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ACTUARIAL RESOURCES, LLC

PLAN SPONSOR QUARTERLY UPDATE
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THIS MONTH'S HOT TOPIC

IRS Launches Pre-Audit Correction Program

by Kelsey Mayo
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Kelsey's practice is focused in the areas of Employee Benefits and Executive Compensation. She works with business owners and HR executives to understand and manage employee benefits and executive compensation arrangements. She routinely represents clients before the Internal Revenue Service, Department of Labor, and Pension Benefit Guarantee Corporation and has extensive experience in virtually all aspects of employee benefit plans and executive compensation arrangements.

Great news for plan sponsors! Effective June 2022, the IRS is launching a pilot program that will allow plan sponsors a chance to avoid costly audit sanctions. The program allows plan sponsors to find and correct plan errors in advance of an IRS audit. As outlined in the June 3, 2022 IRS announcement, the pilot program should work something like this:

- The IRS will send the plan sponsor a letter that it was selected for examination and give the employer 90 days to conduct a self-audit. The letter will identify one or more areas that the IRS is focused on (including specific review procedures for that issue) and also direct the sponsor to review other plan documentation and operations to find plan compliance issues.

- If a plan sponsor finds an error, it may correct the error using principles set forth in the IRS Employee Plans Compliance Resolution System (EPCRS).
  - o If the error is eligible for self-correction under EPCRS, the plan sponsor can correct in the 90-day period and then submit documentation of the error and the correction to the IRS.

  - o If the error cannot be self-corrected, the plan sponsor may disclose the error and ask to correct using a closing agreement. The IRS will assess a sanction in this case, BUT unlike in the past when these errors would generate large sanctions, if the only errors discovered are those self-identified by the sponsor, the IRS will assess a sanction equal to the much lower VCP correction fee. Under the current structure, the highest potential VCP fee is $3,500 (determined based on the amount of assets in a plan).

- Regardless of whether an error is discovered, the plan sponsor will respond to the IRS within 90 days and provide information regarding the issue identified and its other review procedures.
  - o The IRS will open an audit for any plan sponsor who does not respond during the 90-day period.

- The IRS will review the documentation submitted and can choose to: (1) close the examination, (2) conduct a limited-scope audit, or (3) open a full-scope audit of the plan.

The pilot program is designed to reduce the burdens of IRS examinations and encourage plan corrections and compliance.

If you receive a letter from the IRS, contact your TPA and ERISA attorney as soon as possible. The 90-day review period will pass very quickly, so time is of the essence—you'll want to use every day possible to review the plan and respond to ensure you avoid a broader audit and, if needed, take advantage of the correction opportunities. Your plan partners are here to help, so reach out quickly!

WHAT'S NEW IN WASHINGTON, D.C.

House Passes and Senate Debates SECURE 2.0

by Kelsey Mayo
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On May 26th, the Senate Health, Education, Labor and Pension (HELP) Committee circulated a discussion draft of the RISE and SHINE Act. This followed the House of Representatives' passage of H.R. 2954, the Securing a Strong Retirement Act of 2022 ("SSRA"). These are commonly thought of as competing versions of "SECURE 2.0".

Both Acts (if adopted in their current forms) would have wide-ranging impacts on the retirement industry. The following provisions are in both Acts:

- **Reduce the service prerequisite for long-term part-time employees.** The SECURE Act requires that long-term part-time employees—those who work at least 500 hours in three consecutive years—be permitted to defer to the 401(k) plan (generally beginning in 2024). Both Acts would reduce this to two years—SSRA beginning in 2023; RISE and SHINE beginning in 2024.
- **Unenrolled Participants.** Plans would be able to provide fewer notices to employees who elect not to participate.
- **Cashout Limit.** Mandatory cashout limit would be increased from $5,000 to $7,000. SSRA beginning in 2023; RISE and SHINE beginning in 2024.
- **Limit Overpayment Recovery.** Would change the rules relating to recovery of overpayments (preventing recovery in many instances).

The RISE and SHINE Act also includes the following provisions that SSRA does not contain:

- **Emergency Savings Feature.** Would allow plan sponsors to offer an "emergency savings account" feature in the 401(k) plan. The ESA account would be limited to $2500 and permit immediate distributions not subject to the 10% penalty if a number of requirements are satisfied.
- **QACA and EACA Re-enrollment**. Any plan that adds a qualified automatic contribution arrangement (QACA) safe harbor or an eligible automatic contribution arrangement (EACA) design after 2024 would be required to re-enroll participants who opt out of participation at least once every three years.
- **Certain Design Expenses Payable from Plan.** Plans would be allowed to pay "incidental expenses solely for the benefit of the participants and their beneficiaries" from plan assets. Examples of such expenses could include cost of amendments, enhancing a match or employer contribution.
- **Pension Plan Modifications.**
  - o New notice requirements and reporting to both DOL and PBGC when a pension plan offers a lump sum window.
  - o Change the content of the required pension plan annual funding notice, including revisions to require demographic information, average return on plan assets, and information on interaction of plan funding and PBGC guarantee amounts.
  - o Revise non-discrimination testing for cash balance plans to make variable rates more administrable.
  - o Eliminate indexing of the PBGC variable rate premium, creating a static $48 rate.
  - o Extending the permissive transfer of excess assets to a retiree health account.

The SSRA contains provisions that RISE and SHINE does not contain, including the following:

- **Increase the RMD age.** The SECURE Act increased the RMD age to 72. SSRA would increase the RMD age to 73 in 2023; age 74 in 2030; and age 75 in 2033.
- **Boosting small plan tax credits:** Currently, sponsors of small plans can claim a tax credit equal to 50% of plan startup costs, capped at $250 per non-highly compensated employee (but with a minimum of $500 and a maximum of $5,000) for three years. SSRA would raise the credit to 100% of startup costs (with the same min and max), but only for employers with up to 50 employees. In addition, certain sponsors of small plans could claim a tax credit, up to $1,000 per employee, for providing employer contributions to non-highly compensated employees for up to five years.

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WHAT'S NEW IN WASHINGTON, D.C.

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- **Change catch-up provisions.** Beginning in 2023, all catch-up contributions would have to be made on a Roth basis. Beginning in 2024, the catch-up contribution limit would be increased to $10,000 (indexed after 2024), but only for the 3 years in which a participant attains age 62, 63, and 64. (In 2022, the indexed catch-up limit is $6,500).

- **Permit treatment of student loan payments as deferrals for matching contributions.** Employers would be permitted to treat an employee's student loan payment as an elective deferral for purposes of determining employer matching contributions beginning in 2023. Currently loan payments can be matched by a plan, but this changes the treatment for nondiscrimination testing.

- **Update in-service withdrawals.** Plan sponsors would be expressly allowed to rely on an employee's certification that he or she meets the hardship distribution requirements (essentially a codification of current IRS guidance). SSRA also would permit penalty-free withdrawals for victims of domestic abuse and would limit repayment of birth or adoption distributions to the three-year period following distribution.

- **Expand IRS's EPCRS program** The bill would expand the self-correction program making it nearly always available to correct plan errors.

- **Establish online lost and found database for pension benefits.** DOL would be required to create a national database of employee benefit amounts to allow employees to track benefits across employers (and to aid employers in finding lost participants) and plans would have a new reporting obligation for plan years beginning at least two years after enactment.

- **Incentives.** Employers would be allowed to provide small financial incentives to participants to encourage participation in a 401(k) plan.

- **Permit treatment of employer matching contributions as Roth.** SSRA would permit employers to offer employer matching contributions on a Roth basis. (Currently, matching contributions must be pre-tax only, although the plan could then offer a Roth conversion.)

- **Requiring that new plans have auto-enrollment.** SSRA would require most new defined contribution plans to contain automatic enrollment and automatic deferral escalation features.

No action is required at this time because SECURE 2.0 is not yet law. The final version, if passed, is likely to be some combination of the two bills and might include a few extra provisions to boot! While it will change, now is still a great time to familiarize yourself with the provisions. You may also want to broach plan design issues (such as Roth features and part-time employees) with your TPA and plan vendors now, as these provisions may take effect quickly if approved.

BEST PRACTICES FOR PLAN SPONSORS

Fiduciary Tune-Up

by Kelsey Mayo
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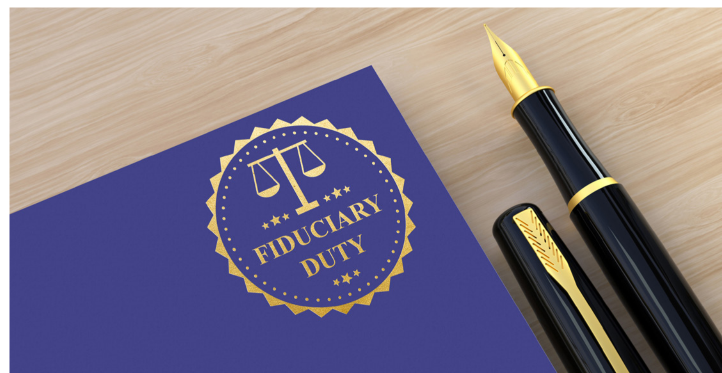

Much as it is a good idea to give cars and other vehicles regular inspections and maintenance, so too is it a good idea for plan fiduciaries to regularly review their fiduciary duties and assess attendant processes.

A "fiduciary" for retirement plan purposes generally is any person who has authority or control over the administration of a plan or its assets, including anyone who renders investment advice for a fee. The duties of an ERISA fiduciary are often thought of as the highest known to the law. Breaches of fiduciary duty can result in penalties ranging from civil penalties to jail time, and fiduciaries may be held personally liable for plan losses flowing from any such breach. Therefore, it is important for fiduciaries to regularly "tune up" their fiduciary processes, particularly as new guidance is issued.

Recently, several pieces of guidance on the ERISA fiduciary duty of prudence have been issued. First, the Supreme Court issued a decision in *Hughes v. Northwestern* University (142 S.Ct. 737 (2022)) that considered how the duty of prudence applies to a large investment lineup. The DOL then built on that decision in its guidance on how the duty of prudence applies to cryptocurrency.

The duty of prudence requires a fiduciary to act with the same care, skill, prudence, and diligence that a prudent person familiar with these matters would use under the circumstances. In the context of investment selection, this requires that fiduciaries exercise prudence in selecting, monitoring, and removing investment options. This duty to select and monitor investments was the focus of the Supreme Court's analysis in *Hughes*.

Overall, the opinion's biggest takeaway is one unsurprising to those in the retirement plan space: *all* investment options must be prudent. The inclusion of prudent investment options does not excuse the inclusion of imprudent ones. Said another way—fiduciaries should never consider themselves "off the hook" for a bad investment option just because there are good investment options that a participant could have chosen instead. As we discussed last quarter, the Department of Labor then, citing that opinion, provided specific guidance on how they believe the duty of prudence applies to cryptocurrency.

So, how might a plan sponsor put this new guidance into practice and ensure it is incorporated into your plan's prudent processes? A few starting points:

- Hold regular fiduciary training for all plan fiduciaries, to ensure all fully understand their duties and are brought up to date on any new guidance.
- Ensure any investment policy statement you have adopted still accurately reflects your policies and practices (we recommend these not be too detailed to avoid inconsistencies).
- Discuss the process for reviewing investments with your investment advisor or manager and inquire how their recommendations or processes comply with the new guidance and whether they are making any changes in light of the guidance. Keep in mind that *all* fund options must be prudent, each fund must be evaluated independently, and special attention should be given to brokerage windows if cryptocurrency is available.
- Document this review and inquiry to ensure it is clear that you are monitoring your investment fiduciary.
- Ensure you document compliance with plan processes to show procedural prudence. This can include documentation of: (1) plan administration and management activities, such as minutes of meetings and discussions; (2) advice received from experts and advisors; (3) deliberations based on the advice received; and (4) actions taken.

The immensity of ERISA fiduciary duties can be overwhelming, but careful action and planning now can help maintain and document good fiduciary process. Discuss your fiduciary process in light of this recent guidance with your internal fiduciaries and external plan vendors to ensure you stay on the path to compliance.