineligible for distribution on account of hardship.

EFFECTIVE DATES

The changes to the hardship distribution rules made by the Bipartisan Budget Act of 2018 are effective for plan years beginning after Dec. 31, 2018, and the proposed regulations provide that they generally would apply to distributions made in plan years beginning after Dec. 31, 2018. However, the IRS notes that the prohibition on suspending an employee's elective contributions and employee contributions as a condition of obtaining a hardship distribution may be applied as of the first day of the first plan year beginning after Dec. 31, 2018, even if the distribution was made in the prior plan year. Therefore, a person under elective deferral suspension in the second half of the 2018 plan year could resume deferring (if the plan allows) during the 2019 plan year.

The IRS also notes that the revised list of safe harbor expenses may be applied to distributions made on or after a date that is as early as Jan. 1, 2018. Moreover, it notes that a plan may be amended to apply the revised safe harbor expense relating to losses (including loss of income) incurred by an employee on account of a disaster that occurred in 2018 (such as Hurricane Florence or Hurricane Michael), provided that the employee's principal residence or principal place of employment at the time of the disaster was located in an area designated by FEMA for individual assistance with respect to the disaster.

CURRENT STATUS

Assuming these proposed regulations are finalized, plan sponsors will need to amend their plans' hardship distribution provisions by the end of the second year after the issuance of the Required Amendments list. What's less clear at this point (but might be cleared up via the comment period/process) is the timing and manner of changes to preapproved plans. PC

MILLENNIUM TRUST COMPANY®

AUTOMATIC ROLLOVERS REMAIN THE BEST SOLUTION FOR MISSING PARTICIPANTS

BY TERRY DUNNE

Missing or non-responsive former employees can drain plan resources, impairing effective plan administration and exposing you to potential fiduciary risks. Automatic rollovers were created to provide an easy way for retirement plans to remove costly, small balance accounts of former employees, while preserving the tax-deferred status of their savings.

At Millennium Trust, we are passionate about improving retirement readiness. Automatic rollovers remain the industry standard for reconnecting participants with their savings in ways that benefit participants, plan sponsors and providers.

SAFE HARBOR

Automatic rollovers are the only solution to dealing with missing participants that is covered by an explicit Department of Labor (DOL) safe harbor from fiduciary responsibility.

PORTABILITY

Automatic rollovers give participants a chance to choose the right path for their retirement assets.

FIGHTING LEAKAGE

Automatic rollovers protect the tax-deferred status of employees' retirement assets, therefore limiting the amount of asset leakage from the retirement system.

Today, our solution has been implemented by more than 100,000 retirement plans, providing them a simple, secure and client-friendly solution that is easy to use for both the plan and former employees. We can easily process a large volume of small accounts, including balances of less than $1,000.

But we go above and beyond just automatic rollovers. Our full suite of retirement services gives plan sponsors and providers all of the tools they need to combat and prevent missing participants.

UNCASHED CHECK RESOLUTION

Many of the distribution checks sent to former employees go uncashed. Uncashed checks that meet specific criteria can be rolled over into IRAs under regulations put in place by the DOL.[1]

MISSING PARTICIPANT SEARCH SERVICES

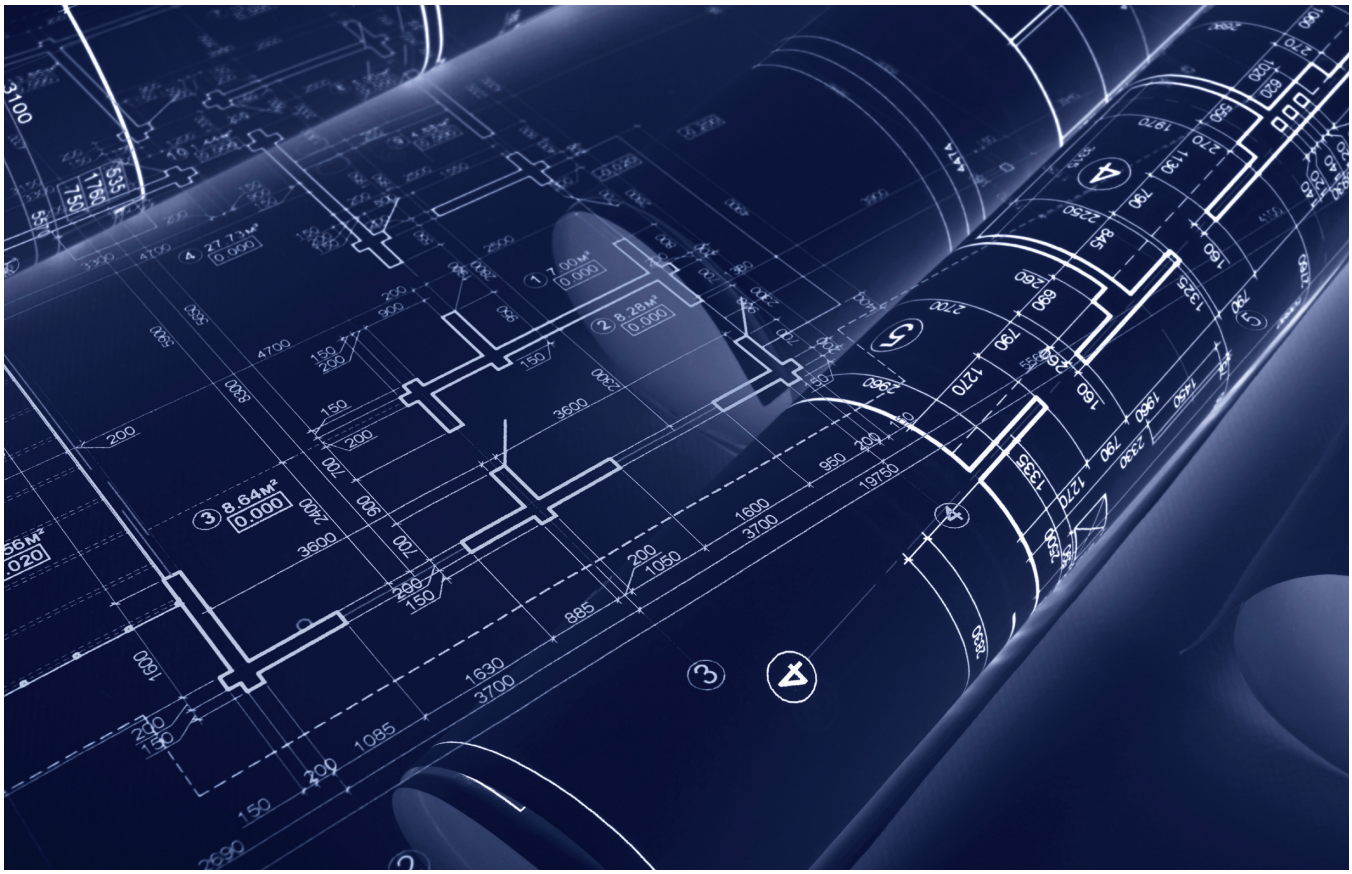
When missing participants leave balances behind, it can cause serious complications for administrators. Our search services are designed to help reduce costs and fiduciary liabilities associated with missing participants and reflect our commitment to reconnecting participants with their retirement savings.

PLAN TERMINATION ROLLOVER SERVICES

Millennium Trust has helped thousands of fiduciaries complete their plan termination by rolling eligible accounts into Safe Harbor IRAs, with a goal of preserving assets and reconnecting those accounts with their owners.

Terry Dunne is senior vice president and managing director of Retirement Services at Millennium Trust Company, LLC. Mr. Dunne has over 40 years of extensive consulting experience in the financial services industry. Millennium Trust Company performs the duties of a directed custodian, and as such does not sell investments or provide investment, legal or tax advice.

[1] https://www.americanbenefitscouncil.org/pub/?id=2abc7f21%2D95f5%2D5269%2Dea28%2Dab038034cf14



81-100 Trusts vs. Open MEPs

Delivering a solution to your clients that includes some level of "pooling" can give you lower costs – and great outcomes.

BY R.L. "DICK" BILLINGS

"We'd like to adopt a plan, but it's just too costly and complicated." If you have been in the retirement plan market for any amount of time, you have encountered this retort from a plan sponsor.

Many prospects simply focus on the cost. As I was told early in my TPA career, *"Cost is only relevant in the absence of value."* Your prospect's dilemma is this: Does a cost-effective solution exist that also meets their other needs? I think so. Delivering a retirement plan solution to your clients that includes some level of "pooling" *can* give you lower costs – and great outcomes.

However, unless you are well-versed in the law, it can be confusing to understand some of the nuances in our marketplace. We hear many terms like group trusts, 81-100 trusts, MEAPs, closed MEPs and open MEPs. My intent here is not to provide an exhaustive analysis that gets into the weeds on each term. Rather, this article will concentrate on the two terms we seem to hear the most: open MEPs and 81-100 trusts.

From a technical viewpoint, comparing these two entities is like comparing apples to oranges. Both are good – but totally different from each other. An 81-100 trust is "a group of trusts" to hold qualified assets; nothing more. MEPs connotate a "plan." When a client adopts a pre-approved adoption agreement, even though there are just a few words and a signature on the agreement, the client is legally adopting a plan and a trust. The plan sets out eligibility, vesting, etc., while the trust (the piece most clients never read) outlines how the investments are held and invested.

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> In general, employers do not want to be named as the plan sponsor and take on all the legal obligations that go along with that title.

In today's marketplace, MEPs and 81-100 trusts are marketed as competitors to each other. And if you look "under the hood," typically you will see many similarities – with some subtle differences.

OPEN MEPS

First things first: open MEPs are not, *and have never been*, illegal. Many open MEPs exist in the United States today and have been in existence for decades. Some large financial institutions have their own open MEPs. So, if someone tells you that open MEPs are illegal, they are mistaken. I encounter many players in this business who believe open MEPs were killed by the Department of Labor's Advisory Opinion (AO) 2012-04A. Did that AO set guidelines for open MEPs? You bet – but it did *not* make open MEPs illegal. Open MEPs continue to be popular and valuable among TPAs, recordkeepers and investment advisors; but most importantly, small employers.

This is how open MEPs are typically (but not always) structured:

- Established as one plan under the Internal Revenue Code; considered a "collection of plans" under ERISA (more on this later).
- Participating employers (PEs) join the open MEP by signing a shorter "Joinder Agreement" outlining any allowed plan design choices (e.g., eligibility, vesting, match rate, etc.);
- The open MEP is sponsored by an outside party, not the PE.
- A 3(38) investment manager can be engaged to determine the plan's investment fund lineup offered to all PEs. The lineup is typically zero-revenue-share mutual funds, index funds, or both.
- An outside professional ERISA Section 402 named fiduciary and 3(16) plan administrator is hired; this professional firm can also serve as the plan sponsor.
- An outside corporate directed trustee can be engaged.
- A TPA and a recordkeeper are engaged to perform services for the open MEP (both services could be done by a single vendor).
- Investment adviser solutions – there are different arrangements that will work. A PE can choose its own advisor; there may be no choices available; etc.
- ERISA's one-bad-apple rule applies. This issue has never been a huge concern since the DOL considers open MEPs to be a "collection of plans." But thanks to the IRS, this issue appears to be going away, due to regulations issued on July 3, 2019.

Congress loves MEPs; and all the discussion occurring in Washington today about improving retirement plan coverage involves changes to existing MEP rules. This does not automatically make the MEP better than an 81-100 trust, but increasingly MEPs are taking up all the oxygen in the room, so to speak.

81-100 TRUSTS

Again, in today's marketplace, 81-100 trusts look a lot like an open MEP, and can largely accomplish the same goals. Proponents of 81-100 trusts claim their concept to be a "real thing" – that is, a specific ruling from the IRS gave its blessing to this concept. Conversely, MEPs existed long before ERISA passed in 1974, so MEP language that has been created since then has tried to address, and catch up with, the various MEP variations. With the SECURE Act waiting in the wings on Capitol Hill, this evolution continues.

Typically (but not always), 81-100 trusts are structured like this:

- Each PE adopts its own separate plan and trust document. Each PE legally has its own trust, separate and distinct from every other PE. Therefore, the one-bad-apple rule does not apply.
- Each PE retains the position of plan sponsor and the associated fiduciary liabilities, unless it hires outside professionals like a 3(38), 3(16) or 3(21).
- A corporate directed trustee can be hired, or some trustees use Collective Investment Funds (CIF) in lieu of mutual funds; some even offer their own CIFs.
- A TPA and a recordkeeper are engaged to perform services for the plan under the 81-100 (both services could be done by a single vendor).

- Investment advisor solutions – this too operates similarly to an open MEP and can involve different advisors among the plans, a single advisor for all plans, or no options for all PEs.

WHAT ARE THE DIFFERENCES?

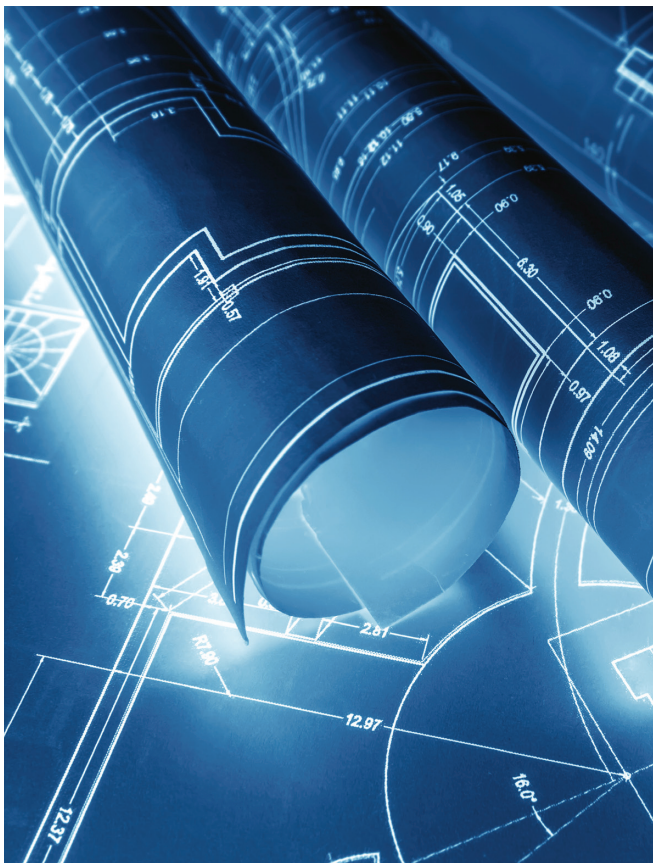
If you look at the typical services provided by each offering above, you will see that most of the features are the same. So, now let's concentrate on the differences:

» **Plan Sponsor:** In an open MEP, the PE is not the main plan sponsor, while in an 81-100 trust the PE is the only plan sponsor. Is this difference significant? Absolutely. In general, employers do not want to be named as the plan sponsor and take on all the legal obligations that go along with that title. Even with an open MEP, the PE still retains a certain amount of fiduciary responsibility, but it may appear to be less than under an 81-100 trust.

» **A "Collection of Plans Under ERISA":** This open MEP issue makes it equivalent to the 81-100 trust. Under either construct, a Form 5500 is required to be filed for each PE.

» **One-Bad-Apple Rule:** For as long as open MEPs have existed, critics have pointed to this as the reason employers should not join them. On July 3, 2019, the IRS issued proposed regulations that would essentially eliminate this rule, as long as a certain "kick-out" process is followed. There are also two major bills in Congress that would also eliminate this rule. If these initiatives are enacted, they will essentially eliminate the risk to PEs.

» **Use of CITs:** If we were to compare open MEPs and 81-100 trusts 10 years ago, we would typically see mutual funds being used in an open MEP, with Collective Investment Trusts (CITs) being used within an 81-100 trust. Since CITs were not regulated by the Securities and Exchange Commission, they were historically much cheaper than mutual funds. But with the increased use of non-revenue-sharing mutual funds, index funds and ETFs, the cost advantage of CITs is now virtually nonexistent.



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DUE DILIGENCE

If there is a bottom line here, it is that you and your PE client should make sure that all parties understand the documents in question and what fiduciary responsibilities are retained by the PE. Before you can assist a client in the decision to select either an open MEP or 81-100 trust, it is important to make sure the arrangement itself is proper and operating correctly.

Here are some leading questions you might want to ask any sponsor of an open MEP or 81-100 trust:

- Who is legally responsible for determining each vendor's "reasonableness of fees"? What is the process for doing this?
- Who is the named fiduciary, as required under ERISA Section 402?
- What is the process for a PE to transfer out of the plan? Are there any withdrawal fees or other restrictions?
- Are any proprietary investments used? If yes, why?
- What specific fiduciary duties are retained by the PE? Is that okay with the PE?

CONCLUSION

MEPs, 81-100 trusts and other "pooling" constructs are finally getting the proper attention in our industry. Forthcoming laws and regulations should help narrow down the subtle differences we see. If you are planning on using any "pooling" type of product for your retirement plan client, your safest bet is to determine and vet each plan's named fiduciary under ERISA Section 402. This is any plan's primary fiduciary – it takes on the most fiduciary risk and responsibility. And ensure that the 402 named fiduciary has the experience – a*nd the fiduciary insurance coverage* – to handle this oversight task. PC

R.L. "Dick" Billings, RF, CPC, CEBS, ERPA, is a Principal and Director of Marketing at Fiduciary Wise, LLC in Phoenix, AZ, a 402 named fiduciary and 3(16) plan administrator.

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Perspectives on Benefit Conversion Factors and Recent Lawsuits

Retirement professionals should make their DB clients aware of the requirement to use factors that do not violate the "reasonable actuarial reduction" requirement.

BY MARK SHEMTOB

Benefit conversion factors (often referred to as actuarial equivalence) used by defined benefit plans have attracted attention recently as the subject of several class action lawsuits. The initial lawsuits, filed by both current or retired employees of American Airlines, Inc., Metropolitan Life Insurance Company, PepsiCo, Inc. and US Bancorp, claim that the IRS regulations governing non-forfeiture of vested accrued benefit rules were violated.

Those IRS regulations prohibit adjustments to plan benefits payable in alternative forms and/or alternative ages (when compared to the plan's standard benefit payable at the plan's normal retirement age) if such adjustments are in excess of reasonable actuarial reductions. Though the regulations refer to "reasonable actuarial reductions," no single measure or specified range of reasonableness is provided under the Internal Revenue Code or by the IRS. Thus, the lawsuits' claims that the benefit conversion factors were unreasonable are not based upon a bright-line determination.

PLAN SPONSOR RESPONSIBILITIES

Benefit conversion factors are provisions of a pension plan that are specified within the plan document. This requirement ensures that the plan administrator applies the factors on a consistent basis. The many considerations that might go into the factor selection include:

- the goal of having the plan provide alternative benefit commencement ages or optional benefit forms;
- the demographics of the covered participant population; and
- the importance of ease of plan administration.

The factors may be designed to be cost-neutral in value or to provide employees with options that are subsidized financially. A subsidized approach may be used to encourage certain types of behavior such as early retirement. A neutral approach should theoretically result in the plan and participants not expected to be better or worse off economically in the aggregate as a result of participant elections to retire earlier or later, or to elect a different form of payment.

While a plan is not required to offer optional benefit forms (with some exceptions) or alternative benefit commencement ages, if either are offered, then the benefit conversion factors may not be designed in a way that would be deemed to be "actuarially unfair" to the participants.

What constitutes "actuarially unfair" is at the heart of the lawsuits, and relates back to the issue of "reasonableness." There are some legal restrictions on the selection of factors, including the requirement to apply the same conversion factors regardless of the gender of the participant even though life expectancies differ. In addition, the factors used to calculate the minimum amount for benefits paid as a lump sum are specified by the law. However, these "minimum lump sum assumptions" are not required to be used for other purposes.

A plan's benefit conversion factors need not be based directly on actuarial equivalence factors (mortality tables

> "There are many combinations of interest rates and mortality tables that might be considered reasonable, depending on the purpose under consideration."

and interest rates), though they often are. Nevertheless, in the determination of whether benefit conversion factors, when applied, satisfy the "reasonableness requirement," an actuarial determination using mortality tables and interest rate assumptions is used.

The mortality assumption is necessary to take into account how long benefits are expected to be paid, and the interest rate assumption is required in order to reflect the difference in the time value of the expected benefits to be paid. The relevant IRS regulations focus on the overall results of these adjustments, rather than on the reasonableness of individual assumption components. It is possible, for example, that a plan uses a fixed interest rate or specified mortality table, either of which might not be considered reasonable on its own, but that offset one another to produce benefit conversion factors that might be considered reasonable.

There are many combinations of interest rates and mortality tables that might be considered reasonable, depending on the purpose under consideration. Three alternative approaches are commonly used by plans in the selection of benefit conversion factors:

- fixed actuarial equivalence factors;
- automatically adjustable actuarial equivalence factors; and
- numerical factors which are generally based on fixed factors at the plan inception (or subsequent amendment) and converted to numerical percentages for ease of application.

Each approach has its own advantages and disadvantages.

In addition to the lack of guidance in the evaluation of "reasonableness," there is also uncertainty as to when benefit conversion factors that once were considered reasonable cease to be so. It is also unclear as to when the reasonable standard should be applied to a benefit conversion factor. Among the possibilities are at the time that the benefit is earned, as of the date that a plan participant makes an election to receive benefits, or possibly they need not be reevaluated provided that they were reasonable at the time they were adopted.

There are other relevant complications to consider. Pursuant to ERISA, a plan may not be amended to reduce benefits that have already been accrued. This includes the impact of a change in benefit conversion factors associated with an accrued benefit. A plan must provide that the resulting benefit cannot be any lower than it would have been before the plan amendment. Repeated plan amendments to update benefit conversion factors could result in multiple benefit amounts determined as of the dates of the changes that must be compared, thus potentially complicating plan administration.

In addition, certain poorly funded plans may not be amended to increase benefits unless the additional cost associated with that benefit increase is currently funded by additional contributions. Thus, a change in the benefit conversion factors may not be permitted without additional funding.

While the merits of the recent lawsuits are beyond the scope of this article, following are some relevant considerations:

- Lawmakers and regulators deliberately choose to provide discretion to the plan sponsor.
- Plan sponsors do not have free reign to use any factors.
- Reasonableness is not a single unique measurement and may be based upon the specific purpose.

CONCLUSION

The application of benefit conversion factors is among the more complicated issues in the administration of defined benefit plans. Though the selection of benefit conversion factors is under the authority of the plan sponsor, it may be a best practice for professionals who help service defined benefit plans to make their clients aware of the requirement to use factors that do not violate the "reasonable actuarial reduction" requirement. The lack of clarity regarding "reasonableness" has created considerable uncertainty that has contributed to the recent lawsuits. Time will tell whether the outcome of these lawsuits will provide some clarity on this issue. PC

Mark Shemtob, FSA, MAAA, EA, has four decades of experience specializing in the design and administration of retirement programs for private employers. He has taught courses on financial retirement issues as an adjunct professor at Rutgers University. Mark is an active member of the American Academy of Actuaries and has authored many commentaries on retirement issues and spoken on topics related to retirement security.

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408(g): RHYMES WITH OPPORTUNITY

Serving participants in a fiduciary capacity can be a great differentiator in today's world of conflicts, sales quotas and a lack of holistic, comprehensive financial knowledge.

BY BRIAN KALLBACK

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As presenter Don Jones of Fiduciary Wise began a webinar on ERISA §408(g) exemptions earlier this year, these two numbers jumped off the screen: 21 million and $13 billion *(Jones, 2019)*. Specifically:

- 21 million more participants could be served
- Over $13 billion saved by providing advice

Today we see low financial literacy, participants dependent on expertise, and a dangerously inadequate understanding of the role of a qualified plan in retirement planning. In that world, ERISA §408(g) is a monster of an opportunity to assist participants in a fiduciary capacity. And yet this prohibited transaction exemption (PTE) remains underutilized.

This topic sounds like it pertains to investment advisors. As recordkeepers, TPAs and plan fiduciaries, why should we care about this PTE? ERISA §408(g) is important for plan fiduciaries because a plan fiduciary can offer participants investment advice from a fiduciary advisor without the plan fiduciary being liable for that advice. As discussed below, the role of the plan fiduciary is to monitor the fiduciary advisor rather than the specific advice given.

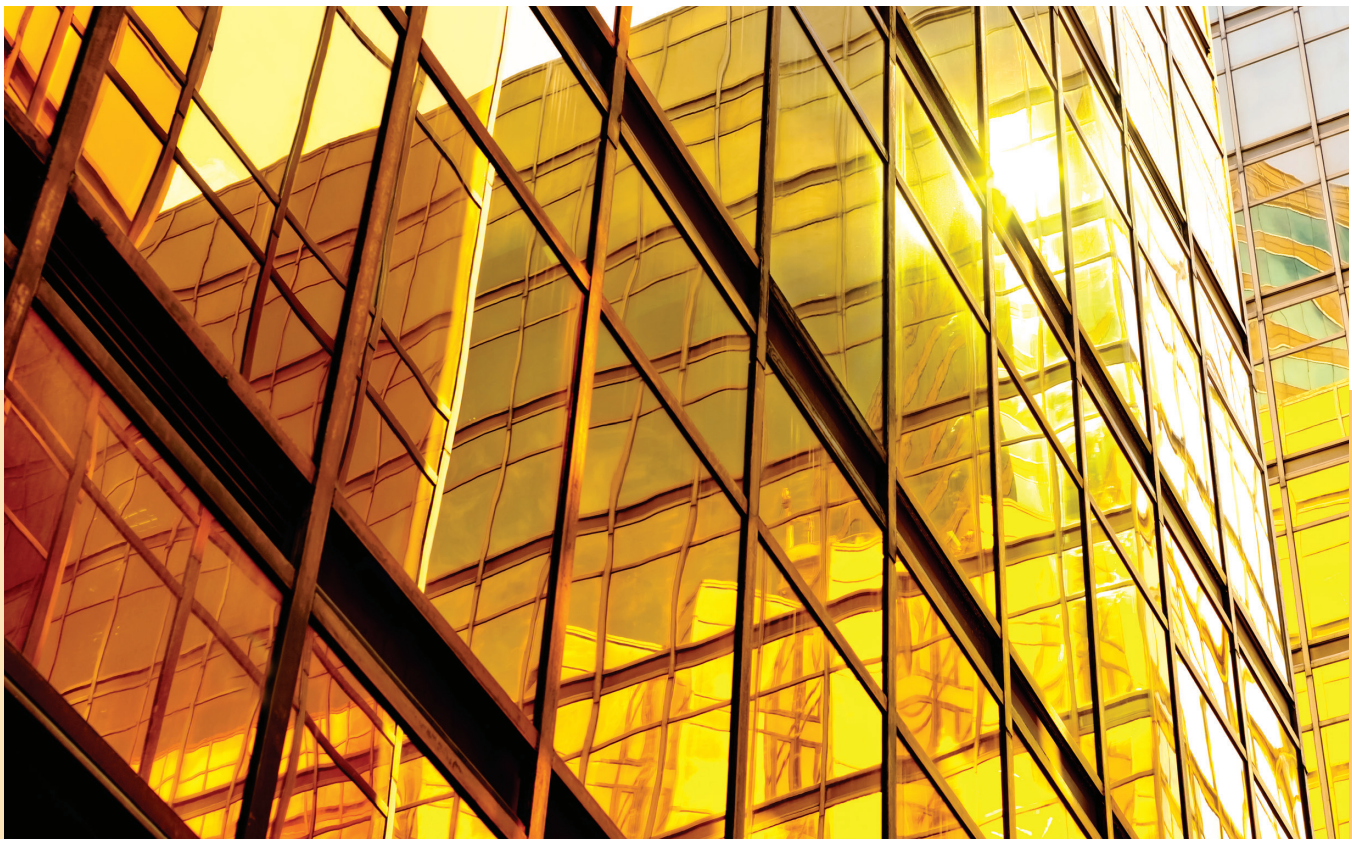
So, why should we care? ERISA §408(g) is another tool in our toolbox to serve the needs of our participants, to strengthen a workforce's benefit offering, and create further empowerment concerning financial literacy.

Since every exemption includes some conditions, this article will explore the basics of ERISA §408(g) – specifically, what it is and what is required to qualify for the exemption.

WHAT IS §408(g)?

Created by the Pension Protection Act of 2006, ERISA §408(g) created a statutory exemption for the prohibited transaction rules concerning investment advice to participants – specifically, for the transaction rule that says a fiduciary cannot use its authority or control to affect its own compensation *(DrinkerBiddle, 2009)*.

ERISA §408(g) is meant to provide insight, guidance and relief from ERISA §406 and IRC §4975 surrounding certain transactions connected to investment advice for plan participants and beneficiaries. ERISA §406 prohibits certain transactions between employee benefit plans and parties in interest (as defined in ERISA §3(14)); IRC §4975 describes the various taxes imposed on prohibited transactions.



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WHAT IS A FIDUCIARY ADVISOR?

A fiduciary advisor is an important term for a plan sponsor to understand, as sponsors that utilize a fiduciary advisor will not be responsible for the investment advice given, as long as certain disclosure and monitoring rules are followed. Yet the duty to select and monitor the investment menu for the plan and conduct oversight of the fiduciary advisor remains with the sponsor.

Fiduciary advisors may provide investment advice to qualified plan participants through an "eligible investment advice arrangement" that is based on a level-fee arrangement for the fiduciary advisor, a certified computer model, or both [ERISA §408(g)]. A fiduciary advisor may work with IRA owners as well *(Carl, 2017)*. A fiduciary advisor could be a registered investment advisor, a broker-dealer, a trust department of a bank, or an insurance company.

This term is a "particular term only to be used with an eligible investment advice arrangement" *(Jones, 2019)*. It is not a marketing term or sales nomenclature.

WHAT IS AN ELIGIBLE INVESTMENT ADVICE ARRANGEMENT?

Under ERISA §408(g), two types of exemptions are possible: the level fee exemption and the computer model exemption.

Level Fee Exemption

DrinkerBiddle describes the level fee exemption as "inappropriate" as "it applies only to situations where the fiduciary advisor's fees are level, but not to situations where the compensation of affiliates – or under the class exemption in the regulation, of supervisors – is level. In other words, it is an exemption for a "limited" level fee" *(DrinkerBiddle, 2009)*.

According to ERISA, the level fee exemption:

- is based on generally accepted investment theories … that [may or may not] take into account additional considerations [ERISA §408(g)(b)(3)(i)(A)];
- considers investment management and other fees and expenses [ERISA §408(g)(b)(3)(i)(B)];
- can incorporate additional planning information [ERISA §408(g)(b)(3)(i)(C)]; and
- disallows any fee or compensation that varies … depending on selection of a particular investment option [ERISA §408(g)(b)(3)(i)(D)].

For advisors who operate in a level fee arrangement – specifically those who are independent – there is not a prohibited transaction. According to DrinkerBiddle, "Where a fee is level, like a percent of assets or a set dollar amount, there is not and cannot be a prohibited transaction. Therefore, the benefit of the new exemptions [is not needed] and, consequently, [the advisor] does not need to comply with the requirements in the regulation" *(DrinkerBiddle, 2009)*.

Computer Model Exemption

The computer model brings an additional layer of diligence with the certification from an eligible investment expert. As stated in ERISA §408(g)(b)(4)(G)(ii), "prior to utilization of a computer model, fiduciary advisor shall obtain written certification … from an eligible investment expert … that the computer model meets eligible requirements." According to ERISA, the computer model exemption:

- is based on generally accepted investment theories … that [may or may not] take into account additional considerations [ERISA §408(g)(b)(4)(i)(A)];
- considers investment management and other fees and expenses [ERISA §408(g)(b)(4)(i)(B)];
- appropriately weights the factors used in estimating future returns of investment options [ERISA §408(g)(b)(4)(i)(C)];
- can incorporate additional planning [ERISA §408(g)(b)(4)(i)(D)];
- utilizes appropriate objective criteria to provide asset allocation portfolios comprised of investment options available under the plan [ERISA §408(g)(b)(4)(i)(E)]; and
- avoids investment recommendations that inappropriately favor investment options: [ERISA §408(g)(b)(4)(i)(F)]
  - offered by the fiduciary advisor or related or affiliated parties [ERISA §408(g)(b)(4)(i)(F)(1)]; or
  - that may generate greater income for fiduciary advisor or related or affiliated parties [ERISA §408(g)(b)(4)(i)(F)(2)].

Author's Disclaimer

PLEASE NOTE: This is a layman's attempt at interpreting ERISA §408(g). I am not an attorney, nor do I play one on TV. **Every part of this article should be considered education and not advice.** I will make every attempt to stay within the compliant foul lines, but it's important to understand that this is intended to be a primer, not a textbook. Also, with various scenarios possible, I do not intend to get deep into the weeds, so specifics may be left out. You should consult your ERISA attorney should you wish to determine your eligibility or status for the ERISA §408(g) exemption.

ERISA §408(G) IS A MONSTER OF AN OPPORTUNITY TO ASSIST PARTICIPANTS IN A FIDUCIARY CAPACITY.

Regardless of the model used – computer or level fee – the selection of an arrangement must be completed by the plan fiduciary [ERISA §408(g)(b)(5)(i)].

WHO IS AN ELIGIBLE INVESTMENT EXPERT?

An eligible investment expert "has the appropriate technical training or experience and proficiency to analyze, determine and certify … whether a computer model meets requirements … and cannot have any material affiliation or material contractual relationship with fiduciary advisor" [ERISA §408(g)(b)(4)(G)(iii)]. In other words, this person has the training and expertise without materially conflicted relationships to investigate and validate the computer model based on applicable regulations.

This certification is to be in the form of a written report that identifies and explains the computer model methodology, describes its limitations, and defines the adequacy of the eligible investment expert.

According to ERISA §408(g)(b)(4)(G)(v), the "selection of an eligible investment expert [by a plan fiduciary] … is a fiduciary act."

WHAT IS REQUIRED OF A FIDUCIARY ADVISOR?

Written notification from a fiduciary advisor must be given to plan fiduciaries. The notification will announce the advisor's intention to use an eligible investment advice arrangement and submit to an annual audit from an independent auditor. Before any advice is given, the fiduciary advisor must give "detailed written notices" to plan participants "regarding the advice arrangement *(Carl, 2017)*.

WHY AN AUDIT?

The Qualified Independent Fiduciary Audit Report of the eligible investment advice arrangement must be performed by a qualified independent auditor annually. Based on the prudent expert rule, the auditor must be "independent and qualified, so that the 'fox [is not] looking over the chicken coop'" *(Jones, 2019)*. The auditor's report should include the name of the fiduciary advisor, the type of relationship agreed upon, the name of the eligible investment advice expert, the date of computer model certification (if applicable), and the findings of the auditor.

Based on a review of Dalbar's auditor's report on T. Rowe Price Advisory Services, Inc., specific documents and data may be included in the audit as evidence of compliance *(ERISA §408(g) Fiduciary Advisor Audit, 2018)*. These may include the Investor Agreement, the level of investor complaints, the enrollment and advice process, online surveys, comparison to peer groups, and a review of sample materials. Of course, audit documentation and evidence can vary based on each unique situation.

WHAT DISCLOSURES SHOULD BE PROVIDED BY A FIDUCIARY ADVISOR?

As previously mentioned, a fiduciary advisor is responsible for certain written disclosures.

For participants, the fiduciary advisor must provide notification prior to investment advice regarding investments options. Disclosure should refer to the "material affiliation or material contractual relationship," if any, of the fiduciary advisor and any other party that "may be involved in the development of the investment advice program and selection of investment options" [ERISA §408(b)(7)(i)]. Also to be referenced are past performance and historical rates of return, all fees for compensation for investment advice, any rollover or other distribution of plan assets, types of services provided concerning investment advisor, and the fact

DOL Activity

"It appears the DOL has markedly increased its examination and enforcement activity directed at broker-dealers and registered investment advisors. Moreover, some clients have recently reported being the subject of DOL/SEC joint or concurrent examinations. We believe that supervision will be a key area of concern in these examinations; therefore, we are working with clients to identify potential areas of exposure and recommending actions to mitigate or eliminate activities that may give rise to regulatory enforcement, especially in the area of investment advice to participants." *(DrinkerBiddle, 2009)*

that the advisor is acting as a fiduciary in connection to the investment advice provided [ERISA §408(g)(b)(7)(i)(A) - ERISA §408(g)(b)(7)(i)(H)].

These disclosures must be written in a manner that can be understood by the average plan participant, and can be provided in written or electronic form [ERISA §408(g)(b)(7)(ii)].

CONCLUSION

As the role of fiduciary advice is addressed in the halls of federal and state government, serving participants in a fiduciary capacity can be a great differentiator in our world of conflicts, sales quotas and a lack of holistic, comprehensive financial knowledge (even among some retirement educators). Participants often yearn for direction and guidance, only to be turned away by a justifiable fear of liability. However, when ERISA grants exemptions to allow for advice, as ERISA §408(g) does, an opportunity arises for those providers willing to complete the due diligence and process to ensure compliance.

"Unfortunately, there is confusion [about the role of fiduciary advice and 408(g) in the qualified plan world]. [It's important to realize] if the advice would not and could not result in a prohibited transaction, the exemption is not needed. In other words, you don't need to rely on an exception to a rule if you don't violate the rule" *(DrinkerBiddle, 2009)*.

If your team is willing and able to consider a world that involves selfless, fiduciary investment advice, ERISA §408(g) offers the opportunity to provide that advice. Remember the numbers: 21 million more participants and more than $13 billion saved. PC

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TECHNOLOGY'S IMPACT ON TPA SERVICE MODELS

WE NEED TO CONTINUE TO ADAPT OUR SERVICE MODELS TO DEAL WITH THE DISRUPTION – BOTH GOOD AND BAD – THAT TECHNOLOGICAL INNOVATION IS BRINGING.

BY MICHAEL E. KING & JESSICA MARSON

The impact of technology on our roles as service providers in the retirement industry has been transformative. Each year, the speed of transformation seems to increase, and now it's more important than ever to understand how technology will affect how we provide services to our clients. It's about staying relevant.

All of us in the retirement industry – recordkeepers, advisors, consultants and TPAs – will need to continue to adapt our service models to deal with the disruption – both good and bad – that technological innovation is bringing. We will have to create or adapt to new technologies, new processes and new service models. Most large recordkeepers are already well down the road of implementing technology investments – they must in order to stay competitive. These investments include the development of self-serve tools for advisors, participants, plan sponsors and, to a limited extent, TPAs.

Here's the good news: Technology is available today that, when used correctly, helps improve the customer experience. And here's the bad news: Many smaller service providers are "too busy" to step back and assess what can be done to improve efficiency.

Two technologies, blockchain and artificial intelligence (AI), will become more than buzzwords used in articles. Blockchain has the potential to significantly reduce the costs associated with retirement plan administration (see the cover story in the Spring 2018 issue of *Plan Consultant*).

Though this article is directed primarily at TPAs, we will also discuss the impact of technology on customer service for recordkeepers and advisors. The rest of this article dives in to concepts (e.g., Robotic Process Automation) that you can implement today in your own organization.

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RECORDKEEPERS' PERSPECTIVE

One could say that the thing single biggest risk that we face every day as retirement professionals is the digitization of retirement plans. It's a disruption.

Some of the most well-known recordkeepers are leveraging technology to digitize most functions related to administration and recordkeeping. In many cases this eliminates the need for a TPA or a 3(16) fiduciary service provider. If complete payroll data is sent to a recordkeeper, and the rules-based environment that we work in receives the data, a system can be programmed to process the data based on those rules.

"Straight through processing" is a term all of us need to familiarize ourselves with. In simple terms, it can also be described as "data in, data out." This is how many of the major recordkeepers automate – or *intend* to automate – the experience for plan sponsors.

Most recordkeepers have already implemented programs to automate some functions. Many of our recordkeeping partners no longer need us to review vesting and triggering events with distributions. They have eligibility tracking built into their recordkeeping systems. Most are providing fulfillment services for some of their communications to participants. Their bundled service offering aims to provide a similar experience, with testing completion and reporting all done by having the plan sponsor upload a data file.

Are recordkeepers building these systems to minimize the role of a TPA? Absolutely not. They need to stay relevant and competitive, and the only way they can do that is through digital technology and automation. All retirement plan industry providers, but especially recordkeepers, are being pressured to lower costs. If margins are squeezed, there is less money left over to invest in customer service. This creates an opportunity for the TPA industry to provide consultative services on the administration of their plans, regulatory requirements, and plan design opportunities.

THE ADVISOR/CONSULTANT PERSPECTIVE

Many of the tools and technology improvements made by recordkeepers are created for either participants or plan advisors. Tools, in any application (think power saw), are designed to make a job easier to complete – that is, *if* the user is knowledgeable and experienced in completing the task. (You wouldn't want a participant using a tool without any training or knowledge, would you?)

I recently spoke with Tim Jaynes, a retirement plan consultant with ISC Financial Advisors, an independent wealth advisory firm based in Minneapolis, to get his perspective on the role of technology in delivering his service model. His comments didn't surprise me. He said, "Look, I'm thrilled that recordkeepers are investing heavily in technology advancements and tools. Many of them have made my job easier and improved the participant experience. However, it's a love/hate relationship. I'm concerned that the various recordkeepers are in a technology arms race, a race to produce flashy new tools without consulting advisors on how these tools are benefiting participants. With so much focus spent on what tools can be provided, not enough attention is spent evaluating what should and shouldn't be provided to the masses. Our team believes many of the tools that are readily available on most recordkeepers' websites are outright dangerous, as they can provide the users with a false sense of confidence regarding their financial well-being."

One example Tim provided was mobile phone applications. "This is my most hated technology advancement," he said. "Why would you want participants to be able to access their retirement account – a long-term savings vehicle – on their phones at all times? This is a recipe for disaster." He went on to say that there is "a mountain of evidence indicating that retail investors underperform buy-and-hold strategies when attempting to actively manage their own accounts."

Another breakthrough tool is the prevalence of retirement planning calculators on recordkeeper websites (see the cover story in the Summer 2019 issue of *Plan Consultant*). Tim indicated that it seems like a good idea, but in practice he has seen it do more harm than good. "In the last few months, my team has received calls from two participants who were about to give their notice to their employer and retire based on the retirement calculator provided by the recordkeeper," he says.

In one case, an individual employee of a plan sponsor was looking to retire and utilized the retirement plan calculator offered by the plan's recordkeeper. However, the employee had made significant input errors. The employee assumed a linear 9% annual return on his investment portfolio, but he was in a 60/40 investment allocation model that had no chance of achieving such a return. The Social Security income assumption was derived by the recordkeeper's calculator using his current salary. However, in the past he was self-employed for nearly 20 years at a significantly lower income

TECHNOLOGICAL ADVANCEMENTS SHOULD ALLOW A CLIENT RELATIONSHIP MANAGER TO BETTER SERVE ADVISORS AND PLAN SPONSORS BY HAVING THE TIME TO DEVELOP DEEPER RELATIONSHIPS.

than his current salary level. The employee also incorrectly entered his spouse's Social Security information and the savings rate for his retirement plan. Finally, the retirement plan calculator defaulted the amount of money the participant needed in retirement to 70% of what he makes today. This was $2,000 less than he needed per month. Over a 30-year retirement, this is a $1 million mistake! This participant (as well as the other one who called) decided not to retire.

As a plan consultant, Tim sees his role as counseling his plan sponsor clients and their employees through the available technology to create a retirement outcome. In effect, he is better able to serve his clients with the technology that is being provided by the recordkeeper. But like anything in life, in the hands of the wrong person, technology can wreak havoc.

THIRD-PARTY ADMINISTRATORS

One of the core responsibilities of a TPA is to make all the separate service providers of a retirement plan work together to create the desired outcome for the plan and the plan sponsor. As these "parts" start to talk to each other through technological improvements, the role of the TPA must evolve.

Many things that we used to do manually are now done by computers. Consider how we used to process a typical 401(k) loan. It was all via paper, received via a fax machine or the U.S. Postal Service. Now the process has been automated by recordkeepers to such a level that to get a loan processed, in most cases a TPA does not even need to be involved.

Quite frankly, most participants would rather just go online and make their request, especially when they find out it's a lot cheaper to request and process it online.

Now consider this new plan administration reality: Your client processes payroll using their payroll provider of choice, and the payroll data file (all the data needed for plan administration) gets pushed to data integrity software, which automatically checks it for errors and discrepancies. Once processed, the data integrity software pushes the data directly to the recordkeeper and/or to a plan compliance software system. The recordkeeper and the compliance software system receive the data, process it, and transactions are automatically executed based on that data. All of this requires very little human intervention. Eventually, it will just involve machines talking to machines, and the recordkeepers will be using payroll data that is 100% correct.

Now, you may believe that such a scenario is either impossible or years in the future. Actually, however, that scenario is here now, and has been in use since March 2018.

Integration by Robotic Process Automation

One of the newest tools in the service firm toolbox goes is called Robotic Process Automation (RPA). It is a form of automation based on the idea that "robots" are built to perform and automate repetitive tasks. (There are no actual robots – it's just a figure of speech that references software automatically executing a series of tasks, or commands, that otherwise might be done manually by a staff member.) The more repetitive and rule-based the task, the better RPA performs.

While RPA can take various forms, for this discussion we will focus on system-to-system

communication. As noted above, the job of a TPA is to make sure all the "parts" work together. The constraint with this goal is that the TPA does not control the underlying systems. This is where RPA comes in!

Imagine you have two systems owned by two different vendors that have no integration. As a TPA you can create an information hub where each independent vendor's data can be pushed (think File Transfer Protocol) or pulled (think Web Scraping). Once the data is received, a series of commands are given (scripted within software) to process, manipulate and finally communicate the data back to the end user. That end user can be a recordkeeper, your compliance software, a payroll system or the plan sponsor itself.

This is a technology that is readily accessible and available to the TPA industry. In fact, I know of a consortium of TPAs that are currently using and/or developing efficiencies using RPA.

The beauty of implementing RPA within the TPA community is that most of what we do is rule-based and repetitive in nature. Five years ago, I believed that I needed three or four operational staff for every client relationship manager. Boy, was I wrong! Today, I know it's just the opposite – I expect to need just one operational staff member for every three client relationship managers. Why? Because a lot of the operational activities can be performed by RPA.

In a smaller company, of course, the client relationship manager is performing both operational and client-facing duties. Technological advancements, therefore, should allow a client relationship manager to better serve advisors and plan sponsors by having the time to develop deeper relationships.

Payroll Data Integrity: Implementing Integration and Creating a New Service Model

It's been well documented in this magazine and others that one of the core components of successful plan administration is ensuring that you're working with complete and accurate payroll

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THE SINGLE BIGGEST RISK THAT WE FACE EVERY DAY AS RETIREMENT PROFESSIONALS IS THE DIGITIZATION OF RETIREMENT PLANS. IT'S A DISRUPTION.

data. In recent issues of *Plan Consultant*, there have been discussions of a payroll contribution upload service that is (or can be) offered by TPAs or 3(16) fiduciaries. Basically, the TPA logs in to the payroll provider's website (with their own or the employer's log-in credentials), downloads the data, ensures that it's in the right format, and uploads it to the recordkeeper. The TPA follows up on any feedback file that may be received from the recordkeeper.

One challenge is the difficulty of dealing with archaic payroll service providers. In our practice, we educate our plan sponsors on the importance of payroll data and having access to it, and help them find a payroll provider that has the technology to work with us as the TPA. (It takes anywhere from 45 to 90 days to convert a retirement plan from one platform to another. A payroll conversion can be done in as little as an hour.)

So, in that contribution service model, who is responsible for assuring the payroll data is correct? Back in February 2019, I was speaking with a leader of a major recordkeeper who indicated he believed that the future value of a TPA was to make sure the data that gets to the recordkeeper is accurate and complete.

Our job is to make our partners' and clients' lives better and easier. What creates chaos and difficulty for plan sponsors? Plan errors. And what causes plan errors? The answer, nearly always, is errors in payroll data. For any retirement recordkeeper to be effective, it must have good, clean, reliable data. Plan sponsors are solely responsible for ensuring that the data used is correct. Recordkeepers generally do not audit data, nor are they responsible for finding errors in payroll data. Some TPAs use Excel to sort through the data and look for errors or inconsistencies, but Excel has its limitations.

Payroll data errors occur often and are not checked by the recordkeeper, but simply used to execute tasks. Bad data sent to the recordkeeper creates a bad outcome for the plan sponsor.

Many plan sponsors assume that their payroll data and plan administration is correct. Yet the IRS and DOL find errors in many of the plan audits they conduct, and they have determined that the necessary internal controls to prevent these errors do not exist in most plans. (Unfortunately, the

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topic of payroll data integrity rarely comes up in a sales presentation.)

Payroll data errors are simple, surprisingly common, and can lead to increased fees from incorrect billing, required corrections, or IRS/DOL penalties. Every time mistakes happen, employees waste valuable time researching the issue, correcting the data, and resubmitting it. Even worse, mistakes are not found (if they are found at all) until the year-end audit is performed.

Accurate payroll data assures that the plan is managed consistent with the plan document and prevents these costly errors and consequences. Seeing the problem, we set out to design and automate a process for checking the integrity of data.

Through our data integrity check process, we find errors, big and small, in nearly 75% of payroll data files submitted to us. A few examples of categories we can check include all sources of contributions, census data integrity, eligibility calculations and confirmations, ongoing loan activity and monitoring, and vesting confirmations. We work with plan sponsors to solve these errors, assuring the data used in the payroll, HR and recordkeeper systems is correct.

Our proprietary software also allows us to quickly run these checks, whether a plan has two or 200,000 participants, and produces a report that details the actions we've taken and the errors we've corrected. The system reads payroll data on a per payroll basis and compares the data to the plan's provisions. It checks more than 150 data points, including census information and financial information to ensure compliance with the plan document and the integrity of the data.

The software platform is built primarily using Python and SQL as the programming languages. The front end of the platform has been written to allow for a variety of payroll format inputs (Excel, csv, text and JSON). All data is then uploaded to an Azure-based Microsoft SQL Server database. Here, the data can be queried directly, or custom reports can be generated using business intelligence (BI) software.

Depending on the size of the payroll file, the platform can dramatically decrease payroll analysis time and eliminate human error. This has proven to be especially valuable to larger employers.

CONCLUSION

When I first got into this business 15 years ago, I believed this was a business about communication, not about compliance. I still believe that more than ever. We can better serve our clients by utilizing the technology that has become affordable to smaller organizations.

You cannot automate retirement plan services completely. There are too many parts and service providers that need to be aligned to be successful. However, technology always creates a new door of opportunity for innovation. PC

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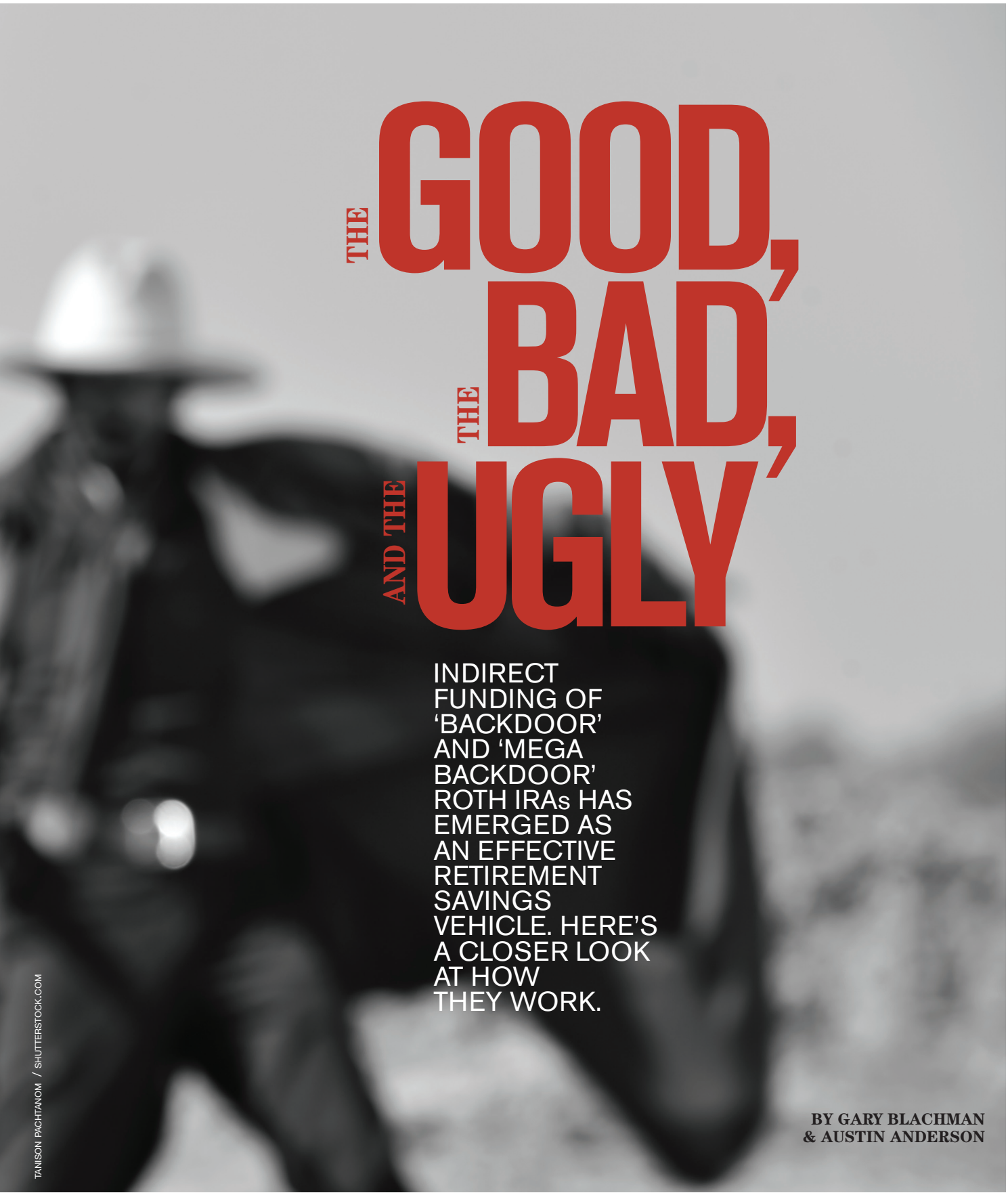

THE GOOD, THE BAD, AND THE UGLY

INDIRECT FUNDING OF 'BACKDOOR' AND 'MEGA BACKDOOR' ROTH IRAs HAS EMERGED AS AN EFFECTIVE RETIREMENT SAVINGS VEHICLE. HERE'S A CLOSER LOOK AT HOW THEY WORK.

BY GARY BLACHMAN & AUSTIN ANDERSON

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ROTH IRAs

have always been a powerful tool to save for retirement. Recently, they became even more powerful. Why? The 2017 Tax Cuts and Jobs Act created a lower income tax rate environment, which makes both contributions and conversions to a Roth IRA more appealing.

Roth IRA contributions are funded with after-tax dollars, which means taxes are paid up front and then the earnings can be withdrawn on a tax-free basis at retirement if certain conditions are satisfied. That's the good news. Additionally, Roth IRAs allow savers to avoid potentially higher tax rates in the future by paying tax at current rates.

IRA, one of the two *indirect* ways to fund a Roth IRA may be a viable option: the "backdoor" Roth IRA and the "mega backdoor" Roth IRA. That's definitely good news.

THE BACKDOOR ROTH IRA

In a backdoor Roth IRA, a contribution is initially made into a traditional IRA, and then the same contribution amount is immediately *converted* into a Roth IRA contribution. This can be done in one of two ways. First, you can contribute funds into an existing traditional IRA, immediately sell those assets before earnings are applied (to avoid taxes on the earnings), and then roll over those same assets into a tax-free Roth IRA account. Second, you can convert an entire traditional IRA account into a Roth IRA account.

Either of these strategies is an option for those prevented from depositing directly into a Roth IRA due to either the IRS annual contribution limits or the IRS income limits. In 2019, the IRS limit on contributions to a Roth IRA is $6,000 (or, $7,000 if over age 50). However, these

ONE OF THE TWO INDIRECT WAYS TO FUND A ROTH IRA MAY BE A VIABLE OPTION: THE BACKDOOR ROTH IRA AND THE MEGA BACKDOOR ROTH IRA. **THAT'S DEFINITELY GOOD NEWS.**

The bad news: Under IRS rules, individuals who earn over a specified amount in any given year are not permitted to contribute to Roth IRAs. In addition, the IRS limits the amount of annual direct contributions to a Roth IRA.

However, there are no income or contribution limits on *conversions* to a Roth IRA. For individuals who are limited by their income or who want to contribute more than the annual maximum ($6,000 in 2019) and may not be able to directly invest in a Roth

contribution limitations do not apply to backdoor Roth IRA conversions.

Additionally, a backdoor Roth IRA allows you to avoid the Roth IRA income limits. Specifically, in 2019 if your modified adjusted gross income (MAGI) is $137,000 (single) or $203,000 (married filing jointly or qualifying widow(er)), you may not contribute to a Roth IRA. However, these *income* limitations do not apply to backdoor Roth IRA conversions.

Cautionary Tax Implications of Backdoor Roth IRAs

Unfortunately, taxes cannot be avoided completely with a backdoor Roth IRA. For example, when converting a traditional IRA to a Roth IRA, taxes will be owed on

the entire conversion amount since you initially received an income tax deduction on the contributed amounts. As another example, if you contribute $7,000 (over age 50) to a traditional IRA, and then later convert only the $7,000 to a Roth IRA, you will owe taxes on the entire $7,000. Additionally, in both cases, taxes are owed on any earnings from the time of the initial contribution into the traditional IRA to when it is actually converted to the Roth IRA. Some might consider this the bad news.

then convert it to a Roth IRA, then only the earnings are taxed. However, if you have a $90,000 traditional IRA (pre-tax contributions), and convert a $10,000 non-deductible contribution to a new Roth IRA, the conversion would be 90% taxable. Essentially, this means that you could be looking at a much higher tax bill than anticipated for the privilege of converting a small portion to a Roth IRA – the really "ugly"!

Additionally, there is a time limitation on when you can access these Roth IRA funds tax-free. Specifically, since these funds are considered "converted funds" and not "contributions" to a Roth IRA, if you are under age 59½, there is a requirement to wait five years before gaining access to the converted funds on a tax- and penalty-free basis. If the funds had instead been "contributed" to an IRA, much like

TAXES ARE OWED ON ANY EARNINGS FROM THE TIME OF THE INITIAL CONTRIBUTION INTO THE TRADITIONAL IRA TO WHEN IT IS ACTUALLY CONVERTED TO THE ROTH IRA. **SOME MIGHT CONSIDER THIS THE BAD NEWS.**

Another downside is that converting to a Roth IRA could unwillingly push an individual into a higher tax bracket in the year the conversion is processed – the "ugly"! Of course, if your income is lower in a given tax year, then the conversion to a Roth IRA may be worthwhile in that tax year to take advantage of the lower tax rate.

Careful financial planning is also required to avoid the "pro-rata rule," which requires all IRAs to be aggregated to determine how much income tax is owed upon conversion. If you have no other IRAs, and open a $10,000 non-deductible IRA and funds are contributed in a regular 401(k) plan, then you can access the funds at age 59½, without the five-year waiting period, and the IRA contributions are tax- and penalty-free!

Finally, in order to invest in a backdoor Roth IRA for any given tax year, there is a requirement to have earned income, such as wages or self-employment income.

THE 'MEGA BACKDOOR' ROTH IRA

The mega backdoor Roth IRA is similar to the backdoor Roth IRA, but it converts after-tax contributions to a 401(k) plan into Roth contributions.

Let's assume Evan is age 60 and contributes the full $19,000 in a 401(k) plan year on a pre-tax basis, plus an additional $6,000 catch-up to his company 401(k) plan. Evan would like to also fund a Roth IRA because he wants to later withdraw these funds income tax-free, which he cannot do with his pre-tax 401(k) contributions. However, Evan is

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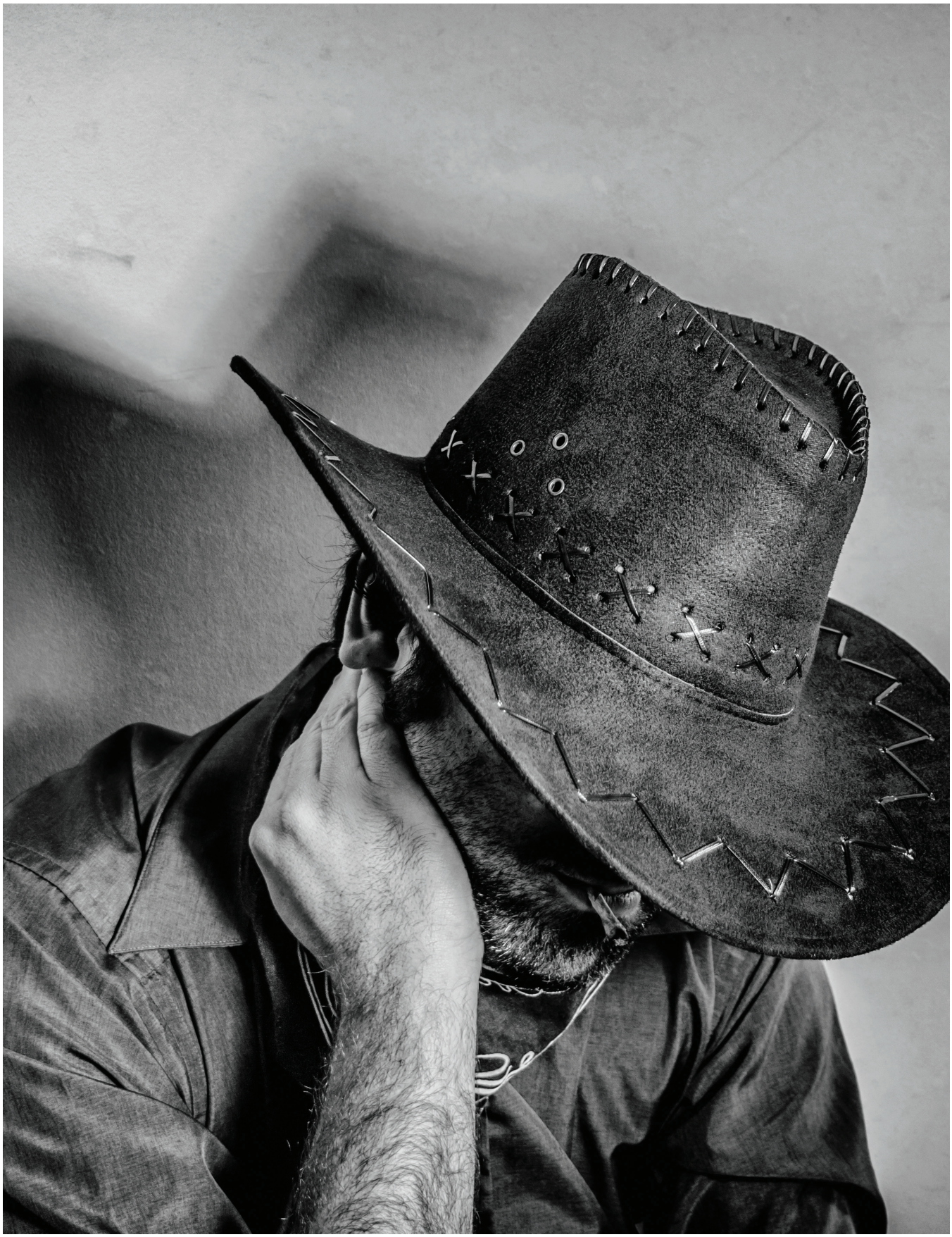

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CONVERTING TO A ROTH IRA COULD UNWILLINGLY PUSH AN INDIVIDUAL INTO A HIGHER TAX BRACKET IN THE YEAR THE CONVERSION IS PROCESSED – THE 'UGLY'!

phased out of *directly* funding a Roth IRA due to his income level.

Since there are no income limitations when making after-tax contributions into a 401(k) plan, he decides to save an additional $5,000 per year until age 65 for a total of $25,000 of after-tax contributions. When he retires, he can then move his $25,000 of after-tax money into a Roth IRA (the "mega backdoor"). He can also move any remaining pre-tax salary deferrals in his 401(k) plan, plus any after-tax earnings, into a traditional IRA.

Had Evan decided at retirement to only roll over available funds from his 401(k) plan into a Roth IRA (assuming he was not phased out due to his income level), then he would have been limited by the annual contribution maximum of $7,000 (in 2019, individual contributions are limited to $6,000, plus a $1,000 catch-up for being over age 50). However, by using a mega-backdoor Roth IRA through his company 401(k) plan, Evan increased the amount he could potentially save in a Roth IRA (e.g., from $7,000 to $25,000), which is really "good" news!

IS A BACKDOOR ROTH IRA STILL 'GOOD' DESPITE THE 'BAD' AND THE 'UGLY'?

One of the major benefits of a backdoor Roth IRA is that once the taxes are paid on the initial conversion, all of the growth accumulates tax-free. This can be a smart investment option for those who are in a lower tax bracket now than they may be in the future. Additionally, qualified withdrawals are income tax-free and there are no minimum required distributions on Roth IRAs. Also, any earnings on a Roth IRA can be withdrawn after age 59½ without any taxes or penalties, as long as the account is at least five years old.

For those who wish to provide an inheritance for their children, it is also possible to leave the Roth IRA to family members. Although there are some inheritance taxes for Roth IRAs, the principal investment can continue to grow tax-free during the owner's lifetime with no mandatory distributions, and then future distributions to family members will be tax-free. The potential tax savings could be really "good"!

For all these reasons, the backdoor and mega backdoor Roth IRA conversions are really "good" options for investors who do not need the tax advantages of a traditional IRA and want to reduce their overall tax bite in retirement. PC

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3(16) services

Questions to Consider

Take the time to think through these issues before you wade too deep into the 3(16) world.

By *Susan Perry*

AS A 3(16), QUESTIONS ARISE THAT WE NEVER ENCOUNTERED BEFORE. HERE ARE A FEW FOR YOU TO PONDER.

How do you know it's the participant?

Assume for this purpose that you approve distributions for a client. Participants in our scenario can call into the recordkeeper's 800 number and request a distribution. The recordkeeper mails the participant the form, and the participant completes it, signs it and mails it you. How do you know it's the participant's signature?

Or perhaps a participant needs help completing the distribution form. She calls you, the contact person listed on the form. How do you know it's the participant you are talking to?

What about a beneficiary of a death benefit? The recordkeeper's website says the beneficiary is Jane Doe, the daughter of John Doe. Jane calls to ask about the amount of money in John's account. How do you know you are talking to Jane?

For some recordkeepers, it is possible to verify a person's identity by confirming a Social Security number plus the PIN number for the online login. But for those who don't maintain websites for participants where they have PIN numbers, what's the right way to confirm identity or a signature?

Keep in mind that the presumption is that you are acting in a fiduciary capacity, so you must act as a prudent expert would. Anyone know of a prudent expert that we can use as the benchmark for identifying participants in a 3(16) capacity? If so, please email me and let me know.

Given that no one is officially an expert on this issue, you are going to have to establish reasonable (that is, at least to you) guidelines for these situations. Do you contact each participant to confirm their request at the time you receive it? If so, what number are you calling and how do you know the person who answers the phone is the participant? Do you send an email to their home email address, say an AOL account, and see if they respond? Where are you going to obtain this contact information?

What about a signature? Can we make participants sign a "signature card" when they first become eligible? Probably not. And signatures can change over time. We aren't handwriting experts. What is prudent in this situation?

If you don't already have prudent procedures in place to ensure you are actually talking to or receiving information from the participant, you should think about what works best for you and your organization.

What do you do with returned mail?

Perhaps you have been engaged to provide communications to participants for your clients. Perhaps you send the Summary Annual Report or the fee disclosure notice. Perhaps you need to issue a new SPD. Maybe you mail out the investment change notifications.

Let's say that the clients provide the addresses and you do the mailings in a timely way. Then the returned mail starts coming in. What do you do with it? Are you going to send the mailings back via certified mail to see if someone will respond? Are you going to run the

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participants with bad addresses through a locator service – probably for a fee that will be paid by the plan? If the participant is actively employed, perhaps contacting the plan sponsor to bug the participant to update their address would work. But what about those pesky terminated participants? How will you find them? And even if you finally located the participant and get the address correct, have you provided a timely mailing? And how much will this cost?

Will the cost be paid by the plan (i.e., primarily by the participants who keep their addresses up to date)? Most recordkeepers can pay us for the costs of distributions, and maybe even the locator costs, but what about when it's a notice and not a distribution that's involved?

Again, there are no right or wrong answers. DOL guidance is rather vague on what to do in these situations. I am still looking for the prudent bad address expert, so if you know one, please let me know. In the absence of this expert, you and your organization will need an appropriate procedure for these types of situations. Ignoring the issue completely is probably not acceptable.

What about enrolling rehires in a 403(b) plan?

I know, it's an odd combination, rehires and 403(b) plans, but the issue here is the automatic entry upon date of rehire or date of hire. Can you assist a plan sponsor with issuing enrollment materials to participants in these scenarios? Can you handle the match in these situations?

If an employee who previously participated in the plan is rehired, that employee is eligible to begin saving as of the date he or she is rehired. What information must be given to this employee? You can't help unless you are monitoring the client's payroll system every day for rehires, which seems outrageously expensive and time consuming. You and the recordkeeper likely won't see the rehired participant until the first payroll is processed after the rehire date, by which time the participant should have started saving already. How are these rehired participants identified?

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GIVEN THAT NO ONE IS OFFICIALLY AN EXPERT ON THIS ISSUE, YOU ARE GOING TO HAVE TO ESTABLISH REASONABLE (THAT IS, AT LEAST TO YOU) GUIDELINES FOR THESE SITUATIONS.

What information needs to be provided to a rehired participant? What procedures do you have in place to provide notices, enrollment forms or other information to these rehired participants? Do you rely on the plan sponsor solely for purposes of rehires to issue this information on the date of rehire? If not, is it acceptable to do these mailings once a month, or must you monitor a client with weekly payroll for rehired participants and handle this weekly?

A 403(b) plan has all of the issues of the rehired participant, because everyone is eligible from date of hire, at least for the deferrals. But, what if the match starts after 6 months of employment or 1 year of service? Some recordkeepers can't track the second eligibility date. How does the plan sponsor know to start up the match? Are you responsible for determining eligibility for the match in this situation, or are you going to rely on the client to do it?

This is another area where you need to think about your processes and procedures.

Why do plans with an hours requirement for eligibility always seem to be messed up?

Hours worked/credited is a critical piece of data in determining eligibility. Many plan documents require that hours be counted during the first year of employment (or "anniversary date hours"). In the next plan year, the counting of hours switches to plan year hours. In probably all payroll systems, however, data is not tracked in this manner; all you have is YTD hours. Therefore, one can't expect the payroll system or the recordkeeper to get this right.

If you have a plan with a year-of-service requirement for entry (i.e., 12 months from date of hire in which the employee completes 1,000 hours), unless you or the plan sponsor is tracking or calculating anniversary hours and overriding the recordkeeping and/or payroll systems, no one has the data to do the calculations.

Most of us use a year of service as the entry requirement for the majority of our smaller plans. We don't consider that the correct data can't simply be downloaded from payroll.

What process and procedures do you use to determine the correct eligibility date when issuing enrollment kits?

Why do loans get overpaid?

Another payroll system fact goes like this: Payroll systems can set up a loan deduction start date, but few systems allow for a reliable deduction end date, or for a total amount of principal plus interest to be paid.

The last loan repayment is rarely for exactly the same amount as the other loan repayments due to rounding. Also, amortization schedules don't allow for leaves of absence, unpaid vacations or other infrequent interruptions of payroll deductions. What if a participant prepays a part of their loan? Payroll systems just keep deductions until they are told to stop. But who will address these issues as they occur, let alone 5 years from now?

While some recordkeepers may attempt to provide some of this information to the administrator via the file that is sent every payday, or on the recordkeeper's website, it will require a 3(16) administrator to go digging for the amounts and for the adjustments.

It's no wonder that loans get overpaid. Are you responsible for ensuring that loans default at the proper time? If so, what procedures do you have in place to account for the issues relating to the final loan repayment? Do you educate your clients on this issue? Is this your responsibility?

Conclusion

Depending on the 3(16) services that you provide, you may need to wrestle with these questions. Take the time to think through these issues before you wade too deep into the 3(16) world. There are no official right answers, oftentimes only more questions. Welcome to being a 3(16)! PC

Susan Perry, ERPA, CPC, QPA, QKA, QPFA, is the President of Fiduciary Outsourcing, LLC. She has more than 25 years of experience managing daily valuation recordkeeping as well as managing a TPA with more than 25 employees.

Are You a Target for Cyber Thieves? (Part 2)

The average cost of a data breach is more than $1 million, including lost productivity, negative customer experiences, and loss of reputation. Don't let it happen to your firm.

BY DAVID J. DISCENZA

Editor's Note: The is the conclusion of a two-part series. Part 1 appeared in the Summer issue.

In Part 1 of this article we saw how cyberthieves look for "backdoor" access to large companies through their vendors who may not be taking cybersecurity seriously. We looked at how cyberthieves stage external attacks on small businesses through the use of "phishing" and malware.

In Part 2, we'll look at how cyberthieves can attack from within a company and discuss strategies for keeping them from succeeding. We'll also consider a sobering, real life story of how retirements accounts were successfully attacked.

INTERNAL ATTACKS

Physical Security Threats

A physical security threat occurs whenever someone gains access to one of your devices. This can happen when you accidently leave your computer without "locking out" the screen. It can happen if your cell phone is lost or stolen.

Here's a sobering statistic: 60% of attacks that occurred in 2016 came from within companies. Of those 60% of attacks, three-quarters were intentional. An unattended, open device is an invitation for an attack.

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Here are some things that you can do to protect yourself and your company from physical security threats:

- Change your password on a regular basis.
- Use strong passwords that contain numbers, capital and lowercase letters, special characters like @,!,$,(,), and are at least eight characters in length.
- Physically secure your laptop by using a docking port that's secured to your desk.
- Do not store sensitive information on your laptop or phone; use a "cloud" service instead.
- When travelling, never let your laptop out of your sight.
- Never allow someone to put a memory stick in any of your computer's USB ports.
- Never use a memory stick to save data unless the data is automatically encrypted.

UNSECURED NETWORKS

Nearly every place you travel in this country and in others, you'll find "free wifi." Your favorite coffee shop has it. So does your grocery store. You can connect to it at rest areas along the highway. Do you have a boat? I'll bet your marina has free wifi. It's everywhere.

It's also a favorite means cybercriminals use to steal your information or hack into your phone or your laptop. How do they do it?

Public wifi is always unsecured. While it may require a password to access, everyone has access to the password, especially when it's posted somewhere for all to see. Cybercriminals can hang out in the same coffee shop with you and steal any information you transmit over the public network. Another tactic they use is to create their own wifi "hotspot" with a name very close to the name of a nearby public wifi network. The network you connect to is theirs, and they'll steal any and all information they can, plus hack into your device for more.

Here's what you can do to protect yourself:

- If you must use public wifi, do not access any password-protected websites like your bank account, social media accounts, or email.
- Install Virtual Private Network (VPN) software on your computer and phone, which will allow you to securely use public wifi by "hiding" the identity of your computer or phone and giving you a secured network on which you can access websites.
- If you connect from home, make certain your home wifi router uses WiFi Protected Access 2 (WPA2), and create a strong password as described above.

A CAUTIONARY TRUE STORY

One of the reasons why cybercriminals still succeed in their efforts is because people believe that it can't happen to them. Hopefully this two-part article has convinced you that you and your firm are just the type of target that's most vulnerable to their efforts. If not, then consider this true story.

Great-West Financial is a century-old financial services firm which offers, among other products, private-label recordkeeping and administrative services for other providers of defined contribution plans through their Empower Retirement brand. An internal audit uncovered a fraud scheme in which nearly $2 million had been stolen from retirement accounts. Here's how it happened.

Between November 2016 and February 2017, three individuals obtained the personal identification information of account holders of retirement funds managed by Great-West. How and from where this information was obtained is still not clear. What is clear is that the three individuals were able to access the funds and begin making withdrawals. The money was wired through a variety of accounts until it was finally wired to a bank in Malaysia.

While it's not known how exactly the three individuals obtained the personal identification information of the account holders, it's clear that the information was stolen. The individuals targeted only people with accounts managed by Great-West. It could have come from Great-West, or it could have come through the breach of a third-party administrator.

SUMMARY

Cybercriminals are relentless in their efforts to steal information that they can convert into cash. They do it because the profit is big and the risk of being caught is low. It is everyone's responsibility to make it as hard as possible for them to succeed. Here's what you must do:

- Become sensitive to "phishing" email attacks – look for signs of fraudulent emails.
- Use a form of two-factor identification by sending a separate email to the original sender of a suspicious email to verify whether it's authentic or fraudulent.
- Keep your laptop and phone operating systems up to date, and make certain you have anti-virus software on all your devices.
- Protect the physical security of all your devices.
- Never use public wifi without using Virtual Private Network software.

We will never completely defeat cybercriminals. With greater awareness and vigilance, however, you can reduce their success in finding an open back door in your system. PC

David J. Discenza, CBCP, is president of Discenza Business Continuity Solutions. His firm provides operational risk management consulting to businesses primarily in the Mid-Atlantic region.

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Working with Taft Hartley Plans

Multiemployer plans are facing numerous challenges today. Here's a closer look.

BY SHANNON MALONEY

The financial markets and investment portfolios of most of our DC clients are prospering, yet limping under the radar are Taft Hartley plans (a.k.a. multiemployer plans). Understanding the unique challenges faced by these plans is imperative to the successful retirement of millions of American workers.

Today there are more than 10 million workers covered by roughly 1,400 multiemployer plans. *(PBGC)* They were created by the 1947 Labor and Management Relations Act sponsored by Robert Taft of Ohio and Fred Hartley of New Jersey. In the years since then, these plans have enabled millions of union members to earn pension benefits while working for various employers.

In order to serve Taft Hartley plans well, it is important to understand the players involved. Most plans are governed by a board of trustees, with labor and management (often from several competing employers) equally represented. Contributions are made by employers, and are collectively bargained. Administration of the plan is often done by the Fund Office. Assets are held in trust, and the plan trustees may hire and retain investment professionals to assist with the management of the investment policy for the funds.

Not only are the players different in Taft Hartley plans, but there is a significant cultural component that should be understood and embraced by the providers working with them. The primary mission of the union (represented by the Fund Office) – whether it's the local, national or international – is building a secure future for its members through advocacy and benefits.

While all pension plans face daunting problems in today's environment, Taft Hartley plans are in a class by themselves. Let's take a closer look at these challenges.

DEMOGRAPHIC CHALLENGES

1. A demographic profile with more retirees than actives results in greater net outflows than inflows. This heightens the need for return and liquidity management.
2. A diverse workforce working with various employers over the life of a career.
3. Movement of jobs outside the U.S. complicates the accuracy of hours-worked forecasting and other projections.
4. Employer participation in Taft Hartley plans remains steady or decreasing (through merger/acquisition, bankruptcy and payment of withdrawal liabilities).

The composition of trustees can create governance issues due to member-management relations. The union trustees represent different member groups, including retirees, former participants and active members, each of which may have different concerns and risk profiles. The management constituents can be even more aggravated, as each participating employer has different operating objectives and constraints. This sets the stage for some of the plan governance issues.

PLAN GOVERNANCE CHALLENGES

1. Fiduciary responsibilities continue to increase and include training, adherence to the prudent man rule and documentation requirements. All trustees should take advantage of training (fiduciary, investment, plan design, plan governance) with their independent consultant and/or from the International Foundation of Employee Benefit Plans, which focuses on multiemployer plans.
2. Ensure that plan design is flexible enough to support the necessary trade-offs between contributions, benefits and risk.
3. Past regulations have contributed to the underfunding of these plans. Prior to the Pension Protection Act of 2006, multiemployer plans were penalized from maintaining a funding percentage higher than 90%. As a result, many Taft Hartley plans increased benefit levels during booming markets that can no longer be sustained. Also, when markets corrected or

turned downwards, anti-cutback rules restricted trustees' ability to correct the inflated benefit levels.

4. Current requirements such as the Multiemployer Pension Relief Act of 2014 have not resulted in the expected increase in funded status and decrease in the funding gap. The PPA zones which this legislation created generate a need for solvency in the plans and have thereby initiated a pressing need for return generation (which may or may not constitute acceptable risk to the constituents of the committee).

Both management and union trustees are committed to keeping the plans healthy and open to new hires, and eventually increasing benefits. However, many Taft Hartley plans have yet to reach the funding status they had in 2007 prior to the financial crisis.

Due to the bull market of the last decade, most plans are recognizing that market-based returns alone will not close the asset-liability gap. Plans invest in a diversified portfolio to try to achieve investment returns that can support higher benefit levels and lower contribution requirements, but that is easier said than done. These challenges include those affecting plan health, monitoring risk, and managing projections. We'll look at each of those next.

PLAN HEALTH

There are three ways to improve funded status for the plan:

1. Sustained market returns above the return-on-asset assumption already built into the actuarial assumptions.
2. Asking employers and members to contribute more to the pension plan as part of the collective bargaining process. While on paper this strategy is the easiest, it is difficult to put into action. Many union members are disgruntled because they have increased their contribution, yet their benefit remains the same. Many employers have begun looking at withdrawal liabilities to prevent increases to contributions to the plan. And lastly, the amount that the pension receives from the increase should be compared to

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> “While all pension plans face daunting problems in today’s environment, Taft Hartley plans are in a class by themselves.”

the amount needed – there still may be a shortfall if the amount requested for the pension is not approved.

3. Portfolio asset allocation changes to increase alpha-generating opportunities. This usually involves increasing the equity component of the plan and possibly adding alternative investments. Adding a payment account/stable value fund (eligible for DB plans) to receive contributions and make payments to retirees is an important consideration so that the fund managers are not selling into the market at inopportune moments to raise capital to fund monthly retiree benefits.

MONITORING RISK

The diverse makeup of the trustees may lead to a struggle with making complex investment decisions and ensuring their timely execution. Risks must be monitored continually and communicated proactively so that decisions can be made at the most opportune time.

Thirty-five years ago, it was relatively simple to achieve the plan’s long-term return on asset (ROA) assumptions of 7%-8% using mostly fixed income instruments and cash with low risk. To achieve that same long-term ROA today, the plan must adopt much more risk – which must be understood and monitored by the trustees. It is important for the investment consultant to understand and incorporate the risk tolerance of the board into the asset allocation.

Today, it is important to have a process in place for analyzing, reviewing and understanding the impact of long-term return projections on pension funded status. In addition, this analysis should include the risk required to achieve the long-term ROA. Most Taft Hartley plans have hired an investment consultant to review the overall portfolio allocation, provide investment reporting for assets compared to appropriate benchmarks, and help advise the trustees when they make certain decisions. In fact, the investment component is so important that many larger plans have hired an outside Chief Investment Officer to reduce trustees’ liability and provide a strategic focus for the plan.

MONITORING AND USING PROJECTIONS

Projections can be a challenge due to disagreements about the outcome and probability of the projection. However, projections are important for the trustees to understand the impact of various factors on the funded status (positive and negative consequences). They are also useful to determine whether the plan is getting healthier or not, as well as which steps are working and which ones need to be revised.

It may be prudent for trustees to assess the plan’s funded status using multiple metrics in order to ascertain the size of the asset-liability gap. Using only one metric may distort the health of the plan.

The capital market assumptions for the next 5 years are substantially lower than they were over the course of the past decade. Reviewing the ROA considering current capital market assumptions and its impact on liabilities is an important projection and guidepost for trustees.

CONCLUSION

These challenges can seem daunting, but with a good strategic plan, dedicated trustees, and competent providers, today’s outlook is hopeful. While it is true that some Taft Hartley plans impacted by the financial crisis face an uncertain future, many more will continue to serve the needs of their members and pensioners for years to come. PC

Shannon Maloney is a co-founder and Managing Director with Strategic Retirement Partners. She has been serving retirement plans for more than 25 years.

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How and Why Are TPAs Reviewed?

The TPA evaluation process is becoming more and more prevalent as potential partners recognize that they should be doing a much deeper dive.

BY JASON BROWN

Our team was asked during a recent meeting whether TPA firms are vetted by recordkeepers (RKs), broker-dealers (BDs) and registered investment advisory (RIA) firms – and if they are, what are the most important aspects that typically get asked in the review process?

Well, our firm can speak firsthand in saying yes, TPAs are evaluated frequently, and it just so happens that we went through this process recently with a prominent BD. The information requested is very similar to a Request for Proposal (RFP) but dives deeper into a TPA business's overall structure, systems and sustainability. It's not quite at the level of the CEFEX Certification process, but somewhere in between.

This evaluation process is becoming more and more prevalent as parties recognize that they should be doing a much deeper dive, considering the technical, regulatory and legal environments in the industry. Each entity (whether BD, RK or RIA) has its own templated version of questions and points of interest. However, there always appear to be

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three primary areas of consideration and focus during this evaluation:

- scale, scope and sustainability;
- qualifications of staff; and
- systems and processes.

Of course, in each of these areas there are specific questions related to that topic. So let's take a look at what normally gets asked and why these points of interest are of significance.

SCALE, SCOPE AND SUSTAINABILITY

Scale, scope, and sustainability are important considerations when evaluating any retirement plan service provider, let alone a TPA. Why are these items important? Well, it speaks to the staying power and prospective longevity of a given firm.

One only needs to look at the recent history of the RK and TPA spaces to get a glimpse of where the overall retirement plan industry is heading. In 2007 the top 10 RK firms held approximately 50% of the DC market, and in 2017 the top 10 RK firms held roughly 70% of the DC market, which is being driven by both organic growth and acquisitions of other firms wanting to get out of the business. In the past five years, we have seen the TPA market go from approximately 2,100 TPAs nationally to roughly 1,800 today.

What this equates to in the evaluation process is that if a TPA is not at a certain level in current plan count and doesn't consistently bring in a strong amount of new business annually, it might not be a viable long-term partner. Annual increases in plan count and revenue are important because not only are they vital for growth, but they also show replacement capabilities for plans that leave through attrition. It primarily comes down to this: If the firm is not growing, the perception is that it will either be acquired or eventually go out of business.

This dynamic also comes into play on another level for financial advisors, as most should be evaluating the maturity of a given TPA for their succession planning purposes. I'm sure most financial advisors would say they do not want a TPA selling or retiring on a book of business anywhere near their personally planned exit strategy.

Here are some of the major considerations in this area:

- Dedicated business development personnel
- Number of plans
- Total assets of plans
- Average annual growth (number of plans, participants and assets)

> Scale, scope, and sustainability are important considerations when evaluating any retirement plan service provider, let alone a TPA.

- Retention rate of clients
- States/cities where the firm operates
- Professional society affiliations
- Recordkeeper relations
- Payroll connections

QUALIFICATIONS OF THE STAFF

The backbone of any top-quality TPA is a deep, experienced and qualified staff. After all, those are the people doing a majority of the heavy lifting concerning compliance testing and providing plan operational guidance. That is why most of the TPA vetting inquiries from RKs, BDs or RIAs include questions to better understand the quality and technical expertise of the people doing the work.

Just saying that a TPA does administration work doesn't paint the full picture of the level of consulting that can be provided or the quality and accuracy of the work that is produced. That is why it is vitally important for firms to know the experience and credentials (ERPAs, QKAs, QPAs, APAs, APRs, CBCs, etc.) of a TPA's staff.

My firm has always envisioned this section as treating a TPA like a restaurant. Sure, there may be a lot of similar items on the menu at other restaurants, but the difference in the flavors and how good the food tastes relies solely on the talents of their chefs. In the same vein, this process is helping to determine the quality of the "administration chefs" that are doing the "cooking" for a given TPA.

The primary points of consideration in this area are:

- Number of staff members
- Staff training program
- How many staff members are credentialed
- What designations are held by staff members
- Is a dedicated Relationship Manager (RM) assigned?
- The average caseload of the RM
- Timeliness and accuracy of work and responses
- Can the firm offer IRS/DOL audit assistance?

SYSTEMS AND PROCESSES

The items in this section are becoming more prominent points of discussion in finals presentations and national conferences, so naturally, RKs, BDs, and RIAs are following suit in inquiring about those areas. In recent finals presentations, for example, our firm has been asked to produce our cybersecurity insurance policy and credit monitoring coverage just in case a security breach ever occurs. In this area, firms are wanting to know that a TPA offers full fee transparency and insurance to help mitigate operational risk, and that IT security measures are in place for breach prevention purposes.

That is why going through a process like CEFEX Certification (a joint certification process through the Centre of Fiduciary Excellence and ASPPA) can be such a significant difference-maker for a TPA. It indicates on an independent basis that the firm can demonstrate adherence to the industry's best practices and is positioned to serve fiduciaries such as investment advisors, investment managers and investment stewards (e.g., plan sponsors) in the metrics listed below (as well as other areas). It is never a detriment to have a reputable outside firm validate to the market that you are doing these things well.

- Fee clarity
- Disclosure of revenue sharing practices
- Cybersecurity measures
- Encryption capabilities
- Cybersecurity insurance
- Errors & Omissions insurance
- Documented business continuity plan and disaster recovery plan

WHAT DO ALL THE RESPONSES AND DATA MEAN?

At the end of the day, all any RK, BD or RIA looking to engage with a TPA partner wants to know is that the firm does quality work, has experienced and credentialed staff, and has the scalability to be a long-term strategic partner. Going through this review process is a great exercise to help validate that a TPA has the resources and infrastructure to accomplish that goal. PC

Jason Brown, APR, CPC, is a principal with Benefit Plans, Plus, LLC in Ft. Wayne, IN. He has more than 15 years of experience in the retirement industry and is a member of the Plan Consultant committee.

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Training Your Staff on Confidentiality

Inexperienced subordinates may be especially vulnerable to professionalism violations.

BY LAUREN BLOOM

In a previous article, we discussed Sharon, a busy third-party administrator who hired Tony, a willing but inexperienced assistant, to help with her growing practice. As we saw, the training that Sharon gave Tony – especially on professionalism – was sporadic at best. Under Section 10 of the American Retirement Association's *Code of Professional Conduct,* however, Sharon has to take reasonable steps to ensure that work done under her supervision is performed with honesty, integrity, skill and care. We examined ways that Sharon could better train Tony, reducing his risk of making accidental errors that could compromise them both.

In this article, we will examine a professionalism violation to which inexperienced subordinates may be especially vulnerable. Employees now entering the workforce have grown up with with 24-7 access to the internet and, in most cases, substantial exposure to social media. For them, sharing information can be as natural as breathing.

Protecting confidential information may be difficult for these employees. However, Section Five of the Code requires ARA members not to disclose confidential information obtained while rendering professional services for a principal without the principal's permission or a legal requirement to do so. As an ARA member, Sharon is obliged to protect the confidentiality of her clients' information. To fulfill that obligation, Sharon needs to ensure that Tony does so as well.

Unfortunately, Tony had an absolute genius for oversharing. When he began working for Sharon, Tony was on social media several times a day, sharing amusing stories with friends and family.

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Sharon thought it was harmless until a client, Jon, called to complain that Tony had posted on Facebook a funny but unflattering photo of him taken at a pool party that Sharon had hosted for her clients. Sharon apologized, of course, and immediately asked Tony to take the picture down. By then, however, several of the other party guests had seen and commented on the photo. Thankfully, Jon proved to be a good sport, and he agreed let the matter drop when Sharon promised it wouldn't happen again.

Tony told Sharon he was very sorry to have embarrassed Jon and promised to be more careful about what he posted on Facebook. Sharon believed Tony had learned his lesson, and privately thought that Jon had been too sensitive. She took Tony off Jon's account for a while and resolved to do Jon's work herself until the incident had been forgotten.

Eager to make up for his mistake, Tony decided to surprise Sharon by upgrading her professional website. His redesign looked sharp and modern, and Tony was so confident that Sharon would love it that he didn't show it to her before posting it on a Friday afternoon. Sharon did love it… until she discovered that Tony had added a "What We Do" page that featured identifiable, confidential information about several of her clients' plans and participants.

Tony had already left for the weekend, but Sharon resolved to discuss client confidentiality with him first thing Monday morning.

On Saturday, Tony went out for drinks with friends. Talk turned to work, and Tony began complaining about a client, Ruth, talking loudly and specifically about plan problems that Ruth would definitely want kept confidential. Unbeknownst to Tony, Ruth's daughter was seated at the next table. She went home, told her mother what she'd heard, and Ruth fired Sharon by phone the following day.

Though she was angry, Sharon quickly realized that the fault was partially hers. She had never trained Tony on client confidentiality, presuming that he would understand its importance. Their conversation about Jon had focused on the importance of never embarrassing a client, not on protecting confidential information. Sharon realized that she had some training to do.

When Tony arrived at work on Monday morning, Sharon was waiting for him with a copy of the ARA *Code of Professional Conduct*. She told Tony about Ruth's call, cutting off his stammered apologies and assuring him that neither of them would leave for the day until he was thoroughly instructed in client confidentiality. They sat down and reviewed a dozen different plans together, with Sharon showing Tony the information that had to be kept confidential for each. Tony asked good questions and seemed to understand what was required. Sharon then asked him how to address several hypothetical situations and was pleased with his responses.

There was only one area of friction between them. Tony, eager to test the limits of confidentiality, wanted Sharon's okay to ask clients for permission to disclose their information. He also grilled Sharon about situations where disclosure is required by law. Sharon insisted that any requests to clients for permission to disclose come from her, not Tony. She also told him that any legal requirements to disclose would be addressed by her, not him, with advice from the firm's attorney. Tony was frustrated, but his recent string of mistakes gave Sharon ample reason to insist that he leave disclosure to her. Eventually, Tony admitted that Sharon was right.

> "Section Five of the Code requires ARA members not to disclose confidential information obtained while rendering professional services for a principal without the principal's permission or a legal requirement to do so."

Sharon gave Tony lots of good instruction on client confidentiality. But perhaps the best advice she offered was to remember that breaching confidentiality presents unique challenges. Many other professionalism violations can be corrected with enough effort. Once confidential information has been improperly disclosed, however, it can difficult, if not impossible, to call it back. With Sharon's help, Tony finally understood the importance of confidentiality, benefitting both Sharon and her clients. PC

Lauren Bloom is an attorney who speaks, writes and consults on business ethics and litigation risk management.

I Came to a Formative Fork in the Road… and I Took it

Empowering employees requires flexibility and 'boots-on-the-ground' understanding. Using formative assessment can help.

BY BRIAN KALLBACK

"Are you on track?" is a commonly used phrase in today's retirement industry. In the world of recordkeepers, TPAs and plan sponsors, "Are you on track?" allows employees to check progress towards retirement goals. Whether based on personalized data, historical averages or peer group comparison, employees have the ability to gauge where they fall on a range of possibilities. However, "Are you on track?" doesn't necessarily gauge individual understanding.

Education platforms and tools have allowed employees further control, self-direction and flexibility to determine progress toward a financially secure retirement. However, not every employee is comfortable with the transition from face-to-face, relational education meetings to an on-demand digital universe. Oftentimes, employees state they do not understand what "all that" is on the screen. Many want confirmation from a real person. Employees believe that "finance everywhere – from retirement assets to investments … is … complicated by the complexity in which finance shrouds itself – mind-numbing acronyms, formulae, and spreadsheets serve as barriers to understanding." *(Desai, 2018, p. 1)* Our profession is confusing to many of the very people we wish to serve.

Digital education platforms can only go so far in creating understanding. Employees engage with technology either because they understand it or because they are guided through their dependency. But what is the ultimate objective? If we want employees to save for retirement, then our digital, auto features can serve us well. But, if we're striving for engagement as defined as a knowledgeable, intentional employee

> “Efforts to design a curriculum to measure whether learning, progress, and empowerment are occurring can be aided by the incorporation of formative assessment.”

base, then digital features serve as a short-term solution for participation and marketing rather than life-changing engagement.

Building a knowledgeable, intentional employee base starts with building strong, individual relationships with employees. This will not occur if we're always trying to sell annuities or proprietary mutual funds, or if we view onsite education meetings as a low-margin activity that should be minimized.

An effort to design a curriculum to measure whether learning, progress and empowerment are occurring can be aided by the incorporation of formative assessment.

WHAT IS FORMATIVE ASSESSMENT?

Formative assessment is used *throughout* an education session or longer learning unit to assess employee understanding of a financial or behavioral topic *while* the learning is occurring. Formative assessment provides “feedback to the learner *during* an instructional sequence or learning activity that is aimed at helping the learner succeed. *Timely and informative feedback* is essential for formative assessment to be effective.” *(Bhagat, 2017, p. 312)* Summative assessment, which is used at the conclusion of a unit or session, evaluates whether an employee learned the overall objectives (see below).

Formative Assessment	Summative Assessment
• Questioning • Discussion • Practice presentations or projects • Peer/self-assessments • Journals • Individual white boards • Simulations / games • Instant feedback via audience apps • Progress towards retirement objectives	• End-of-unit exams, quizzes • Semester exams • ACT/SAT-type exams • ASPPA certificate exams • Final recital • Presentations • Final projects • Surveys • Financial metrics at retirement
Helps an educator modify future lesson planning based on employee needs throughout the learning process	***Used to determine – at a particular point in time – what an employee knows and does not know***

Formative assessments are often written for incremental learning targets rather than unit objectives. An example is understanding how employees feel about Social Security (“My dad died young, so I'm taking mine at 62! I'm not letting the government take my money any longer than necessary!”) as we discuss the strategies and idea behind the program. Knowing these opinions allows us instant feedback and direction as we adjust our tone or message (but not necessarily the content). In my own experience, this interaction allows me, as an educator and presenter, to engage the audience and direct my examples to the situation at hand. This flexibility in presentation is an example of formative assessment and timely feedback.

Formative assessment can also be used to “scaffold [employees'] learning.” *(Clinchot, 2017, p. 72)* Scaffolding is when we build on prior knowledge and experiences to strengthen overall understanding.

Research follows that the “assessment approach we adopt in a given situation is likely influenced by various factors, including our teaching goals, standardized test outcomes, past experiences, knowledge of current students, and a depth of our own content knowledge, together with our interpretation of what the assessment task assesses.” *(Clinchot, 2017, p. 72)* Especially when educating adults, past experiences with learning situations (such as previous classroom success) impacts our ability to positively influence retirement outcomes. By

scaffolding, we can slowly build knowledge and confidence rather than throwing the employee into the deep end without a life vest.

To attempt to understand our employee base and the "variety of factors" that affect eventual success, an employee census and a digital platform can provide a bit of initial information. "Cutting-edge technology (such as data aggregation and revealed preferences tools) [can be used] to get a more evidence-based, holistic picture of a client's actual financial behaviors and underlying values and preferences." *(Spenner, 2019, p. 16)* Time spent on preliminary research is useful in determining an appropriate formative assessment strategy. When I know an audience beforehand, even slightly, I can mentally prepare my presentation and materials to speak directly to their pain and past.

Today's wealth of digital tools allows recordkeepers, TPAs and plan sponsors to learn about employee actions and digital engagement. Yet, face-to-face meetings are often lacking in formative assessment strategies. Empowering employees requires flexibility and "boots-on-the-ground" understanding. Training your education team on formative strategies will strengthen effectiveness and engagement. PC

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You Don't Have to Put the 'F' in Failure

Making mistakes – and becoming a better practitioner for it.

BY ALISON J. COHEN

As you pull out last year's valuation and testing package in preparation of the kick-off to the current year's work, you notice something. At first, you don't think you're seeing things correctly, so you double-check yourself. Then that knot starts to form in the pit of your stomach. Maybe your throat gets dry or your hands get clammy.

You found a mistake.

At this point, as the feeling of dread and panic starts to creep over you like a dense London fog, you remain immobile and uncertain what to do next. Your brain just keeps focusing on the problem. So what should you do? (The answer is never "shoot the hostage," as cool as Keanu Reeves made that sound in the movie *Speed*. And pretending it didn't happen isn't the right answer either.)

STEP 1: BREATHE

The first step is always to breathe. Seriously. When your brain goes into panic and shock, certain parts of it light up and hijack your ability to think rationally. Taking a minute to close your eyes and take a few deep breaths helps to bring the rest of your brain back online. This is important, because we're going to need all those brainy parts to think through the problem and come up with a plan of action to solve it.

Here's the other thing: No matter what you did or didn't do, no one's life is on the line and no one is going to burn for eternity. Remember that you are not the only person who has ever made a mistake. It's just part of being human. But, rather than avoid and bury the episode, instead we can use it as an opportunity to improve our skills and our practice.

STEP 2: ASSESS THE SITUATION

Once your brain has arrived at the party, you need to objectively assess the situation and determine a number of things:

- How did the error occur?
- Who caused it? Or was it a group effort?
- What are the possible solutions?
- Is there a cost to the solution?
- Could the error have been avoided somehow?
- Can you make the correction on your own?

Understanding how the error occurred is more difficult than it sounds, because our ability to wipe away our predispositions and biases is a learned skill and not our default reaction. The majority of people will go one of two ways – either they will blame themselves immediately for everything, even when it's not their fault, or they will blame everyone else for everything, even when it's their fault. The assessment of the error needs to be as neutral and unbiased as possible. If you think you are unable to do this on your own, you can always ask a trusted colleague to look at the situation for you. Figuring out how the error occurred is important, because not only does it tell you whether there are procedures that need to be tightened up; it also reveals options for correcting the error.

Identifying who caused the error is not for finger-pointing purposes. Eventually you're going to have to talk to the client about it, and it is important to determine how to present that narrative. Remember: Clients are human, too, and when confronted with a mistake that they made, they

will have the same responses that you did. You need to take that into consideration when you prepare for the discussion.

If the error was your fault, you need to talk to your legal counsel first before talking to the client. Even though you are covered by E&O insurance, if you talk to the client and tell them how terribly sorry you are, you may have just voided your coverage. Discussing how to notify the insurance company and the client is a tactical decision that needs to be made with care.

Regardless of who caused the error – and most times it's a collective effort – it is important to always bring the solutions and the specifics to the table with you. No one wants to hear that the kitchen is on fire without also hearing that you have a fire extinguisher.

That means that you should have already scoped out all solutions, the costs to those solutions, and the necessary steps to effectuate them. Have these solutions and details written out before you have the conversation. Being able to refer to your notes is extremely helpful, especially when you find these types of conversations difficult, so you can stay on point and remember to cover everything. Written notes can also be used to put the conversation summary in an email for the client's reference.

Finally, the process of assessment and development of possible solutions should have led you to the identification of any areas internally that could be improved. For example, maybe the client failed to return its census data in a timely manner and, despite two reminders, testing never got done for that year. Was the problem caused by the client? Yes. Could you still have done something differently? Yes. If the reminders only went to the same person, the improvement could be to copy the owner of the company – at least on the second and later reminders. Or maybe instead of a fourth follow-up email, a phone call should be made instead. If your emails are going into your client's spam, sending another one isn't helpful. Mailing a hard copy letter to the owner of the company could be another alternative.

Adding these changes to your routine procedures doesn't mean that how you handled things originally was wrong, but instead is an opportunity to improve your customer service.

STEP 3: CORRECTIONS HAPPEN

If you have to make a correction that has financial implications, and you have determined that your firm should take responsibility for whatever reason, the question may arise as to the best way to handle the funding. There are

> "If the error was your fault, you need to talk to your legal counsel first before talking to the client."

options, but the cost of the correction may make the choice for you.

When the cost of the correction is low enough that you don't have to consider your E&O deductible, you may work it out so that the client puts in the corrective contribution (and gets to enjoy the tax deduction) and you agree to waive all fees for a certain period of time. If you agree to this type of settlement, just remember that, if this client has always been a difficult and demanding client, you are now stuck with them because they'll never leave a "free" situation.

Another recommendation is to put the terms of the settlement in writing and have all parties sign off on it. You want to avoid the client coming back for another bite at the apple later on.

Finally, you should take into account all of the liability limitations in your service agreement when you decide what to chip in to fix the error. You can always pay more than you said you would to reimburse the client for your mistake (it's probably necessary if you want to keep the client), but you may not have to.

If the amount of money involved is substantial and you need to let your E&O coverage kick in, your carrier will likely have its own attorney handle the transaction, including the settlement agreement. You will still have to pay your deductible, and your premiums may increase at the next renewal period, but often this may still end up being the least onerous solution for you. Remember – there's a reason why you buy insurance, and this may be it.

CONCLUSION

In the immortal words of Douglas Adams, "Don't Panic!" Mistakes happen to everyone at one time or another. If you keep a level head and allow your cerebral, not visceral, thought process kick into gear, you'll get through it just fine.

Use this as an opportunity to review and improve your processes and procedures. If handled properly, this can actually solidify your relationship with your client. People like doing business with people who have integrity, honesty and technical expertise. You can show off all of these traits during the correction process – and what you thought was going to be your downfall can be your finest hour. PC

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BY WILL HANSEN

SECURE Act Blocked by Senate Rule

What is unanimous consent?

"Woof! You sure gotta climb a lot of steps to get to this Capitol Building here in Washington. But I wonder who that sad little scrap of paper is?"
– *Schoolhouse Rock – I'm Just a Bill*

At the time I'm drafting this article during the summer of 2019, the "sad little scrap of paper" is the Setting Every Community Up for Retirement Enhancement (SECURE) Act, and it is awaiting further action in the U.S. Senate.

But before reaching the Senate, the SECURE Act made its way through the regular order of the U.S. House of Representatives. The bill was debated in the House Committee on Ways & Means, favorably reported out of that committee, and then passed by the House on a 417-3 vote.

This is the process that is described in the classic "Schoolhouse Rock" video. While the "Bill" in the "I'm Just a Bill" video says that once the House process is complete, the same process occurs in the Senate, actually there is a much simpler path to becoming a law, known as "unanimous consent."

According to the United States Senate Glossary, unanimous consent is when "a senator may request unanimous consent on the floor to set aside a specified rule of procedure so as to expedite proceedings." In other words, a senator may request that, without objection from any other senator, a bill pass out of the Senate.

Upon passage of the SECURE Act by the House, Sen. Chuck Grassley (R-IA) did just that, requesting that the SECURE Act pass the Senate via unanimous consent. With a strong bipartisan vote in the House and bipartisan support of the policies in the SECURE Act among a number of senators, there was a chance the legislation could pass via unanimous consent instead of using "regular order" (i.e., debate on the Senate floor and a vote). However, several senators objected to passage of the bill under this process.

> "In the history of the U.S. Senate, simple unanimous consent agreements have been used since the first Senate session in 1789.

Unanimous consent is a tactic that the Senate uses frequently to advance legislation – not only upon final passage of a bill, but also to shorten debate time, agree to amendments, and several other shortcuts to regular Senate rules. In the history of the U.S. Senate, simple unanimous consent agreements have been used since the first Senate session in 1789. The first complex unanimous consent agreement didn't occur until 1846. Until 1846, the typical process to conclude debate on a bill and proceed to a vote was a simple gentlemen's agreement – meaning there was no process in place to force a vote on a bill. But in 1846, with a prolonged debate on the Oregon Treaty with Great Britain, senators unanimously agreed to a fixed time period to conclude debate and vote on the treaty (which later led to Oregon becoming the 33rd state).

Today, unanimous consent is vital to the operation of the Senate. Typically, it is used to frame debate time, number of amendments, vote threshold for amendments, and timing of final passage for most pieces of legislation. Of course, this is necessary if a senator objects to a simple agreement to pass the legislation without debate – which is what happened when Sen. Grassley requested that the SECURE Act pass via unanimous consent.

By the time you read this, I hope the SECURE Act has been signed into law by President Trump (using any Senate procedural process available). In the meantime, I'll keep my fingers crossed and sing "I'm just a bill. Yes, I'm only a bill. And I'm sitting here on Capitol Hill." PC

Will Hansen is the American Retirement Association's Chief Government Affairs Officer.


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