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PLAN CONSULTANT

SPRING 2019

THE NEXT BIG DEAL

THE EVOLVING MEP AND PEP LANDSCAPE

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Plains Speaking

How can we help future retirees when so many people have little or no retirement savings?

In a commentary she penned recently for CNBC, Heidi Heitkamp, the former U.S. Senator from North Dakota, addressed the question of whether or not the nation is facing a "retirement crisis." Heitkamp wrote: "Economists who argue that there is no retirement income crisis are missing the point. The crisis is not today, it is 20 years in the future," adding that the time to act is now, before it's too late.

Heitkamp supported her argument with some sobering statistics from reputable sources. Some were familiar; others were not:

- Currently, nearly half of all American families have no retirement savings. (Economic Policy Institute)
- More than one-third of all private sector workers do not have access to a workplace retirement plan. (Pew Charitable Trust)
- Projections show that 44% of Baby Boomers and Gen Xers risk running short of funds for retirement. (EBRI)
- Families in which the head of the household is 61 years old or younger saw wage declines over the past two decades by about 30%. (Federal Reserve)
- 40% of American adults would be unable to come up with $400 for an emergency expense account, without borrowing money or selling a possession. (Federal Reserve)

Past performance is not an indicator of future results, as we know. Except that sometimes, it is. To summarize: 20 years from now, Americans will be older, and older Americans will probably be poorer.

How can we help future retirees when so many people have little or no retirement savings? Heitkamp offered two answers to that question. First, individuals and families must make saving for retirement a priority, she noted, and understand better the power of long-term investing. For example, a $650 monthly deposit into a 5% compounding account will yield $1 million after 40 years. A little over $10 a day (about the price of a meal at McDonalds these days) would yield half a million dollars.

And second, Heitkamp said, Congress must act. "This retirement crisis is not news for policy makers," she wrote. "Congress needs to invest in hard working families by helping make sure they can save for retirement now, so they will be set up for success in later years. But it also must be careful to avoid further complicating an already overly-complicated retirement savings system."

Like a lot of other folks from the plains states, the former senator displays a command of common sense, and she speaks, well, plainly. Regardless of whether or not you think there's a retirement crisis – either right now or sometime down the road – I think we can all agree that there's a serious financial literacy problem in America. And furthermore, that if they are to be successful, any efforts to address the "retirement crisis" – whether it's solving the one that you think exists today or avoiding the one that's coming – must include financial literacy as a foundational element. The same goes for other aspects of Americans' overall financial health and wellbeing, like saving for college or a home downpayment, rainy day saving, and student loan and credit card debt, to name a few.

> "I think we can all agree that there's a serious financial literacy problem in America."

As for Heitkamp's second suggestion – help from Congress that avoids "further complicating an already overly complicated retirement savings system" – there's an idea that every single member of ASPPA can get behind. Too bad it came from a *former* member of Congress.

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

JOHN ORTMAN
EDITOR-IN-CHIEF

BY JIM NOLAN

Three E's and a V, Follow-up No. 1

The latest on ARA's government affairs leadership team and plans for the 2019 Annual Conference.

As I'm sure you remember from my column in the last issue, the above stands for "education, education, education, and volunteerism." I was going to use this column to expand upon ASPPA's and ARA's advocacy efforts, but as often happens, life gets in the way of plans.

Due to the government shutdown and other sideshows, the legislative and regulatory apparatus affecting retirement plans has slowed to a near halt, but ARA and ASPPA march on uninterrupted. As an example, the ARA revamped its government affairs leadership team with two key additions in January. Will Hansen joined in the new role of Chief Government Affairs Officer and Allison Wielobob joined as ARA's General Counsel.

Hansen, an attorney with an LLM in Employee Benefits from The John Marshall Law School, joins from the ERISA Industry Committee (ERIC), where he was the Senior Vice President of Retirement and Compensation Policy, leading ERIC's efforts to develop and advocate for retirement and compensation public policy priorities at the federal, state and local levels.

Wielobob comes to the ARA from the Washington, D.C. office of international law firm Eversheds Sutherland. Prior to that, she worked for 10 years as an attorney with the U.S. Department of Labor, where she was on the staff of the Office of Regulations and Interpretations of the Employee Benefits Security Administration. During her tenure at the Labor Department, she worked on ERISA fiduciary issues and many of the Department's major initiatives, including retirement plan fee disclosure and default investment alternatives.

> "The ARA revamped its government affairs leadership team with two key additions in January."

My friend Craig Hoffman, a critical part of our advocacy efforts over the last decade, will be moving on to other things later this spring, but I'm sure we will be hearing more from him as time goes by. We wish him all the best!

In the realm of education – transferring knowledge to all of our ASPPA members – in the second week of January I attended a meeting of the Planning Committee for this year's Annual Conference. Ten volunteers and three ARA staff members (Bob Kaplan, Erin Stewart and Melissa Trout) spent a day and a half planning the subjects, sessions and speakers for the 2019 ASPPA Annual Conference. Committee members volunteered their time to brainstorm how to make this fall's meeting more enjoyable, more exciting, and more relevant than any of the meetings in the past. We all owe a debt of gratitude to these volunteers.

As I write this, I am seven days away from spending two days at the Los Angeles Advanced Pension Planning Conference. Committee meetings for this conference started early last summer. Again, dedicated volunteers and ARA staff members donated time and expertise to help make this meeting possible. I will be facilitating a couple of sessions. I'll be looking forward to gaining the knowledge I need to transfer on to my clients and their advisors.

As a result of ASPPA/ARA advocacy staff and ASPPA/ARA member educational efforts, we are all able to do our jobs more effectively, helping our clients and their advisors. My thanks to all the volunteers.

More in the summer! PC

James R. Nolan, QPA, is CEO of The Nolan Company, A Division of T Bank, NA, a TPA providing recordkeeping, administration, actuarial and plan design services in 50 states. He serves as ASPPA's 2019 President.

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BY BRIAN H. GRAFF

A Federal Case

It's time to make the case for a federal solution to the nation's coverage gap that relies on private-sector innovation.

The congressional mid-term elections are over and the Democrats took back control of the House for the first time since 2010, while the GOP slightly expanded its hold on the Senate majority. Believe it or not, while the talk outside the Beltway has largely focused on the prospects for even more gridlock, the prospects for positive retirement plan legislation might have just brightened.

Lawmakers in our nation's capital may have been focused on shutdowns, declared emergencies and "new" deals, but in state capitals across the nation, legislators and regulators have been proposing, passing and implementing change that could dramatically impact your business.

> "While the coverage gap is real, and should be addressed, it should be done so at the federal level."

While the nation's private retirement system has many accomplishments to celebrate, they belong largely to those who have access to a retirement plan at work. Despite the industry's efforts, the percentage of full-time workers with access to those plans has barely budged in a generation. Not surprisingly, states are stepping into the void.

Since 2012, 43 states have acted to implement, study or consider legislation to establish state-based retirement plans. In the past year alone, at least 16 states and cities introduced legislation. Ten states and the city of Seattle have enacted some type of retirement program for private-sector workers. Oregon has had a program in place for more than a year now; Illinois has moved past its pilot phase; and California's CalSavers program is slated to open in July.

Meanwhile, as we head to press, a bill establishing the New Jersey Secure Choice Savings Program, the structure of which mirrors the Illinois program, awaits the signature of New Jersey Gov. Phil Murphy (D). The program requires, at minimum, that employers automatically enroll their employees into a payroll deduction IRA program. Like Illinois, the New Jersey program applies to private-sector employers with 25 or more employees that do not already offer a plan.

We have become increasingly concerned about the compliance headaches caused by these mushrooming programs, particularly to employers that may operate in multiple states. As an industry, we've long benefited from the consistent set of federal standards established by ERISA. While the coverage gap is real, and should be addressed, it should be done so at the federal level.

Fortunately, the new Chairman of the House Ways & Means Committee, Rep. Richard Neal (D-MA), agrees. A prominent voice in retirement plan policy, he introduced the Automatic Retirement Plan Act of 2017 (ARPA) more than a year ago. ARPA required employers with 10 or more employees to maintain a 401(k) or 403(b) plan that covers all eligible employees, exempting governments, churches and businesses in existence for three years or less. The bill also allowed for multiple employer plans (MEPs) and increased the start-up credit for small employers.

In sum, it purported to do at a federal level what is at the heart of these state initiatives – but provided a coverage solution at a federal level, rather than the patchwork quilt that is emerging. Importantly, unlike the state-based initiatives, the ARPA legislation did not create a federally run retirement savings program, but instead relies solely on private-sector solutions. We have been closely working with Chairman Neal and his staff, and fully expect a modified version of ARPA to be introduced in this Congress.

As your advocacy voice, ASPPA and the American Retirement Association are actively engaged with state regulators and the various legislative bodies as we work together to construct effective solutions to these issues.

It's time to make a federal case for a federal solution – and your continued support and involvement is essential not only to our long-term success, but also to the success of America's retirement system! PC

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

Compensation for MEP Sponsors, Part 2

Tips on how a MEP sponsor can get paid without violating the prohibited transaction rules.

BY FRED REISH, BRUCE ASHTON & JOSH WALDBESER

In Part 1 of this article, we explained what a MEP is and the different types of MEPs. We also discussed some legal principles that apply to MEP sponsor compensation and reimbursement of expenses. Here in Part 2, we apply those principles to how a MEP sponsor can get paid without violating the prohibited transaction rules of ERISA or the federal Tax Code.

REASONABLE COMPENSATION

The determination of reasonableness is a facts-and-circumstances test, so we can't provide a bright line description on how to meet this requirement… other than to say that a MEP sponsor should assess, through benchmarking or other comparative means, whether its compensation and that of any affiliates is reasonable. However, the obligation to determine whether the MEP sponsor's compensation is reasonable rests with the participating employers. On the other hand, the MEP sponsor generally is responsible for determining whether the compensation of the MEP's other service providers is reasonable.

The initial decision to join the MEP is made by each participating employer. And the participating employers retain the responsibility to periodically monitor the sponsor's performance and compensation to determine if they continue to be reasonable and whether to continue to participate in the MEP.

Inherent in the oversight obligation of participating employers to monitor and approve changes in services or fees is the fact that the employers do not have a material financial interest in the MEP sponsor that would affect their judgment. In some MEPs – most often an Association MEP – an oversight board is appointed from among the participating employers. This board takes on the oversight role. We refer to this as a "MEP board."

CHANGING THE SPONSOR'S COMPENSATION

Since the MEP sponsor serves as a fiduciary of the MEP, it cannot set or unilaterally change its own compensation. Approving a change will require approval by the participating employers or a MEP board.

There are a couple of ways the sponsor can seek that approval. Where the responsibility is retained by the participating employers, the sponsor typically would send out a proposed amendment with the new fee structure and seek affirmative or "deemed" approval using the "Aetna Opinion" process discussed in Part 1. In plans with a MEP board, the process is

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simplified, since only the board will need to consent to the change.

PROFITING FROM THE MEP

One of the concerns of potential MEP sponsors is whether they can earn a "profit" from the MEP. For example, suppose a local builders association sponsors a MEP. Can it charge a per head fee that comes from plan assets and creates a profit? Or if a TPA is the MEP sponsor, can it make a profit paid from plan assets?

The answer to both questions is "yes," so long as the amount paid is:

- for a necessary service (i.e., "appropriate and helpful to the plan … in carrying out the purposes for which the plan is established or maintained"[1]);
- reasonable relative to the services rendered; and
- adequately disclosed under 408(b)(2).

In the builders association example, if the association takes on the fiduciary and administrative roles of a sponsor, it can build the per head charge into its fee for serving as the MEP sponsor. So long as the fee meets the requirements described in the prior paragraph, the fact that there is profit built into the fee is not an issue.

But if the association's role is limited to making the MEP available to its members, so that the fee is essentially an "access" fee, the answer is murkier. In that situation, the safer course would be for the fee to be paid by the entity engaged as sponsor of the MEP rather than be paid out of plan assets. The sponsor would need to ensure legal compliance. Having the fee paid out of MEP assets as compensation for a service rendered by the association would be even more difficult, in light of the requirement under the 408(b)(2) exemption that a service be "necessary."

The TPA example is clearer in that, when a TPA is a MEP sponsor, the TPA is performing the fiduciary and administrative roles we discussed earlier. To the extent it performs significant administrative services, its fees could be higher than if it served only in an oversight role over other service providers. Either way, it could build a profit element into its fee without violating the prohibited transaction rules so long as its compensation overall is reasonable and is approved by each participating employer.

REIMBURSEMENT OF EXPENSES

Under ERISA, while a fiduciary cannot cause itself to receive additional compensation from a plan, it is permitted to receive reimbursement for certain direct expenses. In this section, we address the following questions:

- Can a MEP sponsor be reimbursed for its expenses?
- Can it be reimbursed for marketing, salary for employees providing education, and support staff to answer questions?
- If it can be reimbursed, what expenses and what best practices should be adopted to document the reimbursement?

The sponsor of a MEP, whether it is an Association, Open or PEO MEP, can be reimbursed out of plan assets for direct out-of-pocket expenses. The DOL has addressed the reimbursement issue in several contexts. First, DOL regulations make clear that even though a fiduciary cannot set or approve its own compensation, it can receive "reimbursement of direct expenses properly and actually incurred in the performance of such services."[2]

The next question is whether an expense can be paid out of the plan or must be paid by the employer/sponsor. In Advisory Opinion 2001-01A, the DOL said that generally, reasonable expenses of administering a plan, including direct expenses properly and actually incurred in the performance of a fiduciary's duties to the plan, can be paid out of the plan. However, the establishment, design and termination, rather than the management, of a plan, is generally not a fiduciary activity, such that related costs are considered settlor

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"In some MEPs – most often an Association MEP – an oversight board is appointed from among the participating employers."

expenses that may not be paid out of plan assets.

The DOL also issued a series of examples to help identify settlor as opposed to permissible plan expenses.[3] In general, expenses of running the plan may be paid out of the plan, while the expense of setting up the plan, assessing various design alternatives and amending the plan would be considered settlor or employer expenses. The DOL recognizes an exception, indicating that the cost of amending a plan to maintain its tax qualification is a valid plan expense.[4]

On the "reimbursement" issue, the DOL has issued a number of Advisory Opinions on plan sponsors reimbursing themselves for out-of-pocket expenses from the assets of the plan they sponsor. In Advisory Opinion 1993-06A, the "Allied Signal" Opinion, the DOL said that a sponsor may be reimbursed for direct expenses, but not for general overhead such as rent, utilities, employee or other expenses that would have been incurred regardless of whether the plan existed.

Though the Opinion addressed reimbursement to a single employer and not a MEP, by analogy, the concepts should apply to MEPs. It may be possible under this Opinion to seek reimbursement for the salaries of employees who provide education or of support staff who answer questions, but the DOL generally is skeptical of this practice. In the MEP context, where the only function of the sponsor's employees is to serve the needs of the MEP, this skepticism may be surmountable, but we think the safer approach is to charge a specified fee for the participant education service and pay the employee costs out of that fee.

Another common question is whether a MEP sponsor can be reimbursed for travel, document production and similar costs incurred in "marketing" the MEP and the benefits of participation to new employer-members. This is a difficult question. On one hand, encouraging further MEP participation could help enhance economies of scale, which potentially could benefit participants or participating employers by reducing plan costs. On the other hand, this activity is arguably not a "service" to the MEP and its existing participants and could be seen as a settlor function, such that the costs could not be paid out of the MEP. The safer course would be for the sponsor to bear these costs out of its revenues and include them in its calculation of its fee.

CONCLUSION

MEP sponsors cannot approve or modify their own compensation, but must instead look to the participating employers or a MEP board established by those employers. That said, the compensation can include a profit element so long as the compensation is for a necessary service, is reasonable and is adequately disclosed. MEP sponsors may also be reimbursed out of plan assets for proper plan expenses – generally those related to the management and administration of the MEP rather than the design or establishment of the MEP. PC

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FOOTNOTES

[1] ERISA Reg. §2550.408b-2(b).

[2] 29 CFR §2550.408b-2(e)(3).

[3] See "Guidance on Settlor v. Plan Expenses" at https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/advisory-opinions/guidance-on-settlor-v-plan-expenses.

[4] Advisory Opinion 2001-01A.

And They're Off!

YULIA SHE / SHUTTERSTOCK.COM

MEPs were the focus of two of the first retirement reform bills out of the gate in the 116th Congress.

BY ANDREW REMO & TED GODBOUT

As expected, the new Congress is gearing up to address retirement security and coverage, as the first full month of the 116th Congress saw the reintroduction of last year's Retirement Enhancement and Savings Act (RESA) in the House of Representatives and the introduction of the Retirement Security Act of 2019 in the Senate. Both bills would give a boost to open multiple employer plans (MEPs).

RESA RESURRECTED IN THE HOUSE

A new House version of last year's RESA legislation was introduced in February. The new bill is bipartisan – sponsored by Reps. Ron Kind (D-WI) and Mike Kelly (R-PA) – as was the one introduced nearly a year ago by the same duo.

The bill, which is the same as last year's legislation except for changes in effective dates and other technical changes, includes provisions intended to improve the retirement plan to improve the retirement plan options available to small businesses by allowing unrelated employers to adopt a MEP.

In addition, the bill would:

- give employers additional time to adopt a qualified retirement plan for the prior year up until the due date of the tax return (with extensions);
- provide for greater flexibility for a business to adopt a safe harbor 401(k) plan;
- reduce the premiums charged to cooperative and small employer charity (CSEC) pension plans like the ones sponsored by some rural electric and agricultural cooperatives and the Girl Scouts;
- enhance automated saving by removing the 10% cap on automatic employee contribution rate increases; and
- provide a tax credit of up to $5,000 to defray the cost of starting a retirement plan and create a new tax credit for plan designs with an automatic enrollment feature.

> As the Chairman of the Senate Aging Committee, ensuring that more people are better prepared for retirement is one of my top priorities."
>
> — Sen. Susan Collins, R-ME

Enactment of RESA was touted as a vital step in expanding access and addressing the coverage gap at a Feb. 6 Way & Means Committee hearing – the first House committee hearing on retirement security in the 116th Congress.

At the hearing, Way & Means Committee Chairman Richie Neal (D-MA) pointed to RESA's provisions strengthening open MEPs as a good starting point for discussion, as well as his Automatic Retirement Plan Act (ARPA) to require all but the smallest employers to maintain a 401(k) plan for their employees.

To bolster his argument, Neal cited statistics showing that for workers earning between $30,000 and $50,000 per year, more than 70% will participate if offered a retirement plan at work, but only 5% would save on their own through an IRA. "These facts underscore that the retirement crisis in America is real and will only worsen unless we strengthen Social Security, make saving easier, and do more to encourage employers to offer retirement plans," Neal said.

MEPS GET BOOST IN SENATE BILL

On the other side of the Capitol building, open MEPs were the focus of bipartisan legislation introduced in the Senate. The Retirement Security Act of 2019 was introduced Feb. 4 by Sens. Susan Collins (R-ME), the Chairman of the Senate Special Committee on Aging, and Maggie Hassan (D-NH). The legislation's stated goal: to help small businesses offer retirement plans to their employees and encourage individuals to save more for retirement.

"As the Chairman of the Senate Aging Committee, ensuring that more people are better prepared for retirement is one of my top priorities," said Collins. "Our bipartisan legislation would significantly improve the financial security of many Americans by reducing the cost and complexity of retirement plans, especially for small businesses, and encourage individuals to save more for retirement."

"By giving more small businesses the support that they need to provide retirement plans to their employees and encouraging people in the workforce to save more for retirement, this bipartisan bill is an important step toward providing a secure retirement for more of our workers," commented Hassan.

The Retirement Security Act of 2019 would:

- enable more businesses to join MEPs to offer retirement programs to their employees by not requiring a nexus between otherwise unrelated businesses;
- make MEPs a more attractive option for small businesses by eliminating the one-bad-apple rule;
- reduce the cost of maintaining a retirement plan by directing the Treasury Department to simplify, clarify and consolidate required notices to lessen costs; and
- simplify compliance for small businesses that choose to provide employees with employer matches on contributions up to 10% of pay, encouraging more generous retirement contributions by businesses.

Suggesting that the nation is on the "verge of a national crisis," Collins appears intent on addressing retirement security through bipartisan solutions. In fact, Collins' Aging Committee also held a hearing on Feb. 6 to review "innovations and best practices to promote savings," at which she singled out the importance of employer-sponsored plans in ensuring retirement security.

Still to come: a RESA companion bill in the Senate. The original Senate version of RESA was last introduced in March 2018 by Sens. Orrin Hatch (R-UT) and Ron Wyden (D-OR), the leaders of the Senate Finance Committee. (Wyden remains the ranking member, while Hatch retired at the end of the last Congress.) That bill previously received unanimous bipartisan support in that committee during the 114th Congress in 2016, but it was never taken up by the full Senate. It's possible that Sen. Chuck Grassley (R-IA), the new Chairman of the Finance Committee in the 116th Congress, will team up with Wyden to reintroduce a Senate version of RESA. What's more, Grassley – who previously chaired the Finance Committee in the early-to-mid 2000s, when the Pension Protection Act of 2006 was signed into law – has also indicated that he plans to advance legislation to "protect and enhance Americans' retirement security," so it's possible that he'll bring new ideas of his own to the table. PC

Andrew Remo is the Director of Legislative Affairs at the American Retirement Association (ARA). Ted Godbout writes about DC plans for the ARA.

SERGEY NIVENS / SHUTTERSTOCK.COM

State-Sponsored Retirement Programs Gather Steam

From coast to coast, state governments are implementing their own plans to help employees of private-sector companies.

BY JOHN IEKEL

There is no federal program that provides benefits to retired Americans aside from Social Security. And the recent short-lived federal retirement account plan, MyRA, never really got off the ground.

But that has no bearing on the states' ability to set up programs, nor their willingness, as more states adopt and implement such plans. And adopt they are, gradually, from sea to shining sea.

On the West Coast, Mt. Hood and majestic evergreens that give way to steppe are the setting for the first such program. OregonSaves, the state-run auto-IRA program for private-sector workers in Oregon whose employers do not provide a retirement plan, was launched on July 1, 2017 and began accepting employer participants three months later; the deadline for employers to register was July 1, 2018. Last October, the rules for OregonSaves were expanded so the program also covers multiple employer plans, multiemployer plans, the self-employed and gig economy workers.

OregonSaves has been implemented in stages, based on employer size; the most recent made the program applicable to private-sector employers with 20-49 employees. The program continues to gain new participants and to grow in the balances set aside through the program. The Oregon Treasury says that at the end of 2018, membership and savings stood as follows:

	July 1, 2018	Nov. 1, 2018	Dec. 31, 2018
Employers registered	990	1,331	2,649
Savings	$4,560,000	$8,800,000	$10,900,000

Also as of Dec. 31, 52,287 employees were participating, 72% of those eligible to do so. They save approximately $100 per month, and the average savings rate is 5.2%.

OregonSaves includes automatic features; among them are automatic contributions, which have begun. And the contribution rates for participants automatically increased by 1% on Jan. 1, 2019 for participants who:

- have been contributing for six months or more;
- are contributing less than 10%; and
- have not opted out of automatic contribution increases.

Oregon's neighbors have jumped on the bandwagon.

On March 19, 2018, Washington State's Retirement Marketplace was launched. Financial services firms offer low-cost retirement savings plans to businesses with fewer than 100 employees, including sole proprietors and the self-employed, through this virtual marketplace.

Participation is voluntary for both employers and employees. The marketplace also is open to self-employed, part-time and temporary "gig" workers. At launch, the site offered five types of 401(k) plans, as well as Roth and traditional IRAs.

Completing the Pacific coast trifecta, on Nov. 19, 2018, California launched CalSavers, a state-run retirement plan for private-sector employees whose employers do not offer a retirement plan. It does not apply to employers that already offer an employer-sponsored retirement plan.

Voluntary registrations for CalSavers start July 1, 2019; registration by employers with five or more employees that do not offer a retirement plan will become mandatory over the three following years for employers of varying sizes. Offering access will be mandatory at full implementation by Jan. 1, 2022.

CalSavers' program management agreement is complete, as is the operational agreement with Ascensus and State Street Global Advisors (SSgA). CalSavers' client service team went live on Oct. 22, 2018, to support the launch of the public website.

In the heartland, legislation creating the Illinois Secure Choice Savings Program Act was enacted on Jan. 4, 2015. The program, through which employees whose employers do not offer a retirement plan will have 5% of their gross pay automatically deducted and placed in an IRA, was to be implemented in 2017. But a subsequent measure delayed enrollment until 2018 and set Dec. 31, 2020 as the deadline for full implementation.

Employers with 500 or more employees began to register last November; those with 100-499 employees will do so beginning in July of this year, and employers with 25-99 employees in November.

But the program's future may be cloudy. In August 2018, then-Gov. Bruce Rauner (R) vetoed a bill that made technical changes to the program and in the process made participation by employers that do not offer a retirement plan voluntary, not mandatory; he also cited uncertainty regarding ERISA applicability. State Treasurer Michael Frerichs disputed Rauner's arguments and implementation continues.

> "On the eastern seaboard, the map is studded with states that either have plans pending or in the works."

On the eastern seaboard, the map is studded with states that either have plans pending or in the works.

Vermont, which declared its own independence from England and has been happy to shake the tree ever since, is among the early states establishing plans. In 2017 legislation was enacted that called for the creation of the Green Mountain Secure Retirement Plan by Jan. 15, 2019.

Applicable to self-employed individuals and employers with 50 employees or fewer that do not offer a retirement plan, the plan allows but does not require employers to automatically enroll all employees in a multiple employer plan (MEP). It also allows employees to withdraw. Initially the program calls only for employee contributions, but provides an option for future voluntary employer contributions.

Neighboring Massachusetts also has a MEP. In October 2017, State Treasurer and Receiver Deborah Goldberg said the commonwealth is collaborating with the Massachusetts Nonprofit Network to sponsor the Massachusetts Defined Contribution CORE Plan, a tax-deferred and post-tax 401(k) savings plan intended to help Massachusetts nonprofit employees save and invest for retirement. The state Senate is now considering legislation that would expand the plan to all – including private-sector – employers in Massachusetts.

Farther south, Maryland has a plan pending. In 2016, Gov. Larry Hogan (R) signed into law a measure establishing the Maryland Small Business Retirement Savings Program, which is expected to begin functioning this year. It requires employers that do not offer a plan to offer their employees automatic enrollment in a personal payroll-deduction IRA.

On the other side of the Potomac, the Virginia House of Delegates is considering legislation that would create a state-based plan. One bill would create a state-based program that would require all private-sector employers, as well as sole proprietors and the self-employed, to offer the program if they do not already have a plan. The other also would create a state-based program similar to OregonSaves, as well as a plan similar to Washington's Retirement Marketplace.

The Garden State legislature also has passed legislation which would establish the New Jersey Secure Choice Savings Program; the measure went to the desk of Gov. Phil Murphy (D) for his signature on Feb. 25. PC

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Time for a QDIA Refresh?

For a plan with a high number of participants without proper diversification, auto re-enrollment in the plan's QDIA can be a smart choice.

BY MICHAEL KAZANJIAN

Today, nearly everything is automatic – or at least appears to be. Tasks that once required some level of manual effort, now just happen. And, for the most part, we like it. Automation ensures we never miss a payment, keeps the pantry stocked or, for the over-committed and slightly overwhelmed new parent, the house will never be without diapers.

Not only have automated services improved our lives on a daily basis, they're also helping many savers prepare for the future. Automatic enrollment into company retirement plans is on the rise at a time when it's more important than ever that people find a way to self-fund their retirement.

A 2017 survey from Willis Towers Watson found that the use of automated plan features by sponsors has risen steadily over the past 10 years.[1] Seventy-three percent of plan sponsors now automatically enroll new participants, up from 52% in 2009 and 68% in 2014. Auto escalation is also on the rise – pun intended – with 60% now offering the feature compared to 54% in 2014.

As a result of these features being added, retirement saving is increasing each and every year. As of 2016, nearly 95 million people had more than $5.3 trillion invested.[2] And plans featuring auto enrollment have an average participation rate of 87%. That nearly doubles the participation rate (45.4%) of plans not offering this feature.[3]

So if we can all agree that automatic features – from Amazon.com to retirement plan enrollment – are good, why are there so many questions about QDIA re-enrollment strategies?

When compared to automatic enrollment, QDIA re-enrollment is utilized far less frequently. In a survey conducted by the Defined Contribution Institutional Investment Association, fewer than 20% of plan sponsors have completed a refresh.[4]

As Matthew Eickman pointed out in his excellent white paper, "Investment Refresh," plan sponsors and participants often overlook the potential benefits of re-enrollment based on name alone – meaning that the term is misleading and overcomplicates the strategy out of the gate. The name implies that an action is required by the participant or they'll no longer be enrolled in the plan — which is untrue on every level. Instead, Eickman posits that the term "investment refresh" is far more accurate and could quell the fears of participants, and, therefore, make plan sponsors more comfortable with the approach. In concept, 80% of large plan sponsors agree with the potential benefits as a way to reverse participant inertia and increase engagement.

But the list of reasons not to initiate the process is long and has, for the most part, stopped many sponsors from moving forward. Administrative burdens and communication challenges near the top of the list alongside participant pushback. And while there's little disagreement that asset allocation is important, plan sponsors often prioritize increasing participation and savings rates as a way to improve plan performance.[4]

To be fair, QDIAs are still a relatively new idea. ERISA Section 404(c) – along with corresponding DOL regulations – defines the ways in which a plan sponsor is protected from fiduciary liability for investment decisions made by the employee. Effective at the end of 2007, sponsors were given the ability to designate a default fund that qualified as the QDIA. If the rules are followed, the plan sponsor will not be held liable for any potential investment losses in the QDIA.

It's not so much the timing of when the rule was released, but what occurred a few months later that stops us from thinking a QDIA refresh is always a good idea. Just nine months after plan sponsors were given the ability to initiate a QDIA, Lehman Brothers collapsed and, with it, the rest of the market. While it's not possible to know everyone's intent when choosing their investments, it would be difficult to explain to a conservative participant who's nearing retirement why his or her conservative allocation was altered just prior to a significant market event. We clearly don't believe that the plan sponsor has anything but good intentions when making plan-level decisions; however, we believe it's a decision that should be made only after rigorous review of the plan and participant-level education has occurred.

There's no set timetable as to when a plan sponsor should consider a QDIA. The sponsor, with their advisor, should benchmark their plan and investment lineup annually. If history has taught us anything, it's that change happens fast and often when we least expect it. Today, there are a number of tools available to help advisors and plan sponsors evaluate their plans at all levels. If there's agreement that the time is right, participants must be given at least 30 days' notice before eligibility or before any QDIA investment is made on their behalf.

> "The sooner participants know that plan sponsors have tactics to help them achieve greater outcomes, the better."

At PCS, we believe education begins with enrollment. Participants should learn the basics of what options are available and about the possibility of things like a QDIA. Trying to explain this concept after the decision has already been made can create an uncomfortable situation. The sooner participants know that plan sponsors have tactics to help them achieve greater outcomes, the better. It's equally important that they know they have a choice in the matter.

If there's one specific event that we encourage a plan sponsor to consider refreshing their lineup, it's if a new advisor is brought in to oversee the plan or a plan conversion. It's a great opportunity to take advantage of the expertise that the new advisor was hired for, and to also – if it's the right situation – experience the potential benefits that the new firm brings to the table.

As noted above, education is the key. If you find that your plan has an unusually high number of participants without proper diversification, start by educating them on how important this is for long-term success. From your advisor to your plan provider, there's no shortage of resources for you or your participants to rely on when making these significant decisions. PC

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FOOTNOTES

[1] https://globenewswire.com/news-release/2018/02/26/1387421/0/en/U-S-employers-enhancing-defined-contribution-retirement-plans-to-help-improve-workers-financial-security.html
[2] Business Insider: https://www.businessinsider.com/americans-maxing-out-401k-retirement-savings-2017-10
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[4] DCIIA Fourth Biennial Plan Sponsor Survey, "Auto Features Continue to Grow in Popularity."

G_B_R_JO / SHUTTERSTOCK.COM

Winners, Losers and Consolation Prizes

Cash balance plans can now use a pre-approved document. Let the games begin!

BY JENNIFER WICZYNSKI

It's everyone's favorite season: restatement season! After a few extensions and the enjoyment of an IRS mass submitter review process, the defined benefit plan PPA restatement documents have been approved and most document providers have their versions available for their customers' use.

While all restatements are exciting (like a root canal), there was much anticipation for this DB restatement because it is the first time that cash balance DB plans are allowed to be on a pre-approved document. This is especially key in light of the recent limitations imposed on determination letter filings with the IRS. This article provides:

- a review of the current pre-approved versus individually designed document situation, discussing the pros and cons of each in our current reality; and
- an overview of the winners and losers of provisions on the cash balance pre-approved documents.

It assumes a general knowledge of plan document restatements and the different types of plan documents available. So hang on to your hats and let's dive in!

PRE-APPROVED VERSUS INDIVIDUALLY DESIGNED

While pre-approved documents had held the vast majority of the market share of the retirement plan document industry prior to 2016, there was still a viable and thriving individually designed plan document market for those plans that for a variety of reasons didn't want to or could not be on a pre-approved plan document. Pre-approved plan documents are documents that a mass submitter – now referred to by the IRS as a "provider" – submits to the IRS for their review and approval of the contractual content of the document. The IRS then approves the language of the document and provides proof of that approval in the form of opinion and advisory letters. The pre-approved plan documents can then be sold by providers to be used on a mass scale by the plan sponsor clients of retirement plan administration firms.

Conversely, individually designed documents (IDPs) are attorney-drafted contracts specific only to the employer that commissioned them. The way that IDPs obtained approval before 2015 was by submitting for a determination letter either upon initial qualification, when the opportunity arose on their 5-year cycle, based on the last digit of their EIN, or upon plan termination. This system worked well for a number of years, especially for cash balance plans, the market for which continued to expand.

RELATIVE ADVANTAGES

Pre-approved plan documents are attractive for a number of reasons. First, from an administrative standpoint, they streamline administration because the firm is intimately familiar with their document provisions and what they do or do not allow. It also helps the firm educate their plan sponsor clients on how their plans should be operated.

Second, pre-approved plans are typically cheaper than IDPs because they are only drafted once and they are essentially mass-manufactured, decreasing production costs.

Additionally, they come already approved, with their handy-dandy approval letter included in the document package. However, pre-approved documents lack the flexibility of IDPs and are limited in how much they can be customized before the IRS would consider them to be an IDP. Pre-approved documents are also required to contain all of the List of Required Modification (LRMs) language, meaning that they tend to be longer documents. An IDP has more flexibility to tailor the language in the document, limiting it to that which is necessary to apply to the plan.

And finally, there are many practitioners who like the look and feel of an IDP better than the two-document set of pre-approved documents, which typically contain an adoption agreement and a basic plan document.

ADVANTAGES OF APPROVAL LETTERS

An important item to note that always comes up during restatement season is whether or not it is a qualification requirement to have an IRS approval letter on the plan document.

There is no requirement under Code Section 401(a) that requires qualified retirement plans to have an IRS approval letter on their plan document language. However, there are distinct advantages for plans with IRS approval letters. First, while having an IRS approval letter is not a qualification requirement, the approval letter does provide protection to the plan sponsor that their plan document at minimum meets the IRC qualification requirements in form.

Second, if a plan sponsor ever wants to utilize the self-correction methods of the Employee Plans Compliance Resolution System (EPCRS), its plan needs to have an IRS approval letter.

Third, any plan with a large plan audit is going to have its auditor requesting a copy of the letter. Without that letter, the auditor may note a disclaimer in its opinion. For plan sponsors whose plan is written on a pre-approved document, as long as they keep up with the 6-year restatement cycles, this will never be an issue; they will get a new opinion or advisory letter with each restatement. But for plan sponsors on IDPs – of which cash balance plans comprise a fair portion – this got a lot more complicated in 2016.

With Revenue Procedure (Rev. Proc.) 2016-37, the IRS eliminated the IDP 5-year restatement cycles and crippled the ability of IDPs to get their IRS approval letters, i.e., the determination letter. Now, an IDP can only get a determination letter upon initial qualification, when it is terminating, or if the IRS makes an exception (which they have yet to do).

So, while a plan sponsor does have the ability to get a determination letter upon the birth and death of a plan, it has no ability to do a "health check" on the language of the plan document during the life of the plan to make sure the IRS would consider it healthy.

This dramatic change in the IDP world was, and still is, concerning to many plan document practitioners. But in my opinion, this is especially concerning to those working with cash balance plans. Every year plan administration firms are adding more and more of these plans, and now there is no way to get that IRS approval protection after the initial qualification.

This would have been a point of greater concern had the IRS not announced in Rev. Proc. 2015-36 that the pre-approved plan document

Winners	Losers
• Traditional DB to CB Plan conversion amendments	• Only conversion amendments based on the A+B conversion formula
• Statutory hybrid formulas that meet the requirements of cash balance formulas	• Statutory hybrid formulas that do not meet the requirements of cash balance plan formulas
• 133-1/3 accrual rule	• 3% or fractional accrual rule users
• Long list of safe harbor interest crediting rates: Treas. Reg. §1.411(b)(5)–1(d)(4)	• Interest crediting rates that are based on participant selection **OR** • Any interest crediting rate that does not meet the requirements of Treas. Reg. §1.411(b)(5)–1(d) (Rev. Proc. 2017-41, Section 6.03(7)(b))
• Interest crediting rates equal to (but not merely based on) the actual rate of return on aggregate plan assets, even if it includes returns on RICs[1]	• Interest crediting rates based on the actual rate of return on aggregate assets of the plan described in Treas. Reg. 1.411(b)(5)-1(d)(5)(ii)(A) **OR** • based on or equal to the actual rate of return on a subset of plan assets (as described in Treas. Reg. § 1.411(b)(5)-1(d)(5)(ii)(B))[2]
• Ability to establish beginning balances in the hypothetical account to build up the plan Funding Target and higher IRC 404(o) maximum in first year	• The rate of return on certain regulated investment companies (RICs) described in Treas. Reg. § 1.411(b)(5)-1(d)(5)(iv) (unless the plan provides that the rate used to determine interest credits is equal to the actual rate of return on the aggregate assets of the plan)[3]
• Ability to define a pay credit period that is shorter than a year, thereby allowing proration of pay credits during a single year	• IRC 401(a)(4) or IRC 410(b) average benefit test failsafe provisions
	• IRC 412(e)(3) funded cash balance plans
	• Floor-offset cash balance plans
	• IRC 401(h) medical account provisions

FOOTNOTES

[1] Revenue Procedure 2018-21.

[2] Id.

[3] Id.

program now would allow cash balance plans. This lessened the concern for many practitioners who should now be able to move a substantial percentage of their cash balance plans to pre-approved plan documents.

So now that we have these pre-approved cash balance plan documents, everything is sunshine and roses, right? Well, not entirely. The DB PPA plan documents for cash balance plans will allow for many cash balance plans to move over to pre-approved plan documents. But there will still be many that will not meet the criteria to be on a pre-approved plan document unless they change the operation of their plans drastically.

In addition, there are the basic plan designs that are just categorically not allowed on a pre-approved plan document, such as multiemployer DB plans, union DB plans and DB plans with Code Section 414(k) benefits. The table on page 22 provides a look at the winners and losers of the cash balance provisions.

MAKING THE MOVE TO PRE-APPROVED

I am sure that opinions vary, but overall many cash balance plans should have the option to consider moving to a pre-approved cash balance plan document during this PPA restatement. A number of these provisions which are excluded from pre-approved cash balance documents, such as Section 401(h) medical accounts and Section 412(e)(3), are relatively unique plan provisions that likely will not exclude a large number of cash balance plans from the pre-approved document world. It is also important to remember that every plan document provider is different and may make internal policy decisions that limit other provision opportunities on their cash balance plans, so make sure to closely review a provider's cash balance documents to make sure that they are right for your clients.

As this restatement period progresses, make sure to have those important discussions with your plan sponsors so they understand the pros and cons of pre-approved plans and the ramifications of being on those documents. While the "one-size fits all" approach never works for everyone, it certainly can work for many – and result in easier plan document administration for both your plan sponsors and for your business. PC

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3(16) or 402 – Who's the King?


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ERISA says that when a qualified plan is established, at least one individual or entity must be the "named fiduciary" – for ERISA purposes, the "king."

BY R.L. "DICK" BILLINGS

Old English law says that "A man's home is his castle." In most castles we find a king. The king enjoys many privileges… *but* he also has a great many responsibilities. History books tell us that the king had complete control of the vassals who populated his kingdom. However, the king also had the responsibility to protect those vassals when outside forces threatened their livelihood or way of life.

When an employer sets up an ERISA-covered retirement plan for their employees, who is the "king" of the plan?

ERISA says that when a qualified plan is established, at least one individual or entity must be the "named fiduciary" – for ERISA purposes, the "king." ERISA grants the "king" a great many privileges, such as the privilege to name the plan's terms, change plan provisions and terminate the plan whenever desired.

In return for all those privileges, ERISA imposes great responsibilities, primarily because that named fiduciary is handling other peoples' money. If you have ever served as a legal guardian or held Power of Attorney for a close friend or relative, you have felt these great responsibilities. If you have never served as the fiduciary for a loved one, you probably have not experienced those sleepless nights debating your next course of action. For those who have experienced this personal responsibility, you know it is ongoing. It is not a one-time decision.

I made up this corollary to try to put the position of a named fiduciary into perspective. Setting up a retirement plan does not come without great risk. An employer cannot set up a plan, appoint the "king," hire some outside vendors, put it on autopilot and walk away. But that is exactly what so many plan sponsors who are also the named fiduciary do on a routine basis.

As with most legislation, the responsibilities of a named fiduciary have evolved. ERISA was signed by President Ford in 1974. Has anything "evolved" since then? Well, for starters:

- Section 401(k) was added to the Internal Revenue Code;
- Al Gore invented the internet;
- the securities industry was deregulated;
- virtually all plans now impose participant investment direction;
- new participant disclosure regulations have required many more notices to be prepared and issued; and
- many thousands of "new" investment vehicles (e.g., ETFs, index funds, target date funds, etc.) have been created and are being marketed.

How prepared and educated are today's named fiduciaries when it comes to these and many other related issues?

Based upon the ERISA definitions (see "Dueling Definitions" at right), I believe the §402 named fiduciary is the "king." *Could* the §3(16) administrator have the same responsibilities as the §402 named fiduciary? Yes. But I have yet to see a §3(16) provider in today's marketplace that accepts all the responsibilities accepted by an outside §402 professional.

Now refer to the §402 definition again – note the phrase "*control and manage*." While an outside professional §3(16) administrator brings a very valuable service to the marketplace, the providers that I see typically offer limited services and do not "control and manage" the *plan*. Rather, their control and management is limited to those duties specifically delineated within their service agreement. Some accept many responsibilities; others accept very few.

From the standpoint of the §402 named fiduciary being the "king," the fiduciary hierarchy is depicted in the illustration on p. 24,, "Fiduciary Hierarchy."

If the Form 5500 is filed incorrectly, or not at all; if the plan document is not signed or dated properly; if participant notices are not issued timely, or not at all; if your investments do not conform to ERISA's "highest standards;" then the named fiduciary is the *ultimate* responsible party. Can the named fiduciary point to the failures of the TPA, the recordkeeper or the investment advisor for these issues? Absolutely – but that is, at best, a state malpractice claim. If a participant, a plaintiff's attorney, or the federal government seeks someone to blame for the plan's failures, they will look to the named fiduciary.

Virtually all plan-related documents I see say one way or another that the named fiduciary has all the privileges… and all the responsibilities. Just take a moment to look through a plan document, whether created by Relius, ftwilliam.com, Datair or any other document vendor. If a separate party has not been named and accepted, the plan sponsor is the responsible and liable party for the position of named fiduciary – both corporately and personally. Note that while most plan documents will not quote §3(16) or §402, every plan document will say, in effect, *someone* is the "king"! And that someone is almost always the employer.

This raises the question, must the employer *always* have all the fiduciary risk? Of course not. Those of us who have been in the business over these past years have seen a plethora of "fiduciaries" who willingly come forward and take on at least some level of fiduciary risk. Here are the most common ones:

- §3(21) investment co-fiduciary
- §3(38) investment manager fiduciary
- §3(16) administrative fiduciary

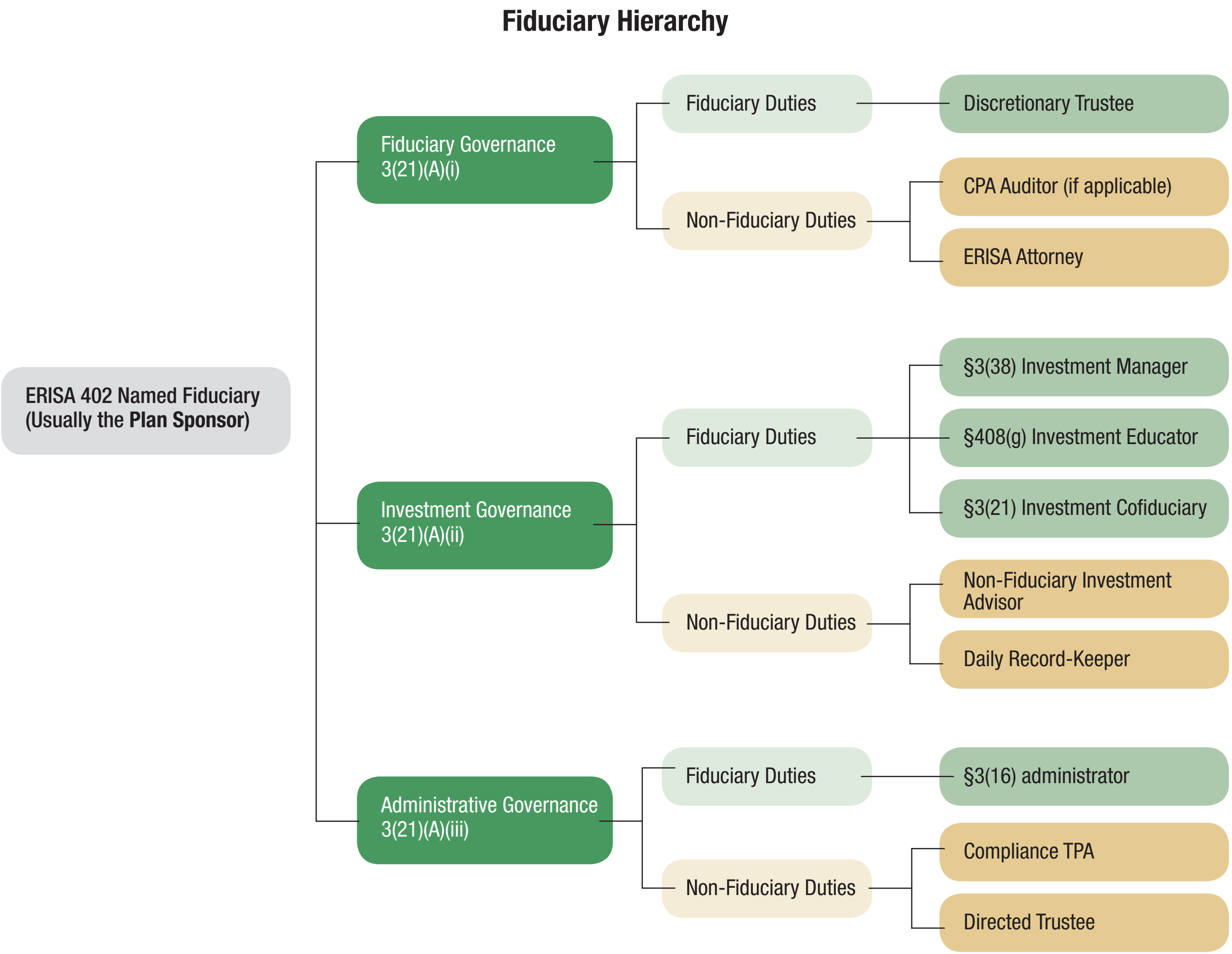
I can remember more than one instance when a new client told me his CPA was his TPA. And when I spoke to the CPA, he or she said they only completed the IRS Form 5500. Was the CPA performing TPA-like services?

Dueling Definitions

As defined in ERISA:

"**3(16)(A)** – Administrator means (i) The person so designated by the terms of the instrument under which the plan is operated; (ii) if an administrator is not so designated, the plan sponsor; (iii) In the case of a plan for which an administrator is not designated and the plan sponsor cannot be identified, such other persons as the Secretary may by regulation prescribe."

"**402(1102)(a)(1)** – Every employee benefit plan shall be established and maintained pursuant to a written instrument. Such instrument shall provide for one or more named fiduciaries who jointly or severally shall have authority to control and manage (emphasis added) the operation and administration of the plan."



Sure. Was the CPA really the TPA? I would say no.

If a firm says to an employer/ plan sponsor that they will take on a fiduciary role, that's great! But just like my CPA/TPA friend, one must look to the written documents in question to see just how much fiduciary risk (if any) is being taken on from the employer/plan sponsor.

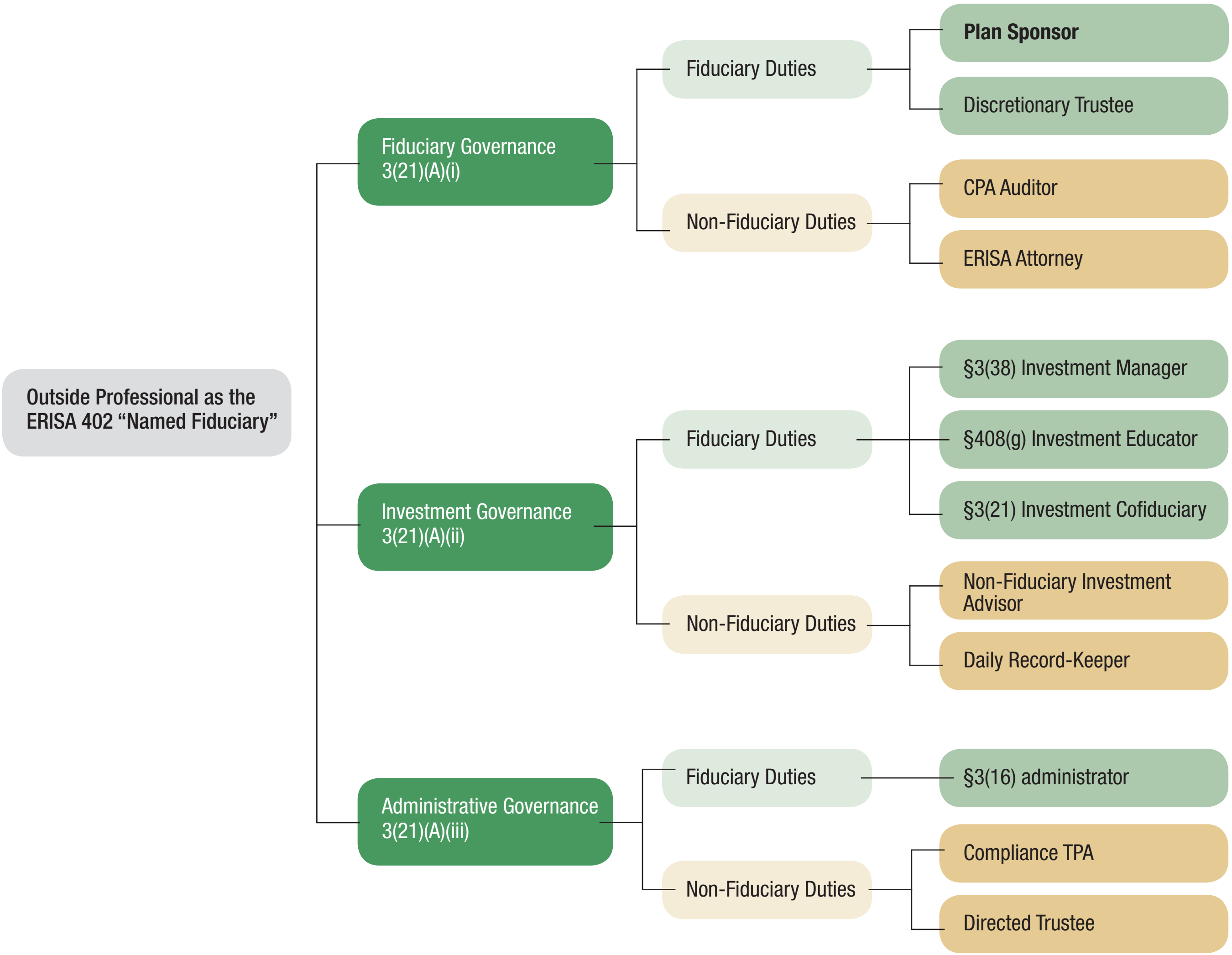
Because of this – and many other reasons beyond the scope of this article – the concept of taking on *almost* all fiduciary responsibilities from an employer/plan sponsor has become a popular one. This makes sense. Think of any successful business owner you know. They love making widgets, but most have little interest in learning how to properly oversee their qualified retirement plan.

Business owners outsource their payroll, their HR processes, their product risk via insurance. Shouldn't a business owner at least consider outsourcing their plan's fiduciary risk? And even if the business owner doesn't really understand his or her fiduciary risk, would they not want to at least "do the right thing" for their employees? An outside named 402 fiduciary gives that business owner comfort in knowing that the tough questions are being asked, detailed answers are being received, and these questions and answers are being memorialized for everyone — especially the employer — to see.

The responsibilities of an outside named 402 fiduciary are depicted in the illustration on p. 25, "Responsibilities of an Outside 402 Named Fiduciary."

Note where the employer/plan sponsor's position has been moved. (Hint: upper right corner.) Compare that position with the "Fiduciary Hierarchy" illustration above. If you were an employer/plan sponsor, where would you rather find yourself – on the left or the right? The plan sponsor

Responsibilities of an Outside 402 Named Fiduciary



is still a "fiduciary," but no longer the *named* fiduciary. The plan sponsor will still need to listen to the results presented by the outside 402. And the plan sponsor, with advice from the outside 402, will probably want to reserve the right to hire and fire all the vendors in question, *including* the 402.

Note the other important fiduciary services listed in both illustrations. They bring great value to a retirement plan and its underlying participants. But unless one legally delegates his or her named fiduciary responsibilities to someone else, that employer/plan sponsor remains responsible under ERISA to review and interpret all documents and reports created by all other fiduciary and non-fiduciary parties. Remember the widget maker? Do they really want to do this?

If you are an employer/plan sponsor, or if you work with them, these four questions need to be answered:

- Do I want to be the named fiduciary and plan administrator?
- Do I have time?
- Do I have the expertise?
- Do I want the liability, both corporate and personal?

If the answer to any of those questions is "no," ERISA basically requires the employer/plan sponsor to investigate other options. Fortunately, viable outsourcing options exist. And as a fiduciary, shouldn't the employer/plan sponsor at least investigate alternatives for themselves – and their 'vassals'? PC

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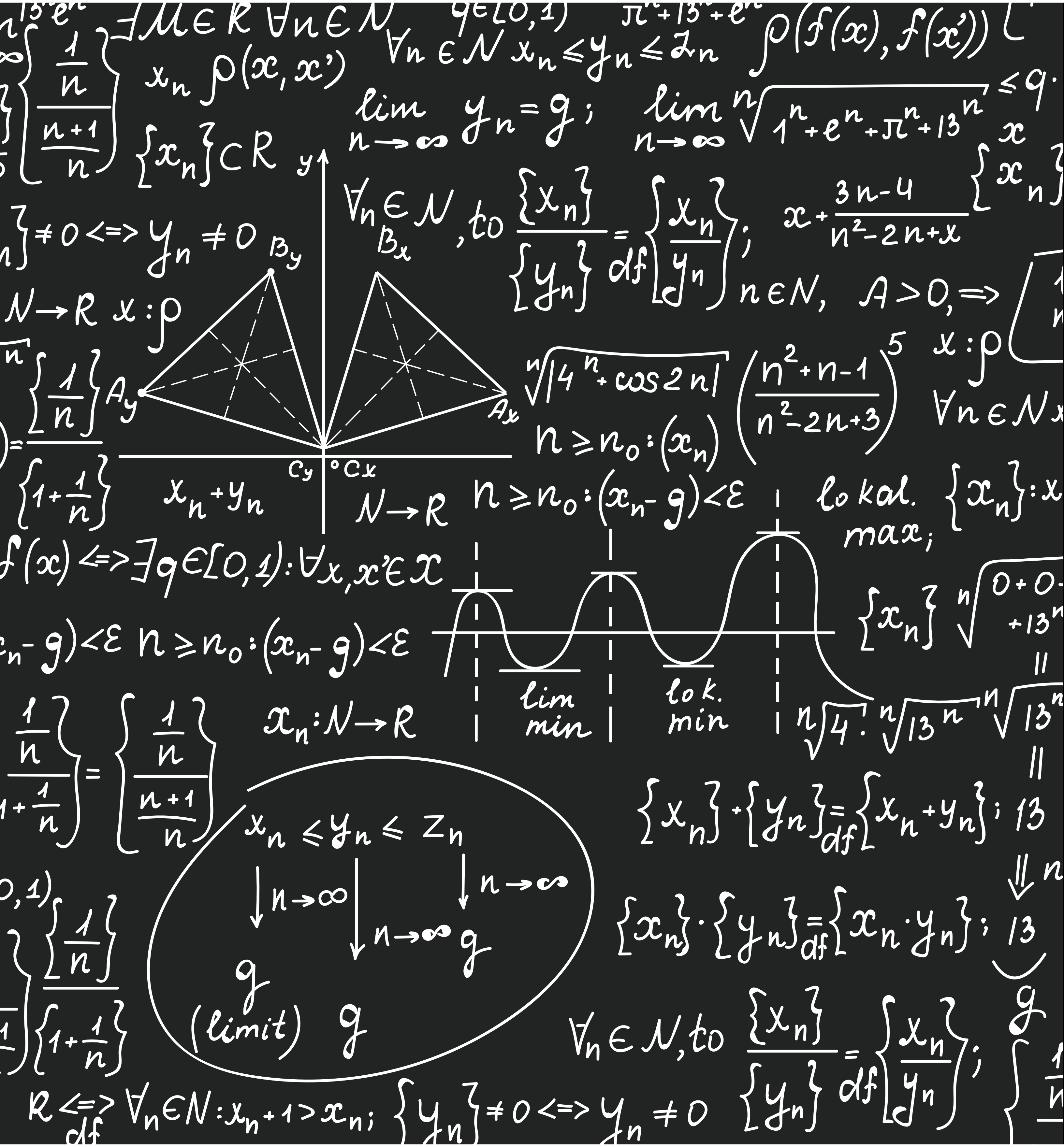
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'THERE'S FRACTIONS IN MY SUBTRACTION AND X DON'T EQUAL Y'

SOCIAL SECURITY MATH, EXPLAINED.

BY BRIAN KALLBACK

MARINA SUN / SHUTTERSTOCK.COM

JIMMY BUFFETT

sings about beautiful faraway beaches, cold refreshing drinks, and a cabana lifestyle free from worries. Yet, when he wrote the song, "Math Suks" in 1999, he could not have envisioned his "fractions in subtractions" and "X not equaling Y" relating to plan sponsor and participant perceptions about Social Security. (*Buffett, 1999*)

For decades, Social Security has been the subject of debates and anxiety. A system built on the contributions of current workers to support current retirees is often blasted by opponents as a big government Ponzi scheme. In today's media environment, anyone can post "news" that purports to tell a secret about Social Security – be it funding inadequacies or a proprietary, beat-the-system type strategy. This leads to political posturing, fear-mongering and blatant misinformation across the financial landscape.

Social Security, once counted on by Americans to support a portion of their retirement life, is under attack. Many members of the Gen X and Millennial generations are completing retirement projections *without including Social Security* in order to plan for a future without its assistance.

How did we get to this point?

For one thing, follow the money. Unfortunately, using fear is a successful sales strategy for selling annuities, cash value life insurance, proprietary investment strategies and other financial products. If a plan participant does not believe Social Security will be around, it will be necessary for him or her to increase contributions into a qualified retirement account or tax sheltered annuity. While it may not be in the sponsors' or participants' best interest to plan for a future without Social Security, it may be in the salesperson's best interest to make them believe it is.

LANE V. ERICKSON / SHUTTERSTOCK.COM

A SYSTEM BUILT ON THE CONTRIBUTIONS OF CURRENT WORKERS TO SUPPORT CURRENT RETIREES IS OFTEN BLASTED BY OPPONENTS AS A BIG GOVERNMENT PONZI SCHEME.

Like so many topics in financial literacy, much of this misinformation – purposeful or not – occurs due to the math behind the messaging. Here is where Buffett's "fractions in my subtractions" relate. Loaded language can be used to convey a sense of fear, and reason cannot shine through when participants' technical understanding is lacking. For example, consider the word insolvency. "Insolvency means Social Security's trust funds are unable to pay benefits *in full and on time*. It does not mean that Social Security will be 'completely broke' and unable to pay any benefits." (*Morton, 2018, p. 4*) However, analyze marketing messages and media stories for the frequency in which "insolvency" and "broke" are often associated.

This pattern of misinformation and scare tactics is not new. Consider Table 1, which presents two narratives – one from 1983 and one from 2018. Notice the language used, the lack of technical depth, and the persuasive elements within the narratives.

This culture of confusion can make it very difficult to individually research Social Security. Both conscious and subconscious bias are inherent in almost every piece of research. The tempestuous climate, the marketing

Table 1: Narratives, 1983 and 2018

1983	2018
Bankruptcy is defined here as the *inability* of the program to fulfill all the benefit promises it is currently making to future beneficiaries. These promises are made to today's taxpayers to *convince them to continue paying their taxes*. Today's workers are *being lulled* into making their future plans based on such promises. The *inability of the program to fulfill these promises* would, therefore, be a major social, economic, moral, and political problem. And, despite the attempt by many to downplay the significance of this potentially enormous problem, *the threat of bankruptcy for the Social Security system remains quite real. (Ferrara, 1983, 53)*	*Social Security is running out of money.* You may not believe that, but *it's a fact.* That FICA money taken from your paycheck *was not saved for you in a "trust fund." Politicians misled us. They spent every penny the moment it came in.* This started as soon as they created Social Security. They assumed that FICA payments from young workers would cover the cost of sending checks to older people. After all, at the time, most Americans died before they reached 65. Now, however, people keep living longer. There just aren't enough young people to cover my Social Security checks. *So Social Security is going broke. (Stossel, 2018)*

Note: Emphasis added.

machines of lobbyists, and the "third-rail" nature of Social Security make it very tough to discuss civilly. As Andy Landis states, "where does an 800-lb gorilla sit? Wherever it wants. And where does the most popular government program sit politically? You got it." (*Landis, 2018, p. 28*) Yet, Social Security is "a math problem that can be fixed by forward-looking politicians." (*Wasik, 2018*) Though with "about one in every six Americans receiving Social Security payments each month – most of them voters," this is a topic that will require political courage, compromise, communication, and content knowledge to move the needle. (*Landis, 2018, p. 28*)

With each paycheck, an employee contributes to Social Security via FICA taxes. A 7.65% tax is separated into contributions for Social Security (6.2%) and Medicare (1.45%).

In analyzing the Social Security portion alone (not the 1.45% to Medicare):

- The majority is used to pay benefits for current retirees, their families, surviving spouses and children of workers who are deceased.
- The remainder funds the current benefits for people with disabilities and their families.
- Any amount above and beyond the current need is contributed to the Social Security Trust Fund, which is a rainy day fund designed to subsidize payments to current workers when current tax revenue is not enough.

Thus, the flow of money highlights that we are paying taxes first to fund the benefits of current retirees, their families and their children, as well as benefits for people with disabilities and their families. Any additional money is saved for future retirees via the Trust Fund.

As members of the pension community, we understand that pension math is not that straightforward. Pension math cannot be simplified into a bumper sticker, a commercial or an ad. The problem is deeper than the flow of money from paycheck to current retiree.

Millions of employees pay into the Social Security system. There are also millions of employees who are currently retired, disabled or deceased and are receiving benefits. Table 2 shows the last three years of the number of people receiving Social Security benefits.

Table 2: Number of People Receiving Social Security Benefits

	Retirement Beneficiaries	Disability Beneficiaries
2017	49,156,959	10,806,466
2016	50,297,237	10,610,070
2015	51,492,108	10,411,252

Source: "Social Security Benefit Statistics" (www.ssa.gov)

Are those numbers high? Are they low? Well, potentially neither. *Meaningful data is derived from the worker-to-beneficiary ratio*, which measures the number of people working and contributing taxes to the Social Security system versus the number of beneficiaries presently receiving Social Security benefits. The ratio matters more than a singular observation of the number of people receiving benefits.

Through most of our history, Social Security has been a pay-as-you-go system in which FICA tax contributions have covered the benefit payments. The pay-as-you-go system worked fine as long as there were enough workers paying taxes at one end of the pipeline to supply the payments for the beneficiaries at the other end. Thus, the higher this ratio, the better.

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As evidenced in Table 3, a major demographic issue has been brewing: *This ratio is declining consistently*.

Table 3: Worker-to-Beneficiary Ratio, 1940-2010

Year	Ratio
1940	159.4
1950	16.5
1960	5.1
1970	3.7
1980	3.2
1990	3.4
2000	3.4
2010	2.9

Source: "Table IVB2, Covered Workers and Beneficiaries, Calendar Years 1945-2086" (www.ssa.gov)

The Social Security Administration's actuaries project the ratio to decline to 1.9 in 2086. Fewer children being born leads to fewer workers, and more people living longer adds stress to the worker-to-beneficiary ratio. Enormous pressure is then placed on the pay-as-you-go model, which can lead to accessing the Trust Fund to pay out current benefits. Should the Trust Fund equal 0% or become negative, it is insolvent. Presently, the Trust Fund is "deemed financially adequate in the short term if … [it is] above 100 percent for the first 10 forecasted years." (*Kashin, 2015, p. 253*) In other words, we are solvent for the short term. But beyond that, insolvency becomes a concern.

Integral to the question of insolvency is the numerous variables and inputs required to understand how much the system needs to pay out in benefits now… and later. These assumptions are "required to project the future benefit payments due to a retiree or a group of retirees. This aggregated lump sum benefit amount is then discounted back to the present day in order to define the required contribution needed today to fund the future payments." (*Kallback, 2018, p. 52*) Assumptions, such as demographic variables (for example, mortality rates) and economic variables (for example, labor force participation rates) help determine the stress on the system. (*Kashin, 2015, p. 240*)

Based on projections, after 2034, "the trust fund will be depleted and the system will revert to the pay-as-you-go" model of old. At this point, "tax income alone is sufficient to pay about 77% of benefits" (*Landis, 2018, p. 261*). Legislative reforms are needed to fill the 23% shortfall, to continue to pay full benefits after 2034." (*Landis, 2018, p. 258*) However, "since the system has the ability to draw on tax rolls it cannot be bankrupted; benefits can decrease and ages for benefits can increase, but it can't go completely broke." (*Blankenship, 2013, p. 147*)

In addition, should the Trust Fund be exhausted, there is an interesting legislative dichotomy that would need interpretation. "The Social Security Act stipulates that every fully insured individual is entitled to receive benefits from Social Security. On the other side, the Antideficiency Act prohibits the federal government from paying Social Security benefits beyond the balance of the Trust Fund. (*Kashin, 2015, p. 253*) On one hand, everyone who is fully insured is owed benefits, but on the other hand, the government is potentially limited (cannot borrow to meet obligations) in what it can pay out if the Trust Fund is exhausted.

No matter our personal feelings on Social Security, it is on the minds of our plan participants. For many people, the numbers do not, as Jimmy Buffett sings, "come together in some kind of 3rd dimension; a regular algebraic bliss." (*Buffett, 1999*)

Social Security is a major portion for many of our participants' retirement income picture. And research after research – whether from higher education or the retirement plan industry – highlights how uncomfortable and unknowledgeable people are concerning their math skills. How we address it will depend upon the expertise and philosophy of our education teams. The skills required to address this may be more psychological than numbers-based. Many of our participants simply need confident reassurance amidst the storm of conflicted advice and the immediacy of the 24-hour news cycle.

Regardless, we are often on the front lines in educating people about their financial lives. So be measured, be realistic, and, above all, be unbiased when plan sponsors or participants ask you about the current state of Social Security. **PC**

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THE EVOLVING MEP AND PEP LANDSCAPE

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PROVIDERS ACROSS THE RETIREMENT INDUSTRY ARE ACTIVELY AT WORK DEVELOPING NEW STRATEGIES AND PRODUCTS FOR A MORE POOLED, PROVIDER-CENTRIC WORLD.

By Pete Swisher

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"SO, when do you think we'll get open MEP legislation?" As an experienced retirement professional, I did the math on this and determined that I would be able to retire 2.7 years early if I had a nickel for every time someone has asked me that question.

There is a lot of genuine movement across the industry surrounding multiple employer plans. Congress is not currently one of the sources of movement, despite a widespread, two-year-old belief that open MEP legislation is imminent. Rather, the movement is in association plans, in advisors actively seeking MEP or MEP-like solutions, and in service providers crafting their strategic responses. This article explores how MEPs actually work in the marketplace in the context of unfolding law and regulation.

LEGISLATIVE AND REGULATORY SUMMARY

- "Open MEPs" that allow truly unrelated employers to join are not considered single plans under ERISA,[1] and this holds most service providers back from actively creating new MEPs.
- Many interested parties want to make MEPs widely available. Congress seems to love the idea, and there have been roughly 20 MEP-friendly legislative proposals since 2010.
- The Retirement Enhancement and Savings Act (RESA), which has been proposed and reproposed several times since 2016, points to the most likely form of open MEP legislation.
- The president's Executive Order on Strengthening Retirement Security in America, issued in August 2018, directed the DOL and IRS to study ways to remove obstacles to MEP formation, and in particular directed the DOL to facilitate "Association Retirement Plans" (ARPs).
- Very shortly after the executive order, the DOL published proposed regulations on ARPs, strongly suggesting that they had been working on the proposal already.

RESA, PEPS, AND PPPS

Reporting on RESA and its contents is widespread, so this article does not discuss it in detail, but a summary is in order. RESA includes a provision creating Pooled Employer Plans (PEPs) governed by a service provider as a Pooled Plan Provider (PPP) as a new pathway to creating MEPs.[2] A PEP is just a MEP – it is not something new – but it is a new *path* for creating MEPs that is not currently available, and the industry is devoting considerable energy to figuring out how best to approach the market if the PEP pathway becomes a reality.

The point to focus on with RESA and PEPs is that they might facilitate a migration toward a more *provider-centric* approach to plan sponsorship and governance. More on that below.

THE ARP REGULATIONS

Proposed regulations were published in October 2018, and final regulations are expected at any time (in fact, they could be published by the time you're reading this). Here are highlights that seem likely to make it into the final regulations:

- The ability to create a MEP that is a single plan for ERISA purposes is expanded. Groups or associations of employers that would not previously qualify for "closed MEP" treatment[3] may now sponsor a MEP.
- Examples of new potential sponsors include groups of employers within a single trade, membership associations of almost any kind, chambers of commerce, and groups of employers in a single state or metropolitan area.
- Professional Employer Organizations (PEOs) can sponsor MEPs, and so can service providers who are not necessarily PEOs, but who provide enough PEO-like services (e.g., payroll) to meet the PEO definition for purposes of sponsoring an ARP.

Note that "Association Retirement Plan" is just a catchy name for a MEP sponsored by one of these groups – it is not a special type of plan that is different from existing MEPs. The key effect of ARP regulations will be a significant expansion in the number of groups or associations that may sponsor

THE MOVEMENT IS IN ASSOCIATION PLANS, IN ADVISORS ACTIVELY SEEKING MEP OR MEP-LIKE SOLUTIONS, AND IN SERVICE PROVIDERS CRAFTING THEIR STRATEGIC RESPONSES.

a MEP. But the ARP proposal does not allow a true "open" MEP – it simply makes "closed" MEPs available to a broader audience.

ARPs, like PEPs, move the needle toward more centralized sponsorship and governance, but with the difference that ARP governance is centered on groups of employers and PEOs, while PEPs are centered on service providers.

WHEN WILL WE GET OPEN MEP LEGISLATION?

This is a mostly pointless question. Factors to consider in making such a prediction include:

- The new Chairman of the House Ways & Means Committee, Richard Neal (D-MA), is a strong supporter of RESA-like legislation and is expected to repropose a variation soon.
- Passage of RESA has been viewed as highly likely since late 2016. A "runaway freight train," some said.[4]
- Support for such legislation remains bipartisan and is all but unanimous. However, this has been going on for nearly a decade; only 4% of bills become law; and unanimous bipartisan support is a slender reed on which to base legislative predictions these days.

WHO CARES, AND WHY? THE TWO BENEFITS OF A MEP

What's the big deal? What do MEPs offer that we cannot duplicate through other means? Everyone thinks the answer is cost: MEPs are cheaper, therefore they will close the coverage gap. This is wrong. MEPs may, in fact, be cheaper, but not in the way people think. And they will help shrink the coverage gap incrementally, but not come close to closing it.[5] It helps, therefore, to understand what the actual advantages of a MEP are: simplicity and "the consortium effect."

Simplicity

There is a layer of simplification that is inherent to the structure of a MEP – something that cannot be replicated in an aggregation of single-employer plans, even if those plans have the same fiduciaries, vendors, and funds in a packaged, specially priced arrangement. The source of the advantage is having a *single plan document* with a *single appointing authority*. One document means one sponsor appointing one or more named fiduciaries and service providers – a central person or group of persons governing the plan on behalf of all adopting employers, instead of each adopting employer retaining its own set of governing chores by virtue of sponsoring its own plan.

Think about the litany of things we tell employers they are responsible for: maintaining their plan document; appointing fiduciaries and committee members; having quarterly meetings; doing benchmarking, RFPs and RFIs; establishing and following investment policies; monitoring performance; and more. These are governance chores that exist at the plan level, so 100 employers with 100 single-employer plans need 100 committees doing 100 sets of chores. In a MEP, with some caveats, governance can be done once for all 100 employers.

To summarize the source of simplification in a MEP, since there are often misperceptions about this: administrative chores and investment chores can be outsourced to professional fiduciaries in a single employer plan, so there is nothing unique in the MEP structure in having a 3(16) plan administrator[6] or a 3(38) investment manager,[7] though these are legitimate advantages of a MEP over plans that do

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not have professional fiduciaries. Fund costs can be minimized through the use of omnibus or super-omnibus trading and by service providers or program sponsors leveraging their scale, and this can be done without a MEP. But the governance chores that come with sponsoring one's own plan are mostly eliminated in a MEP, because those chores are handled *en masse* for the MEP as a whole.

The Purchasing Consortium Effect: Cost vs. Price in MEPs

There is a disconnect between what MEPs actually are and what people want or imagine them to be. The rhetoric in Washington and in the media tends to center on cost and coverage – MEPs are good for America because they're so much cheaper, and will therefore help ensure small businesses have access to affordable retirement plans. The reality is that MEPs have the potential to obtain significant pricing concessions, but do not have significantly lower costs to operate than single employer plans in most respects.

There is a difference between cost and price. If it costs $4,000 to operate a small 401(k), it still costs about $4,000 to operate an employer's piece of a 401(k) MEP. The MEP will not turn a $4,000 thing into a $400 thing, and the tiniest employers hesitate to pay even $400, not to mention contributions for employees.

To understand why operational costs are not much lower in a MEP, consider that each new employer is simply a new increment of work for purposes of compliance testing,[8] training and interacting with the payroll contact, processing payroll, and more. Each new participant, similarly, is a new increment of work for purposes of mailings, trading and call center support. Each new employer location is new work for those handling participant education and other onsite services. Some costs are scalable and therefore go down as the MEP grows (e.g., plan amendments and restatements; fund menu selection and monitoring), but most operational costs do not budge.

The MEP's potential advantage over a single employer plan is therefore not cost – it is *price*.

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Consider an association of employers who come together to bargain for plan services. Assume there are 100 employers with $200 million of assets and 5,000 participants, and the association has empowered a small committee to bargain for the group. What pricing concessions can this group negotiate under the following scenarios?

- **Endorsement Scenario.** The group offers an optional benefit and gives vendors the right to market the program to members. The vendors know from experience that uptake will be modest.
- **"Seeding the Plan" Scenario.** Ten members of the group with $20 million of assets commit to the plan in advance. After that first wave, the program is still just an endorsement and marketing opportunity.
- **Fully Committed Scenario.** All 100 employers are already in the same plan with the same service providers and negotiations for services can be based accurately on moving the entire $200 million without needing to make 100 separate sales.

In all three examples there is a purchasing consortium that has some degree of pricing power, but having an entire block of business already committed and legally movable via decision by a single committee. That's power.

Any group of employers can form a purchasing consortium – the MEP structure is not necessary – but for maximum pricing power, the entire group must be movable by a single decisionmaker. MEPs therefore lend themselves to maximum pricing power with respect to any vendor decision for which decisions are made centrally, not by each adopting employer.

PRICE VS. QUALITY AND LEVEL OF SERVICES

A single fiduciary in charge of getting it right for lots of employers will have a target on his or her back for regulators due to the scale of the responsibility. Getting it right and getting it cheap are not especially compatible, so an unbalanced focus on price is not appropriate.

Furthermore, the exact thing that makes life easier for an employer adopting a MEP – not sponsoring one's own plan and letting someone else handle governance – actually increases underlying costs directly. In a single-employer plan, a vendor can be a non-fiduciary, leave various fiduciary responsibilities on the employer's plate (e.g., mailings, filings), and therefore offer a cheaper price. If the vendor instead has to handle these responsibilities itself – and is responsible for getting them right, not simply claiming to offer them – its costs go up. A consortium can negotiate for the best possible price, but the negotiation is with respect to a higher level of services that cost the vendor more to provide.

Pricing power is a genuine potential benefit of a MEP, but the underlying cost of services on which the price negotiation is based actually is likely to be higher in a MEP than in a self-administered single-employer plan because of the legal imperative to handle fiduciary duties prudently.

That said, it remains a fact that the marketplace thinks MEPs are all about cost and wants cheap MEPs. How this cognitive dissonance will resolve itself is focus of strategy discussions throughout the industry.

IF MEP LEGISLATION PASSES, WHAT WILL IT MEAN?

Open MEP legislation will make provider-led[9] open MEPs possible, but the DOL will need to craft guidance before vendors will be ready to launch. There are several reasons for this, but the most important is the need for prohibited transaction exemptions (PTEs). Here is a framework for how the legislative and regulatory process might play out:

- PEP legislation passes; vendors can now offer open MEPs. This includes TPAs, recordkeepers, advisors, asset managers and potentially others.
- But who is the sponsor? Who is the Pooled Plan Provider (PPP), and which named fiduciary duties must the PPP hold onto versus outsource? Which duties can be shared with other named fiduciaries? What, exactly, is the responsibility of an adopting employer?
- And most importantly, how can a vendor stay in control so that it cannot simply be fired from its entire block of business within a MEP? The essence of the ERISA chain of command is that an independent fiduciary must decide who provides what services for what compensation.[10] You can't have a vendor hiring itself and choosing its own compensation.

THE INDUSTRY IS DEVOTING CONSIDERABLE ENERGY TO FIGURING OUT HOW BEST TO APPROACH THE MARKET IF THE PEP PATHWAY BECOMES A REALITY.

- The DOL therefore crafts guidance to answer these questions. That guidance likely will include one or more regulations and one or more PTEs.

The question, therefore, is what the DOL guidance might look like. Below are some possible approaches which are not mutually exclusive – the DOL could create more than one path. Let's look at three possible approaches.

The 'Vote with Your Feet' Approach
Some industry members would like Congress and/or the DOL to say that simply joining a MEP and thereby explicitly approving the services and compensation for one's own employees constitutes approval by an independent fiduciary. Thus, even though no one would have the power to remove the primary provider over the MEP as a whole, as would ordinarily be the case in an ERISA plan, the independent fiduciary requirement of DOL Reg. Sec. 408(b)(b)(2)(e) would still be satisfied.

But another view is that the vendor in such an arrangement is essentially unfirable and there is no ability for members to control services and compensation, and the binary choice to stay or go – to "vote with your feet" – is not enough control by adopters to satisfy the need for approval by an independent fiduciary. Therefore, if the DOL makes a variation of this approach available, there will be conditions, such as additional disclosures, and possibly the need for a third-party independent fiduciary.

The Third-Party Fiduciary Approach
The term "independent fiduciary"[11] refers to an unconflicted fiduciary, not a particular business model, though the term is sometimes intended to refer specifically to an independent fiduciary who is a third party – such as a fiduciary appointed by the DOL in troubled plans. The employer – not a third party – is the usual independent fiduciary in an ERISA plan. The issue in a MEP is how to replace the employer with someone else. One way is to hire an independent fiduciary who is separate from all parties – a third-party fiduciary who has little or no interest in the service providers and who is not an adopting employer. This person might add a layer of cost and complexity but could answer the independence concern by providing separate approval of the reasonableness of service provider fees and compensation.

The Board of Directors Approach
A MEP controlled by a vendor versus one controlled by a board or committee of adopting employers, or by an association or PEO,[12] bypasses the need for a PTE. In this structure, the vendors are not in control – the adopting employers, represented by the board, committee, or other independent fiduciary,[13] are. Such a structure would not need a PTE to operate because there is no prohibited conflict of interest.

For a large service provider, the problem with this structure is that it puts too much business potentially at risk, so it is not a structure that large vendors are likely to use other than when hired directly by the sponsor of an ARP or corporate MEP. For their own national PEP product, large vendors will probably be looking for more certainty, which is entirely reasonable.

THE 'SECOND SALE'

Retirement plans are sold, not bought, and MEPs are no different. One thing that is clear to those of us on the sales side is that the first sale – to the association, PEO or group of employers itself – does not guarantee follow-on sales. Associations will not, as a rule, sell plans. Association members will rarely pick up the phone and ask to join. "Build it and they will come" is not a distribution strategy that will work with MEPs anytime soon. Someone needs to make the "second sale," as one recordkeeper executive describes it, to adopting employers.

CONCLUSION

MEPs are a big deal because they are a:

- Disruptor. They have the ability to take blocks of existing plan sponsors and combine them into new service provider arrangements. They are causing service providers across the industry to reassess foundational marketplace strategies and product lines. There will be winners and losers.
- Selective disintermediator. In specific circumstances, they can unseat multiple client relationships and consolidate them into a single relationship that leaves some prior vendors out of the picture.
- Simplifier. They can transform the employer's role from that of a plan sponsor in charge of plan governance to being simply a participant in a larger program, governed by others.

But the public discourse about MEPs is partially off base because:

- MEPs are not necessarily cheaper. They can bring pricing power to bear, but the underlying costs to serve them can actually be higher because more services are required.
- They will not close the coverage gap. They may dent it, but not close it.
- They will not sell themselves. A sponsor who builds a MEP and thinks clients will sign themselves up is mistaken. A MEP without distributors is just a brochure.

MEPs are not new, and ARPs and PEPs are just new ways to do something old. What is new is the potential for more widespread MEP usage, leading to increased pooling of resources and centralization of governance. This pooling trend is no longer hypothetical: It is already underway even without RESA-like legislation. Yet only legislation can spur the widespread creation of provider-centric MEPs by recordkeepers, TPAs, asset managers and advisors, because providers are not going to cede too much control without protections that only legislation backed by PTEs can give.

So, back to the question everyone is asking, "When will we get open MEP legislation?" Regardless of the answer, the industry is actively at work developing new strategies and products for a more pooled, provider-centric world. PC

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FOOTNOTES

[1] Employee Retirement Income Security Act of 1974, as amended. DOL Advisory Opinion 2012-04A is the DOL guidance that says open MEPs are not single plans for ERISA purposes.

[2] For a detailed discussion of RESA and PEPs, see *What 401(k) RESA Legislation Means For MEPS and PEPS* at www.pentegra.com.

[3] "Closed MEP" is a term of art referring to a MEP that qualifies as a single plan for ERISA purposes. The word "closed" refers to the fact that membership is limited to employers sharing a common nexus.

[4] In the wake of passage on a vote of 26-0 through the Senate Finance Committee in September 2016.

[5] Without a mandate for employers to offer a plan, the coverage gap is unlikely to close. The marketplace offers plenty of low-cost solutions for small employers, including IRA-based programs like SIMPLEs and SEPs, and the simplicity of MEPs is not sufficient motivation to get the tiniest of employers to adopt a plan. So MEPs can help, but will not close the coverage gap. (My own two cents.)

[6] That is, a professional fiduciary who is the plan administrator as defined by ERISA Sec. 3(16).

[7] An investment manager as defined by ERISA Sec. 3(38).

[8] Most testing in a MEP is done at the individual employer level per Internal Revenue Code (IRC) Sec. 413(c).

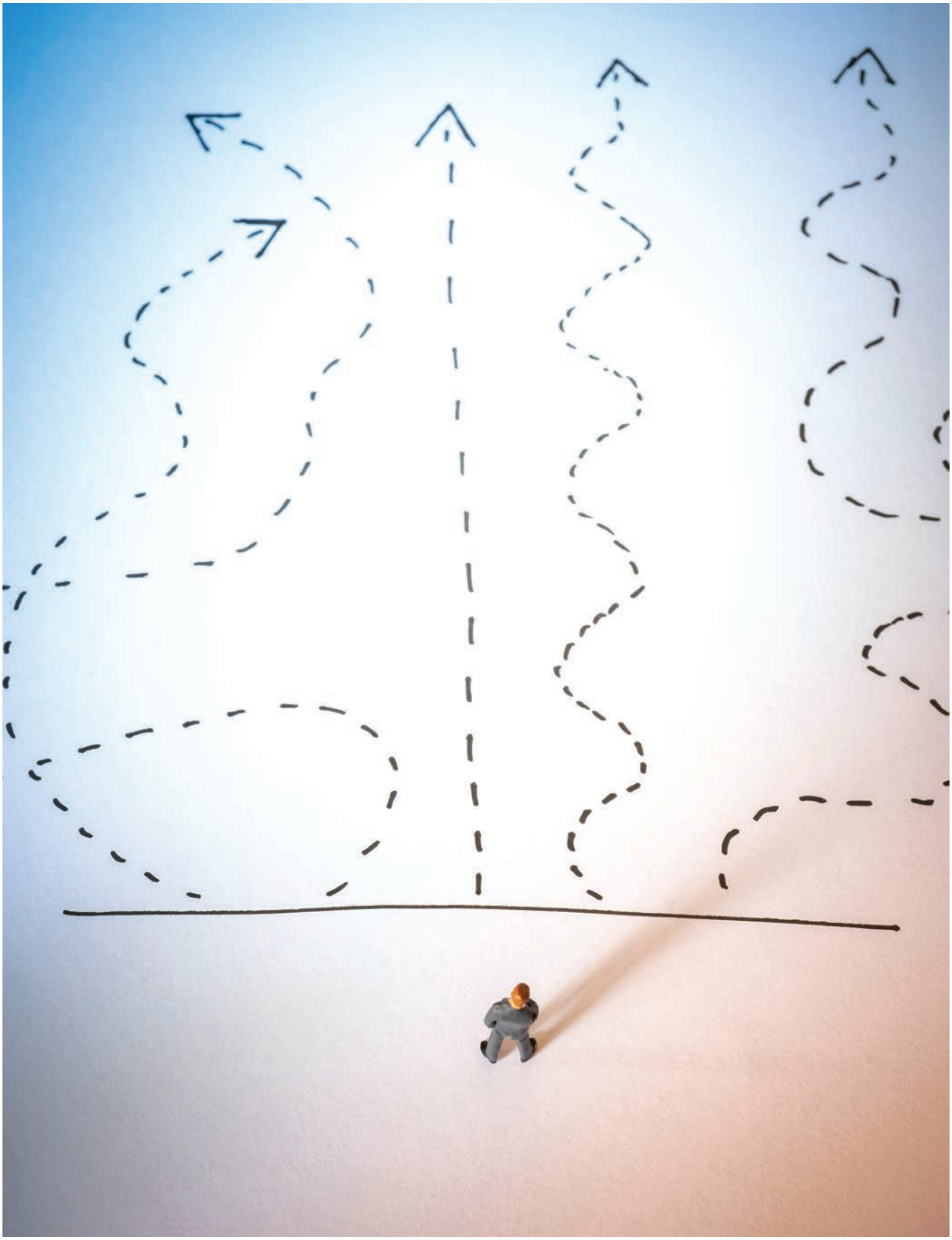
[9] Throughout this article I avoid the modifier "provider-sponsored" with respect to PEPs, because proposed legislation so far has not addressed whether the provider will be the actual sponsor. But for all intents and purposes it appears that "provider-sponsored" is the layperson's version of the intent of RESA.

[10] DOL Reg. Sec. 2550.408(b)(2)(e).

[11] "Independent fiduciary" is not defined by statute, but the DOL has offered guidance on it in the past. See, for example, the definition contained in the now-withdrawn conflict of interest regulations under the Best Interest Contract Exemption (BICE), as well as DOL's 2001 SunAmerica Advisory Opinion, DOL AO 2001-09A.

[12] In other words, controlled by an "employer" as defined by ERISA Sec. 3(5) who is an unconflicted independent fiduciary for purposes of appointing service providers and approving their compensation.

[13] E.g., a PEO, or the lead employer in a "corporate" MEP consisting of related employers.



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3(16) services

and Multiple Employer Plans

There are several different ways a 3(16) fiduciary can assist a plan sponsor and the MEP provider with a multiple employer plan.

By *Susan Perry*

Editor's Note: This is the latest in a series of feature articles by **Susan Perry** *of* **Fiduciary Outsourcing, LLC** *on 3(16) services and the growing 3(16) market.*

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I was planning to write about another 3(16) service this quarter, but with all the recent attention on MEPs, I've focused on the intersection of the two. So, do MEPs work better with a 3(16)? I think so. Here's why.

To get us started, let's assume a MEP is established by Anytown Chamber of Commerce to offer small businesses the opportunity to have a retirement plan. However, the folks at the Chamber of Commerce don't have a retirement specialist on staff. Anytown's financial advisor does a great job selling the new MEP and gets 300 small businesses to join in the first year by selling the ease and simplicity of the MEP structure.

Getting *All* the Data

Those of us who work in plan administration know that "it's all about the data." What data, you ask? *All* of the census information for *all* of the employees covered by the plan sponsor *and* the other MEP members.

Imagine an individual who worked for one MEP member in Anytown for six years, left their current employer and started working for a new employer. If the new employer is a MEP member too, this individual must be provided the opportunity to start saving upon hire with the new employer. If the data about this individual isn't uploaded each pay period, it would easy to see how the new employer could have a missed deferral opportunity by failing to get this individual saving right away.

At year-end, compliance testing must be performed for each member of the MEP. Imagine that half the plans are deferral only. That's 150 ADP tests to be performed. As you know, to complete the ADP test, the TPA or bundled provider needs census data

Those of us who work in plan administration know that 'it's all about the data.'

for the year from each member. But what kind of pull does the Anytown Chamber of Commerce have to get that data from its members? Is it possible that some of the members, if left to handle data uploading on their own, will only upload contribution files, with no census data? Maybe those eligible but not saving aren't yet recorded on the recordkeeper's website.

Who is responsible to ensure the year-end census data is provided, so that testing can be accurately completed? Here's where a 3(16) can help. The 3(16) can provide payroll integration services between the members' payroll systems and the recordkeeper. The 3(16) can pull the payroll information directly from each member's payroll systems if the MEP is set up to require a payroll integration solution. Yes, a non-fiduciary TPA could probably do this as well. However, the TPA can't make discretionary decisions about which types of compensation to include in the census file or which employees should be reported. A 3(16) has this discretionary decision-making authority.

So a 3(16) can get the all data to the recordkeeper each pay period for each member, enabling the plan year-end testing to be done easily for all members.

Automatically Enrolling Participants

Let's continue thinking about the Anytown Chamber of Commerce MEP. The service providers are going to want to be paid from plan assets. Who would want to collect fees from 300 separate members? So growing assets quickly is essential. If we think about an employee education effort, that means going out to 300 members' locations and offering some type of education to employees or doing something web-based. While this might work, automatic enrollment is the easier solution.

I know what you are thinking: "Automatic enrollment always gets messed up. There is no way the 300 members of our MEP are going to do automatic enrollment correctly." I agree. But the 3(16), if given the authority to update deferral percentages directly into the payroll system and issue the enrollment kits, can be the fiduciary over automatic enrollment. So a professional would be doing the automatic enrollment tasks instead of the assigned person at the member's location.

Why would someone want you to be a fiduciary to provide this service? Let's look at an example that my team experienced not long ago. A participant was saving 5% of pay. He logged into the recordkeeper's website and asked to change to 6%, but accidentally hit '6' twice, so he actually requested to change to 66% of pay. He hit 'ok' on the website and submitted the change request. This large change, from 5% to 66%, set off a warning flag. We contacted the participant, who was distressed to learn how close he came to having a 66% deferral. We used our discretionary authority to hold off making the change until after we had spoken to the participant. Without discretionary authority, we likely would have had to process this suspicious request, and as it turns out, would have left this double-digit-punching participant without enough left over to pay this month's mortgage.

> A 3(16) can take on the fiduciary responsible to auto enroll, and even auto increase.

A 3(16) can take on the fiduciary responsible to auto enroll, and even auto increase. That means more money in the plan faster, without the errors and issues associated with automatic enrollment. And the 3(16) has the data necessary to identify the employees moving from one member to another to ensure they are automatically enrolled in the plan.

Requests for Loans and Distributions

The Anytown Chamber of Commerce's plan has its first distribution request. One of our automatically enrolled participants wants to exercise their 90-day refund option. Who is going to approve that transaction? Another participant requested a distribution. Who is going to determine if the participant moved to another employer that is also a MEP member?

Not too much later, there's a participant request for a plan loan. Who is going to approve the transaction? What if the MEP member is only uploading contribution information and not census data each pay period? How would anyone other than the MEP member be able to confirm this participant is actively employed and eligible for the loan?

As we discussed in last quarter's *Plan Consultant* article, many of the recordkeepers will take the responsibility to approve these transactions. Or maybe it's the TPA that has obtained signing authority for loans and distributions. But they cannot act as the fiduciary.

If all of the data is being transmitted from every MEP member's payroll system to the recordkeeper, it probably is perfectly okay to have the recordkeeper or TPA approve the request. But I'm pretty certain that the Chamber of Commerce folks won't want anything to do with approving these types of requests. And, if the Chamber staff has concerns about fiduciary responsibilities, they might want someone to officially

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take a fiduciary role with respect to these requests. A 3(16) takes the responsibility for properly issuing money to participants and beneficiaries, leaving the MEP sponsor and members free from this burden.

Mailing Notices

My individual plan sponsors hate dealing with "annual notice season." They were likely told about participant communications sometime during the sales process, but imagine the MEP member who is told that joining the MEP will simplify their lives. They will likely expect someone else to mail out the notices for them.

What if the MEP members are only transmitting contribution information each pay period? There could be employees of members that the recordkeeper doesn't know about. TPAs generally get data only once a year. How does anyone know who is eligible to receive the notices?

That's where getting good data comes into play. Every pay date, each member needs to transmit accurate census and contribution data about every employee. And if you can't get payroll integration between the member's payroll system and the recordkeeper directly, a 3(16) can bridge the gap to create the payroll integration. Most 3(16)s offer mailing services or perhaps use the mailing service offered by the plan's recordkeeper to issue the mailings.

So a 3(16) can ensure that notices get mailed by providing address and email address information each pay period.

Conclusion

We have identified several different ways that a 3(16) can assist a plan sponsor, and the MEP provider, with their MEP. There are other ways, such as determining eligibility, dealing with all of the emails and to-do items received from the recordkeepers, or answering participant questions that would normally go to the HR department.

A plan sponsor should consider who is responsible for all areas of the plan's administration. If a MEP sponsor doesn't have enough of a relationship with its members to get all payroll data easily, they might be well advised to outsource these and other plan responsibilities to a 3(16). The result would free them to concentrate on their mission rather than risk getting bogged down in details for which they have no expertise. PC

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LIGHTFIELD STUDIOS / SHUTTERSTOCK.COM

2019 Hiring Trends in Retirement Services

The competition for qualified retirement professionals is at an all-time high. Here's a look at the industry numbers – including salary ranges.

BY STEVE ANDERSON

The retirement services industry as a whole kept hiring in 2018. This would follow what CPS Inc. has witnessed across all 12 professional industries we serve – last year, we broke our all-time record for annual revenue, which also went along with the highest-ever average of annual revenue produced by individual recruiters.

While CPS Inc. serves multiple markets, our No. 1 market segment was Retirement Services. In 2018, it was the highest producing market and was responsible for 27% of all hires, which also led the company.

The retirement services industry does not show any signs of slowing down in the near future. That means the competition for qualified professionals is at an all-time high. The need to attract, hire and retain talented professionals should be one of the highest priorities for any provider. The time to address those issues would be now – not when a current employee turns in a letter of resignation.

EMPLOYEE MOTIVATIONS FOR CHANGING JOBS

This year I surveyed retirement services professionals at all levels of experience about why they would consider making a job change. The options given were:

- Higher compensation: 39%
- Want more challenge/responsibility: 20%
- Company culture is not a good fit: 11 %
- Don't feel my current employer values me: 13%
- Concerns about company or job stability: 17%

The largest response – wanting higher compensation – certainly is not a revelation. The 39% cited marks an 8% increase from a previous survey in 2014. The exact same question was not asked then, but it is interesting that compensation is the one response that increased over the 4-year period; the others stayed the same or decreased slightly.

While I have not tracked actual percentages (maybe that's for next year's survey), the increase in base salaries when making a change seems to be increasing as well. Some of that is due to a candidate's expectations and some is due to what an employer will need to pay to compete with what other companies are offering the same candidate.

TARGETING TYPES OF COMPANIES

In more of an informal survey, we asked what types of companies candidates would be interested in working for when considering a job change. Most wanted to work for the same type of company they currently work for. Among those who were open to changing the type of company they would work for, there were some perceptions that stood out.

Recordkeepers. When considering large daily recordkeepers, candidates thought there could be room to grow or a ladder to climb since the work is more functionalized. Many also thought that a larger company might provide more job security.

Consulting Firms. Candidates considered consulting firms because they felt the work would be more complex rather than "cookie cutter" plans. There was also the idea that consulting firms offered a more objective viewpoint if they were not tied to the investments.

Third-party Administrators. TPAs are perceived as a better place to learn the industry, and to allow someone to be "more than a number." The perception existed that there

2019 SALARY TABLE

Position or Activity	Salary Range	Bonus Range
DC Plan Administrator (1 – 4 yrs.)[1]	$40,000 - $56,000	0 - 10%
DC Plan Administrator (5 – 9 yrs.)[1]	$48,000 - $72,000	0 - 10%
DC Plan Administrator (10+ yrs.)[1]	$65,000 - $96,000	0 - 15%
Team Leader[2]	$62,000 - $92,000	0 - 15%
Operations (managing direct & indirect reports)[2]	$85,000 - $165,000	15 - 40%
Internal Account Manager[3]	$55,000 - $76,000	0 - 15%
Relationship Manager, Consultant[3]	$78,000 - $155,000	10 - 40%
Employee Education – Enrollers	$55,000 - $80,000	10 - 25%
ERISA Attorney	$86,000 - $152,000	0 - 30%
Sales[4]	$60,000 - $150,000	W2's 100,000 - 450,000
DB Administrator & Actuarial Associate[5]	$56,000 – $96,000	0 - 10%
Conversions (data input & manipulation)[5]	$48,000 – $75,000	0 - 10 %
Conversions (project manager)[5]	$60,000 – $94,000	0 - 20%
ASA (less than 15 yrs.)[6]	$93,000 - $145,000	10 - 25%
ASA (15+ yrs.)[6]	$101,000 - $200,000	10 - 25%
FSA (less than 15 yrs.)[6]	$113,000 - $175,000	10 - 25%
FSA (15+ yrs.)[6]	$130,000 - $285,000	10 - 25%

FOOTNOTES

[1] DC Plan Administration is some combination of performing recordkeeping, compliance testing, form filings, trust accounting, and client communication.
[2] Salaries vary with the numbers of people managed and responsibilities for budgets, profit & loss, etc.
[3] Salary is in direct proportion to the average plan assets per client managed and the type of provider being worked for.
[4] Incentive packages for sales vary with assets and types of sales; direct, wholesaling, DCIO, etc.
[5] Add 3 – 10% for ASPPA, NIPA, and/or ERPA designations.
[6] Add 5 – 10% for Enrolled Actuaries.

"The retirement services industry does not show any signs of slowing down in the near future."

could be more job security at TPAs because they might have better profit margins. Also, the idea that a smaller company might offer more of a family atmosphere was appealing.

Actuaries. Actuarial firms were desired by those that work with defined benefit plans and to an extent those that want to pursue Society of Actuary exams. The exam incentive also was present for the consulting firms as well. And candidates believe that actuarial firms might produce higher-quality work.

Advisory Firms. Candidates considered working for an advisory firm because of the focus on investments. There also was a belief that a candidate with a strong background in plan design could play a key role for a firm. And some individuals believed there can be more flexibility and creativity with plan design features.

SALARY DATA

Having knowledge of candidates' current salaries and the compensation ranges that employers offer enables me to share data on salaries, bonuses, commissions and other parts of a total compensation package. The information in the accompanying salary table is gathered in my daily work within the retirement services industry.

Of course, actual salaries will be affected by many factors. Please reach out if you have any specific questions that I can share insights on. PC

Steve Anderson is the Section Manager, Retirement Services, at CPS Inc., a recruiting firm. He has more than 20 years of experience consulting in pension staffing. You can reach him at sanderson@cps4jobs.com.

Reimagining Social Security as a Lump Sum Benefit

Describing Social Security as a lump sum helps convey the integration of its value with a participant's qualified plan account balance.

BY MICHAEL E. KITCES & BRIAN KALLBACK

Editor's Note: This article was adapted for Plan Consultant by the authors. An unabridged version may be viewed at https://www.kitces.com/blog/valuing-social-security-benefits-as-an-asset-on-the-household-balance-sheet/

Recordkeepers and TPAs are not investment advisors. Instead, they are available to educate, administer and, in some cases, monitor a qualified plan for sponsors. While many of their education teams will go beyond the investment alternatives offered by a sponsor and discuss in broad strokes a participant's financial plan, the main responsibility of recordkeepers and TPAs is to ensure that the characteristics and functionality of the employer plan have been communicated effectively to a participant. Discussions and analysis on investment advice is for others.

And yet, that doesn't mean recordkeepers and TPAs shouldn't be aware of content that may assist in serving their sponsors. As a result, while Social Security may not be a focus of their education meetings or HR discussions, it doesn't mean Social Security is not a topic in which participants have questions and concerns.

In the past, *Plan Consultant* has included articles about Social Security, specifically the defined benefit characteristics of the program. For many participants, Social Security will comprise a majority of their retirement assets. During education meetings, portfolio allocations and/or myriad retirement accounts are often described as 'slices of a pie' or 'pieces of pizza' of varying sizes. Participants seem to understand the income retirement certain accounts will provide, or be relied upon, more than others, but they do not comprehend the complexities of the Social Security system.[1]

However, Social Security – as a stream of income – is not often included in that tasty retirement pie or pizza, which is typically focused just on assets on the participants' balance sheets. Yet in practice, the lump sum equivalent of Social Security can be calculated as an asset on the balance sheet, rather than a stream of income,

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which may actually help to provide clarity for participants trying to fully understand the true relative sizes of their pizza or pie slices.

ESTIMATING THE LUMP SUM VALUE OF SOCIAL SECURITY

Social Security is a guaranteed income stream available at retirement for those who qualify. Of course, any stream of income has an economic value to it; however, because Social Security is available *only* as a guaranteed income stream, with specified payments based on wages earned and a fixed starting date that can only be adjusted forwards or back by a couple of years, most people think of Social Security separately from the rest of their (other) assets. A portfolio is a portfolio, and guaranteed income is guaranteed income, and never the twain shall meet.

Nonetheless, the availability of Social Security is of material value to most participants, and decisions about the timing of how and when to use Social Security can impact the needs for drawing on other assets for retirement income. And in point of fact, it's actually relatively straightforward to estimate what the approximate value of Social Security *would be* as an asset on the balance sheet.

After all, Social Security's expected payments have an anticipated time horizon – the employee's life expectancy – and as payments backed by the federal government, have risk approximately comparable to that of any other government bond. And once you've determined the payment stream, a time horizon, and a growth/discount rate, it's quite straightforward to calculate a "present value" of the series of cash flows as though it were a lump sum asset. (See Table 1.)

COORDINATING THE VALUE OF SOCIAL SECURITY WITH OTHER RETIREMENT ASSETS

The factors that drive the value of Social Security also have an impact on the other assets in the retirement portfolio. When viewed from the balance sheet perspective, Social Security is not only a highly valuable asset overall, but one with very unique investment characteristics; unlike most other assets, its relative value *rises* in low-return environments (reducing the discount rate on future payments), and is further *enhanced* by unexpected inflation (which lifts the nominal amounts of future payments).

In addition, Social Security's asset value rises naturally the longer you live, which means its income stream which cannot be outlived (unlike the other retirement assets on the personal balance sheet) continues to grow exactly when it may be needed most. In other words, one of the primary reasons to delay Social Security and spend other assets first is that the Social Security asset is the one best hedged to the three risks that most damage traditional asset-based retirements: low returns, high inflation and unexpected longevity.

One notable caveat, though, is that the inclusion of Social Security on the personal balance sheet can actually lead to a materially "distorted" asset allocation, given that most would characterize Social Security as the asset-class equivalent of a government bond (or more accurately a TIPS bond given its inflation characteristics). After all, for most households that enter retirement with relatively modest retirement savings, a Social Security asset worth about $300,000 (for the average benefit) might be equivalent to the size of their entire retirement portfolio! A more affluent household that saves $500,000 for retirement – and has higher Social Security benefits also worth about $500,000 – may still find Social Security comprising about 50% of the total retirement assets. Yet if this household has $1 million in total retirement assets, including a "balanced" 50/50 portfolio *and* a Social Security "bond" asset, then their true asset allocation is not 50/50, but 25/75!

Unfortunately, though, the fact that the Social Security "asset" biases the household balance sheet towards bond holdings is difficult to fix. After all, given that Social Security isn't *actually*

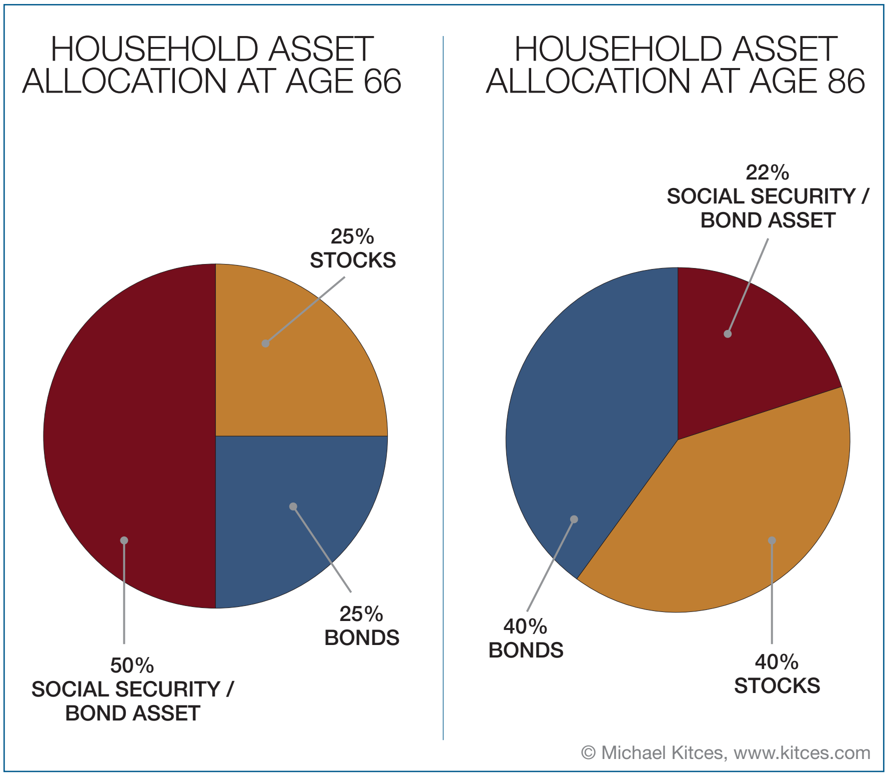
Table 1: Present Value of Social Security Benefit

	Male	Female
Average Social Security retirement benefit[2]	$1,413/mo	$1,413/mo
10-year Treasury rate[3]	2.73%	2.73%
Assumed inflation	3%	3%
Life expectancy[4] (at age 66)	17.09	19.55
Average "lump sum" value of Social Security	$296,281	$323,172
Maximum Social Security benefit[5]	$2,642/mo	$2,642/mo
Average "lump sum" value of Social Security	$529,903	$604,260

a liquid asset to be invested/allocated – or typically even seen as a lump sum account balance equivalent – getting to a 50/50 *total* mix of household assets would actually *require putting 100% of retirement portfolios into equities*! Yet while this may be justified from a total household net worth basis, it would clearly be difficult to implement in practice, where clients may fixate on the "equity-only" portfolio and its volatility, and not necessarily recognize the role that the Social Security "bond" asset is playing to diversify it!

Ironically, though, as most employees tend to rely on Social Security payments first (at least once they begin) and allow the portfolio to grow to the greatest extent possible, the distortion of the household balance sheet toward a bond-heavy allocation (once Social Security is included as an asset-equivalent value) actually resolves itself over time. As the years go by, the remaining value of the Social Security fixed-income-equivalent asset depletes (as it self-liquidates with payments), while the more-equity-based retirement portfolio tends to grow (especially in the first half of retirement when Social Security is spending down but portfolio withdrawals tend to still modest). Accordingly, the equity allocation of the household balance sheet actually glides higher on its own throughout retirement (as the equities in the portfolio comprise a larger percentage of total wealth) even if the portfolio itself typically remains 50/50 (or some similar allocation) in stocks and bonds.[6]

The bottom line, though, is simply to recognize that while it is not a "liquid" asset or one that is naturally valued, Social Security is actually a very material retirement asset for many participants… and one concentrated entirely into a government bond fixed-income-equivalent allocation, which can materially influence the overall pizza or pie slices of the household's asset allocation. Thus, while recordkeepers and TPAs are not investment advisors, their education and communication can still reflect holistic knowledge and recognition of Social Security. And in that context, describing Social Security as a lump sum can serve to better convey the true integration of the value of Social Security income payments and a qualified plan's account balance. PC



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THICHA SATAPITANON / SHUTTERSTOCK.COM

Increase Customer Loyalty with Social Media

Here's a simple way to reinforce your customers' decision to hire you.

BY SPENCER X SMITH

What's the best (and free) way that you can ensure your customers stay loyal to you? The answer: Love what you've *already* sold them.

You may be saying to yourself:

- "But I already check in with my customers every quarter."
- "But I already send them holiday gifts thanking them for their business."
- "But I already send them those handy return address labels in the mail each Thanksgiving."

All of those things are great, and I definitely wouldn't stop doing them. However, there's something deeper your customers want from you: reinforcement that they've made a good decision. They want to feel good about hiring you as their TPA or recordkeeper. Or put another way, they want reassurances that you're the best choice for them.

Here's where that perspective comes from. Back when I was working in the 401(k) industry (3,000+ in-person sales meetings between 2008 and 2015 for two of the nation's largest record-keepers), the vast majority of work we did entailed replacing an existing retirement plan. It was important for us as consultants to highlight the benefits of our offering, understanding at the same time that the person who chose their existing solution probably still worked there.

People don't want to be told they've made a bad decision, whether it's five minutes ago or five years ago, especially by someone trying to form a business relationship. So without insulting the incumbent 401(k) provider, we needed to highlight the benefits of our solution without criticizing anyone, especially our competitors.

Wait – isn't it better to throw stones and insult your competition? No way. The person who chose the incumbent will come to the defense of that company because he or she needs to defend their own decision.

Better to praise your competitors while highlighting the benefits of your offering.

So, in a customer retention situation, since you're the incumbent and you're trying to retain your customers, what can you do right now? What's a simple way to reinforce your customers' quality decisionmaking?

Here's an idea. Take out your portable video camera (a.k.a. your smartphone) and share with your customers – once a week, in video form so they can actually see you – a customer problem that you've fixed recently. Of course, protect the confidentiality of that customer (make it anecdotal) but briefly share a quick story. Start to finish, this video will take you less than an hour to record, edit and publish.

Then use your existing social media channels to show your followers and fans what you're doing. Simply upload this video to your YouTube channel, LinkedIn company page, Facebook business page and Twitter account. Many of us encourage our customers to follow us on social media, but very few of us actually produce valuable content for that audience.

This is really important for two reasons. First, it maintains top-of-mind awareness for you. I call this "ROTOMA." A play on ROI (return on investment), it stands for "Return on Top of Mind Awareness." People are either thinking about you or they're not, and it's much better if they are. Social media is where the vast majority of the population is directing their attention at some point each day, so why not show up where they are?

And second, it solidifies in your customers' minds your position as an expert in your field, showing them why doing business with you now and in the future is a great decision.

Okay, so you're not criticizing your competition right now, but you have the same question that we all do: What about compliance?

Let me answer that question with an example. There is a medical doctor of whom I'm a big fan. His name is Peter Attia. He writes blogs, records videos, and produces podcasts, many of which are hours long. Among these various channels, Dr. Attia discusses – in incredible detail – medical problems and possible remedies for them. He also shares the latest news on physical performance, supplements and drug therapies. If you've ever wondered how your body works (in great detail), I highly recommend his stuff.

Dr. Attia includes this disclaimer in his written material, as well as in his video and audio content:

> *"I will not respond to requests for medical advice, either as comments/questions on the blog, or direct messages to me, as I am not legally permitted to practice medicine over the interwebz. If I don't see a person in the flesh, I can't be his or her doctor over the ether."*

Yep, he says "interwebz." This physician, even in his disclaimer, makes a joke. He realizes the purpose of his content is to raise questions, not give advice. I think we can all agree that if a board-certified medical doctor is sharing his insights over the "interwebz," those of us in the retirement industry can too.

If you're not producing content on social media to help maintain your current customer relationships (and assist with your business development efforts, for that matter), what's holding you back? PC

> **"There's something deeper your customers want from you: reinforcement that they've made a good decision."**

Spencer X Smith has worked as a wholesaler for two of the nation's largest recordkeepers. He now runs AmpliPhi Social Media Strategies (a social media marketing company) and speaks approximately 60 times per year for financial services organizations and companies. He can be reached at spencerXsmith.com.

Training Your Staff on Professionalism

To protect clients from substandard work, new hires need to be trained in professionalism. Here are some tips on getting started.

BY LAUREN BLOOM

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Employee benefits professionals are busy people. Whether they're finding new clients, serving the clients they have, attending professional meetings and seminars, managing their firms, or writing for professional journals, they have a lot going on.

Let's take Sharon, for example. She opened a practice as a third-party administrator 15 years ago after leaving the Human Resources department of a large accounting firm. At first, she had only one client and was able to run her business from her home office. Sharon was skilled; her rates were reasonable; and prospective clients appreciated her warm personality and low-pressure marketing. She also became active in a few community groups and professional associations, including the American Retirement Association, where she quickly became a valued member and popular presenter.

Today, Sharon's practice has grown to the point where she can't handle all the work herself. She recently hired Tony, a young man fresh out of college with a degree in mathematics and computer programming, to pick up some of the work. Tony is smart and energetic, but he didn't know the first thing about benefit plan administration when Sharon hired him.

Sharon knows that Tony needs a lot of training, but she doesn't want to give up her association work, and she needs to generate more business to be able to pay Tony (and herself). Consequently, Sharon has given Tony some general instructions about how to fulfill various tasks, assigning him to work on several of her smaller plans. She reviews his work, corrects individual mistakes as she finds them, and – sometimes – remembers to tell Tony what the mistake was so he won't make it again.

Lately, though, Sharon has been busy enough that her review of Tony's work has been more of a spot-check, and she still hasn't given him any significant training on the ethical responsibilities that she and, by extension, Tony both have to the clients that they serve. However, Tony seems like a good guy, and Sharon has been assuming that he has enough common sense to avoid any obvious ethical lapses.

may want to invest in sending Tony to one or more of those meetings. She may even choose to close the office for a day or two and go with him to refresh her own understanding. If that approach is too pricey, there are also professionalism webinars available online. Sharon may want to watch them with Tony so they can discuss the webinars afterward and clear up any questions that he may have.

When Sharon reviews Tony's work, she'll train him better if she not only shows him the mistakes he made, but also explains what he did wrong and how to correct it. It may take longer than fixing it herself, but it will build Tony's understanding. She can also encourage him to start working toward his own professional credentials. A subordinate now, if Tony obtains his needed licenses and professional designations, he may grow into a junior partner in Sharon's expanding firm, able to train up talented young newcomers in his own right.

> "The internet is full of resources on ethics and professionalism, including the ARA Code of Conduct."

Sharon is courting disaster.

As a member of the ARA, Sharon is bound by the ARA's Code of Conduct. Precept 10 of the Code requires her not only to perform professional services with honesty, integrity, skill and care herself, but also to take reasonable steps to ensure that work performed under her supervision is performed that way as well. If questioned, Sharon would admit that she has been too busy to give Tony any meaningful professionalism training. However, Precept 10 has no exemptions for "busy-ness." Additionally, if Tony's work proves faulty, an angry client won't care that Sharon didn't have time to train her subordinate. So, what should Sharon do?

The internet is full of resources on ethics and professionalism, including the ARA Code. Tony knows his way around a computer, so Sharon could instruct him to put together a set of materials that are relevant to his professional obligations as an aspiring third-party administrator. Once he has them together, Sharon can go over them with him and discuss why he chose them, what seemed important to him, and what other materials he might have considered. This first step will likely give Sharon a better sense of how well Tony understands the importance of bringing high professional standards to his work.

The ARA and other organizations also offer meetings and seminars that include professionalism training. Sharon

Sharon may also want to include Tony in client meetings, both to let him see what happens and to familiarize him with the people for whom he's working. That should deepen Tony's loyalty to the clients and determination to do excellent work for them. It may also be helpful if one of Tony's mistakes slips through. A client who knows and likes Sharon's bright young trainee may be more forgiving than one who does not.

Sharon should also go over the ARA Code of Conduct with Tony, highlighting Precept 10 and explaining her obligation to oversee his work. While that obligation may seem obvious to an experienced practitioner, it may feel intrusive to an eager young subordinate. That conversation can lead to others about the Code, teaching Tony while reminding Sharon of her own responsibilities.

To protect clients from substandard work, subordinates need to be trained in professionalism. In my next column, we'll look at a common ethical mistake that inexperienced employees often make and review ways to prevent it. PC

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The Perils of Employer Stock in a 401(k)

The increased risk of litigation has caused many employers to reconsider the decision to offer employer stock as an investment option.

BY BRIAN KALLBACK

Ponder this anecdote from the 2013 book, *The Smartest Guys in the Room: The Amazing Rise and Scandalous Fall of Enron*:

> Later in that same meeting [a December 1, 1999 participant meeting], Cindy Olson, who ran human resources for Enron, took to the podium to answer questions. One written on a card was handed up to her. "Should we invest all of our 401(k) in Enron stock?" she read. She looked up at the auditorium full of participants and replied, "Absolutely! Don't you guys agree?" She smiled at Lay and Skilling. *(McLean, 2013, p. 242).*

As we know the eventual fate of Enron, this anecdote should make us all cringe.

Employer stock in a qualified plan is a complex issue. From an organizational standpoint, it can produce desired cash and liquidity. By creating a market for its own equity, an organization can pursue a variety of strategic objectives and initiatives. From a morale and motivation standpoint, participants who own employer stock may be better aligned with organizational goals, as they have "skin in the game."

Participants may also benefit if the expected return of the employer stock exceeds other investment options. Though undiversified and concentrated, employer stock can provide an efficient, low-cost manner of investing. Finally, participants may receive favorable tax treatment due to net unrealized appreciation (NUA). (For NUA, it's imperative an organization's benefits team track the historical basis of employer stock contributions, as otherwise determining NUA could be a mess… but that's a story for another day and column.)

The benefits for inclusion of employer stock sound enticing. Yet, "the increased risk of litigation has caused many employers to reconsider the decision to offer employer stock as an investment option. There have been numerous participant claims regarding participant stock in employer-sponsored plans." *(Tedesco, 2017)* Unbiased investment management for a qualified plan is difficult enough, and employer stock makes it all the more problematic.

ERISA CONSIDERATIONS

ERISA includes rules concerning investments offered within qualified plans, but there is no list of approved investments. In general, a plan sponsor who wishes to act in a fiduciary manner should exercise judgment that a prudent investor would use in investing his or her own assets. ERISA requires plan sponsors to:

- work solely in the best interests of the participants;
- exercise the prudence and diligence of a knowledgeable fiduciary;
- ensure diversified investments, especially away from employer stock; and
- adhere to the relevant plan documents.

"Unbiased investment management for a qualified plan is difficult enough. Employer stock makes it all the more problematic."

Concerning employer stock, restrictions are based on whether the plan is a DB or DC plan. Plan sponsors can include employer stock as an investment alternative and avoid prohibited transaction status if "the acquisition or sale is for adequate consideration and no commission is charged on the acquisition or sale." *(Turley, 2017)* A 401(k) plan, as long as it offers at least three diversified investments, may allow for greater flexibility concerning employer stock inclusion.

YES, ERISA §404(c) IS ATTAINABLE

However, it may not be easy. ERISA §404(c) is attainable *in a limited manner* for employer stock. The limitation results from the DOL's recognition that conflict can occur in the inclusion of employer stock in a plan, as well as the difficulty many proprietary investments have in qualifying as an appropriate investment.

For ERISA §404(c) to potentially apply, the following requirements must be met.

The employer stock is publicly traded

Employer stock must be publicly traded in order to qualify for ERISA §404(c) treatment. Stock of non-publicly traded, closely held companies is not subject to ERISA §404(c), regardless of whether the participant elects to invest in the employer's stock.

There is a liquid market for the employer stock

Participants must be able to execute transactions as desired. When an investment is lightly traded, it may not be subject to ERISA §404(c) due to lack of liquidity. In addition to ensuring adequate liquidity, certain investment alternatives within the plan (money market or "core" funds, for example) must accept transfers of employer stock as frequently as transfers can be made from other alternatives.

The information received by participants is the same as that received by shareholders outside the qualified plan

There are few complaints when an employer's market value is roaring. Participants struggle with intentional investment selections and the rise in usage of target date funds and managed accounts suggests participant comfort in delegating allocation decisions. Participants (and many others) are prone to behavioral biases and mistakes that may cloud prudence in allocation to employer stock. "Everyone thinks their baby – and their business – is more beautiful than all the others, no matter how statistically impossible that is." *(Crosby, 2018, p. 72)* Thus, over-allocation to employer stock can result when education is insufficient.

When employer stock is included in a qualified plan, extra attention should be paid by educators to the importance of diversification. Educators should not show any greater bias, excitement or emphasis for the employer stock. Though not always as overt as the Enron example that begins this column, even subtle messaging (such as the fear of missing out) to purchase employer stock can be impactful for participants often looking for direction and guidance.

ERISA §404(c) requires that participants receive quarterly statements that include "a statement of the risk that holding more than 20 percent of a portfolio in the security of one entity (such as employer securities) may not be adequately diversified." *(Turley, 2017)* Yet, participants may not comprehend the risk they face, as "our brains are the most metabolically inefficient part of our body and one way we conserve energy is by going with the familiar." *(Crosby, 2018, p. 67)* Thus, the "devil we know" option is less mentally taxing than deciding on a new avenue.

All voting rights, tender offers and related rights have been distributed to the participant

These rights must include confidentiality and protection for participants in the form of procedures regarding participant actions with regard to employer stock. Proper procedures should be well-documented

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and given to participants. Participants should feel no unspoken pressure or influence to retain employer stock based on feelings their employer is watching their investment decisions.

An independent fiduciary has been assigned to ensure lack of employer influence

Influence from an employer is a main concern for regulators who appreciate a participant may feel compelled or pressured to maintain employer stock out of fear. Thus, a fiduciary must be assigned – whether in-house or independent – who is accountable for ensuring confidentiality of participant investments and no undue influence from an employer.

CREATE A DILIGENT PROCESS

"Simply relying on the plan's ERISA §404(c) language is not enough; there should be dedicated plan provisions devoted to the employer stock." *(Henson, 2013)* Just as with all investments within a qualified plan, plan sponsors should consider a process for evaluation of employer stock. The process should include documentation of not only the process but also how and why decisions were determined. Documentation is key under ERISA for demonstrating that a plan fiduciary took care to reasonably discharge his or her fiduciary duties with respect to the plan. *(Taylor, 2017)* Without documentation, proof can be difficult to ascertain.

Ultimately, "the propriety of including employer stock in a plan's investment menu ultimately can depend on the unique character of that plan's population, as well as the diligence and documentation of that plan's decision-makers." *(Turley, 2017)* Care and prudence should be taken when choosing to include the equity of an employer within a participant's qualified plan. Knowledge of participants' behavioral traits, regulatory and fiduciary concerns, and prudence of including the equity as an investment alternative are all considerations that can advise the process.

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BY CRAIG P. HOFFMAN

Looking Back at 10 Years of ASPPA GAC

Our opinions matter and this is a direct result of the efforts of the ASPPA members and their dedication to our government affairs mission.

As many of you may have heard, after 10 years, I am retiring from my role as General Counsel for the American Retirement Association, effective March 31, 2019. As you may have also heard, I will be leaving GAC in good hands, as Will Hansen has come on board as ARA's Chief Government Affairs Officer and Allison Wielobob will take over the General Counsel role. And I am not completely riding off into the sunset – I will become "Of Counsel" to the Trucker Huss law firm and plan to stay involved with GAC as a volunteer ASPPA member.

Since this will be my last GAC Update column for *Plan Consultant*, I wanted to begin by talking about the volunteer members of ASPPA GAC. Without question, the successes that ASPPA GAC has enjoyed over the years are a direct result of the hard work and efforts of the GAC volunteers. Their knowledge and expertise with regard to tax and ERISA matters is recognized and respected by the government regulators with whom we interact.

The IRS, DOL and PBGC don't always agree with our positions, but they realize that the real world experience of our members is invaluable as they formulate policy. On numerous occasions, I have been contacted by a government official with a request that ASPPA provide comments on a proposed regulation, revenue procedure or similar piece of guidance. Our opinions matter and this is a direct result of the efforts of the ASPPA members and their dedication to our government affairs mission.

I particularly want to mention the work done by the GAC committee leadership. I have had the pleasure of working with a succession of very talented GAC co-chairs and sub-committee chairs who have all made my job much easier. Similarly, I have worked with 10 different ASPPA Presidents and Boards of Directors, all of whom cared deeply about and supported GAC and our mission. There are so many people that I need to thank, to try to list them all would invariably result in someone being missed. So thank you to the collective group! I have really appreciated your help and counsel.

During my tenure, GAC has dealt with quite a few interesting and significant regulatory initiatives. Following are a few of my favorites.

FORM 5500

There were several IRS and DOL initiatives with regard to the Form 5500 that drew the interest of ASPPA GAC. Perhaps the most controversial related

"The successes that ASPPA GAC has enjoyed over the years are a direct result of the hard work and efforts of the GAC volunteers."

to the questions that were proposed to be added in 2015 as part of the Form 5500-SUP. The new questions were released with little advance notice and mandated that the name and address of the return preparer be included on the 5500 rather than being a voluntary disclosure. Our members objected to the timing as well as the fact that Form 5500 data is public and could be "mined" for a list of clients based on the preparer disclosure. Thanks to our advocacy efforts, particularly with officials at the Office of Management and Budget, the questions were delayed and ultimately dropped. However, like a bad dream, they may be back, so ASPPA GAC will need to continue to monitor this initiative and remain vigilant.

FUNDING QNECS THROUGH FORFEITURES

The latest iteration of 401(k) regulations were finalized late in 2004. Approximately 8 years later, the IRS issued so-called LRM master language for pre-approved plans that prohibited using forfeitures to fund safe harbor contributions. The IRS position was based on a very narrow reading of the 2004 regulatory language that required safe harbor contributions to be fully vested "when contributed to the plan." This interpretation of the regulation was contradictory to the actual language in the Internal Revenue Code. ASPPA GAC objected to this new interpretation. We submitted several comment letters and regularly raised the issue with the IRS. It took some time, but in 2017, the IRS revised the regulations to conform to the wording in the Internal Revenue Code to correct the error. ASPPA GAC's efforts were directly responsible for this change.

INVESTMENT DISCLOSURES

Beginning in 2009, the DOL embarked on the three-part project to give plan sponsors, plan participants and the DOL better and more transparent information with regard to the fees being paid by retirement plans. The results are the expanded disclosures on Schedule C to Form 5500, the service provider disclosures required under ERISA section 408(b)(2) and the participant level disclosures under the ERISA section 404(a) regulations. ASPPA GAC provided a great deal of input to DOL at every step along way.

CROSS-TESTING PROPOSED REGULATIONS

Much to the surprise of just about everyone, in January 2016 the IRS proposed a significant change to the cross-testing rules in conjunction with a proposed regulation providing relief for frozen defined benefit plans. The proposal would have added a subjective "reasonable classification" component to the testing process that would have significantly and detrimentally affected small business cross-tested designs. Thanks to ASPPA GAC's advocacy efforts, the IRS withdrew the proposal 4 months later.

SELF-CORRECTION UNDER THE DOL VOLUNTARY FIDUCIARY CORRECTION PROGRAM (VFCP)

This project began soon after I joined ASPPA as a staff member and continues to this day. It is focused on adding to VFCP a self-correction component for the late deposit of elective deferrals or loan repayments. This type of fiduciary breach can be self-corrected today but the "lost earnings" component of the correction procedure must be done by calculating the actual lost earnings rather than using the DOL's "online calculator." Our dialogue with DOL on this topic continues and the most recent DOL guidance plan includes a project to update to VFCP. I believe self-correction under VFCP will eventually come to pass and my only regret is that it has taken so long.

I close by thanking Brian Graff for the opportunity he gave me 10 years ago to come to work for ASPPA. I have greatly enjoyed my time here and remain dedicated to our mission of improving the private retirement system. PC

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

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