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Fiduciary Tool Kit for Compliance: Common Errors in Qualified and Nonqualified Retirement Plan Administration

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Fiduciary Tool Kit for Compliance: Common Errors in Qualified and Nonqualified Retirement Plan Administration



BY SUSAN E. BERNSTEIN, MARK E. BROSSMAN
AND HUGH A. MALLON III

The Investment Company Institute reported that U.S. retirement plan assets reached \$21.7 trillion as of Sept. 30, 2013, which represents 34 percent of all household financial assets in the U.S.¹ The Department of Labor reported in June 2013 that 88.7 million Americans have defined contribution plan accounts,

¹ See http://www.ici.org/research/stats/retirement/ret_13_q3

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based on data from 2011 annual reports.² With so many millions of people depending on these plans for retirement security, the government has placed significant legal requirements on the role of fiduciaries. Employers that sponsor retirement plans are being put under an increasingly high degree of scrutiny for their actions and inactions with respect to the qualified and nonqualified plans that they sponsor.

Plan sponsors are subject to fiduciary standards, but do not always understand their role and obligations as a fiduciary. To comply with the plethora of duties and requirements governing plans, plan sponsors must understand their role as a fiduciary, identify plan errors and resolve those errors to reduce risks of noncompliance and exposure to fiduciary liability and penalties.

Who Is a Fiduciary?

Generally anyone with discretionary authority or control over the management of a plan, the administration of a plan or investment of the plan's assets will be a fiduciary. A plan must have at least one fiduciary (a person or entity) named in the written plan, or through a process described in the plan, as having control over the plan's operation. The named fiduciary can be identified by office or by name. For some plans, it may be an administrative committee or a board of trustees. An individual can become a fiduciary even if he or she is not named a fiduciary in the plan documents. Some people may be fiduciaries based on their role with the plan. This will usually include, but is not limited to,

² <http://www.dol.gov/ebsa/pdf/2011pensionplanbulletin.pdf> (page 64).

trustees and individuals who have discretionary control over certain aspects of the plan, investment advisers to the plan and members of a plan's administrative committee (if one is established). Many actions involved in operating a plan make the person or entity performing such actions a fiduciary, to the extent discretion is used. Thus, fiduciary status is based on the functions performed for the plan, not just a person's title.

Fiduciary Duties. Fiduciaries have important responsibilities and are subject to standards of conduct because they act on behalf of participants in a retirement plan and their beneficiaries. The standards of conduct for fiduciaries are provided by the primary law governing the administration of retirement plans—the Employee Retirement Income Security Act, enacted in 1974 and enforced by the DOL.

The duties of plan sponsors and their fiduciaries are numerous and complex. It is nearly impossible to spell out all of the relevant rules, and plan sponsors usually need assistance to ensure compliance. Yet failure to comply with ERISA rules can result in penalties, government audits and even personal liability. With careful attention to legal requirements, plan sponsors should avoid liability and develop a road map to compliance. Among the most significant duties that a fiduciary has to follow are:

- A duty to act solely in the interests of all participants and beneficiaries (the exclusive benefit rule).
- A duty to act with the care, skill, prudence and diligence under the circumstances that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aim (the prudent expert rule).
- A duty to diversify the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so (the diversification rule).
- A duty to follow the plan documents unless inconsistent with ERISA.
- A duty to prudently select and monitor service providers.
- A duty to pay only reasonable plan expenses.

Delegation of Duties

It is very important that the governing board of trustees or directors of the plan sponsor understand that if it delegates duties to a person or entity, the board will maintain residual fiduciary responsibility. Fiduciary appointments might include an investment adviser and any board committees that have discretionary authority to manage the plan or its assets. If a plan committee is appointed, the individual committee members are fiduciaries and must perform their duties under ERISA fiduciary standards.

Delegating fiduciary responsibility and deciding whether to continue an existing delegation are themselves fiduciary functions subject to ERISA. Not only does this mean that a named fiduciary must satisfy ERISA's prudence and exclusive-benefit requirements when it delegates its fiduciary responsibilities to third parties—it also means that the named fiduciary is responsible for oversight of the third party's performance.

A named fiduciary's failure to monitor a third party's performance and, if appropriate, terminate the delegation, is a breach of its fiduciary responsibilities and could result in co-fiduciary liability for enabling a fiduciary breach or for failing to try to remedy such a breach when the named fiduciary knew or should have known that a breach had occurred.

Penalties

Plan sponsors should assess their compliance with the plethora of requirements that govern the plans that they maintain to minimize their exposure to fiduciary liability and Internal Revenue Service violations and penalties. Ignorance, good faith on the part of the fiduciary or lack of harm to the plan are not defenses to a violation of ERISA. If a plan sponsor identifies a failure, it can take action to correct the failure and thereby minimize the exposure it might otherwise have.

A fiduciary who fails to follow its duties may be held personally liable to restore any losses to the plan incurred from a breach of fiduciary duty. Fiduciaries are liable for legal and professional fees for defending a breach. The DOL can assess civil penalties, and criminal sanctions can be applied for willful violations. In addition, a participant or beneficiary can bring a civil action against a plan fiduciary. Noncompliance can also result in fines and tax liabilities if certain plan qualification rules are not met. If a qualified plan becomes disqualified, all vested benefits become subject to immediate taxation.

Tools for Compliance

The fiduciary provisions of ERISA impose a legal maze within which a fiduciary must operate. To ensure compliance with these substantial provisions, fiduciaries should acquaint themselves with the legal requirements and familiarize themselves with changes in the law and new developments. Fiduciaries should never hesitate to ask questions of plan administrators, other trustees or service providers, such as attorneys, accountants, actuaries, etc. Fiduciaries should attend seminars, which concentrate on aspects of trustee responsibilities and read periodicals and major publications focusing on fiduciary issues. Plan sponsors can also keep abreast of important developments through their professionals, including trust administrators, service providers and other trustees.

Finally, fiduciaries should take an active interest in the administration of the plan. Many different situations can affect a plan. Rather than sitting back and waiting for the consequences of events to unfold, fiduciaries should proactively influence the outcome by becoming knowledgeable of an issue, evaluating how the issue will affect the plan, and using knowledge and evaluation to take appropriate action.

Several trends have focused increased attention on the role of retirement plan sponsors and fiduciary obligations. These trends include continued volatility in the investment markets, allegations of misconduct in the mutual fund industry, greater scrutiny from government regulators and more instances of litigation by employees against employers. As a result, many plan sponsors are taking a closer look at their fundamental fiduciary responsibilities and taking steps to ensure compliance.

There are a number of ways for a fiduciary to minimize his or her potential liability. In this regard, employers and plan sponsors should:

- Identify plan fiduciaries and make sure they are clear about the extent of their responsibilities.
- Have fiduciaries acknowledge their status, duties and responsibilities in writing and sign a conflict-of-interest policy.
- Educate fiduciaries and conduct training on fiduciary duties and responsibilities.
- Establish a retirement plan committee and consider adopting a committee charter to define responsibilities.
- Document fiduciary decisions made and maintain thorough and prudent governance processes.
- Hold fiduciary meetings at least quarterly and retain minutes of meetings to demonstrate that it has engaged in a prudent governance process.
- Adopt an investment policy statement and review it annually.
- Hire qualified and independent investment service providers.
- Consider shifting investment responsibilities to the individual participants by allowing them to make their own investment decisions in accordance with Section 404(c) of ERISA.
- Retain legal counsel to review plan for compliance issues and voluntarily correct any failures identified.
- Benchmark fees and expenses paid by the plan to ensure reasonableness.
- Continue to monitor service providers.
- Maintain audit preparedness.
- Purchase an ERISA fidelity bond from a surety company in the name of the plan to protect the plan against theft of assets.
- Purchase fiduciary liability insurance or review existing policies and exclusions to ensure proper coverage and make sure that all of the fiduciaries are properly named as insureds. Standard directors and officers liability insurance does not typically cover claims for actions of ERISA plan fiduciaries.
- Review the plan documents with legal counsel.
- Establish internal controls and procedures to ensure plan compliance. For example, compare salary deferral election forms with actual amounts deducted from employees' paychecks. Verify marital status before making distributions. Ensure that participants over age 70 received their minimum required distributions.
- Review the included charts identifying common errors and take immediate action to resolve them. Never wait until the error is identified on audit by the IRS or examination by the DOL when the cost of correction will be more severe.



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Source: Checklists: Pensions & Retirement > Common Errors and Fixes for 403(b) Plans: Checklist

Common Errors and Fixes for 403(b) Plans: Checklist

Susan E. Bernstein, special counsel, Schulte Roth & Zabel LLP, Mark E. Brossman, partner, Schulte Roth & Zabel LLP and Hugh A. Mallon III, president and chief executive officer, Executive Compensation Concepts Ltd., contributed this chart.

The following chart identifies common Section 403(b) plan errors and what employers and plan sponsors should do to maintain compliance with applicable law. The best practice is to monitor plan compliance with internal controls to avoid mistakes from occurring in the first place. But, if the plan sponsor identifies an error, the mistake should be fixed as soon as feasible because the cost to correct an error that is identified on audit by the Internal Revenue Service or examination by the Department of Labor will be more severe.

403(b) Chart (printable)

Qualified 403(b) Retirement Plan

The following items are common elements of qualified tax code Section 403(b) retirement plans, where errors frequently occur. For each item, guidance on how to resolve the issue is provided.

Compliance With Adopting Plan Document and Required Amendments	
Issue	Resolution
Failure to timely adopt the plan document or legally required amendments.	Adopt the plan or amendment retroactively and file a correction with the Internal Revenue Service through its Voluntary Correction Program.
Compliance With Provisions in Plan Document, Including Adoption Agreement	
Issue	Resolution
Failure to follow the terms of the qualified 403(b) retirement plan or adoption agreement and monitor the plan's annual operation based upon the terms of the plan document and adoption agreement.	Create a master checklist and process to assure key provisions are reviewed regularly and that the plan's operations match the terms in the plan document. Read and understand the terms of your plan documents. Also, if there are changes to the plan, it is important that all of the plan's service providers are notified.
Definition of Compensation—Eligible Wages and Exclusions	
Issue	Resolution
Failure to properly define compensation that is used. For example, selecting W-2 wages, which include taxable fringe benefits, but not taking into account elements that are excluded in operation.	Identify what is included and excluded from eligible wages and properly define the exclusions in the plan document for determining benefits under the qualified retirement plan (i.e., are stipends, bonuses and overtime included in the definition of compensation). Severance pay should be excluded from eligible wages. The plan definition and payroll procedures need to match.
Definition of Plan Year	
Issue	Resolution
Failure to confirm that the plan is administered utilizing the correct plan year (i.e., calendar or fiscal) and application of the appropriate annual IRS contribution limitations.	Recognize that there are differences in annual IRS limitations depending on whether the plan year is based upon a calendar year or fiscal year. The annual tax code limitations for a fiscal year plan are based upon the calendar year limitations as of the first day of the qualified plan year (i.e., July 1).
Employer Contributions	
Issue	Resolution
Failure to make contributions when the plan document requires nonelective contributions.	Understand the difference between elective contributions and discretionary contributions, which can be decided on an annual basis by the plan sponsor.
Contribution Limitations	
Issue	Resolution
Failure to limit elective deferrals and/or employer contributions as defined in the following IRS limitations: <ul style="list-style-type: none"> √ Eligible compensation (tax code Section 401(a)(17)(A)). √ Section 402(g)(B) limit. √ Maximum addition by employer and employee (tax code Section 415(c)(1)(a)). 	Create procedures to monitor that limits are not exceeded and that refunds are made where necessary prior to April 15. Maintain a checklist and confirm that the payroll provider/system maintains the correct plan year limits: <ul style="list-style-type: none"> √ Eligible compensation (tax code Section 401(a)(17)(A)) (i.e., \$260,000 in 2014).

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Qualified 403(b) Retirement Plan—Continued

Contribution Limitations—Continued	
Issue	Resolution
<ul style="list-style-type: none"> √ Impact of age 50+ catch-up contributions. √ 15 year of service catch-up contribution (tax code Section 414(v)). √ "ACP" test impact—the average compensation percentage test limitation of employer matching contributions (tax code Section 401(m)). 	<ul style="list-style-type: none"> √ Section 402(g)(B) limit (i.e., \$17,500 in 2014). √ Maximum addition by employer and employee (tax code Section 415(c)(1)(a)) (i.e., \$52,000 plus Age 50 catch-up contributions \$5,500 in 2014). √ 15 year of service catch-up contribution (Section 414(v)) (this often overlooked special contribution type allows up to an overall increase of \$15,000. Check with plan administrator to determine if a participant has unused elective deferral credits—\$3,000 for each of five years). √ The ACP test limits the annual elective deferrals by highly-compensated employee's (HCE's) that are eligible for the employer match. The plan must satisfy one of the following tests: <ul style="list-style-type: none"> a. The ACP for a plan year for participants who are HCE's for the plan year shall not exceed the prior year's ACP for plan participants who were non-highly compensated employee's (NHCE's) for the prior plan year by 1.25; or b. The ACP for a plan year for participants who are HCE's for the plan year shall not exceed the prior year's ACP for plan participants who were NHCE's for the prior plan year multiplied by two, provided that the ACP for participants who were HCE's does not exceed the ACP for participants who were NHCE's in the prior plan year by more than two percentage points.

Fiduciary Committee	
Issue	Resolution
<p>Failure of employer to establish a committee within the governing board. Responsibilities could include, but are not limited to:</p> <ol style="list-style-type: none"> 1. Monitoring the plan investment decisions. 2. Developing an investment policy statement for the plan. 3. Reviewing the annual report on the status of the plan (i.e., pension audit and investment performance). 	<p>Create formal pension committee, duties and responsibilities to assure the plan is in compliance with the provisions of the plan, ERISA and IRS regulatory updates, etc. (If a committee is not appointed, (i) the employer or board of trustees by default will be the named fiduciary and this may include individuals who are not aware of their duties; (ii) the employer may not meet regularly to address its responsibilities whereas a named committee could be set up to meet each quarter to monitor and oversee its duties).</p>

Eligibility	
Issue	Resolution
<p>Failure to determine an employee's eligibility.</p>	<p>Create a master eligibility checklist based upon the date of hire and meeting 1,000-hours-per-year test. Be careful with misclassifying employees as "part time" when they work more than 20 hours per week.</p>

Universal Availability	
Issue	Resolution
<p>Failure to notify employees of their eligibility to participate in the contributory component of the plan.</p>	<p>Ensure all eligible employees have been identified and provided a meaningful notice each year of their opportunity to make deferrals. For any improperly excluded employees, the employer should make a corrective contribution to the plan for the missed deferral plus missed matching contributions and lost earnings.</p>

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Qualified 403(b) Retirement Plan—Continued

Mandatory Employee Contributions	
Issue	Resolution
Failure to treat employee contributions that are mandatory as a separate type of contribution. Mandatory contributions should not be treated as employee elective deferrals and should not count against a participant's Section 402(g)(B) annual limit of \$17,500 in 2014.	Create different payroll code for mandatory contributions and ensure that these contribution types are not counted when tracking the maximum employee elective deferrals for a plan year.
Loans	
Issue	Resolution
Failure to follow requirements of loan program and enforced repayment as required under tax code Section 72(p).	Create a checklist to determine that each participant meets the requirements of the loan program and the loan repayment is enforced to prescribe the repayment agreement. Understand that loans taken in the prior 12 months reduce the total amount of available for a loan. If there is more than one vendor, the totals must be coordinated.
Hardship Distribution	
Issue	Resolution
Failure to follow hardship criteria or to have adequate documentation ensuing hardship distributions until requirements are met.	Implement procedures to assure that the hardship requirements are met.
Timely Deposit of Employee Deferrals	
Issue	Resolution
Failure to remit employee deferrals into the plan on a timely basis. The Department of Labor requires that contributions be deposited as soon as possible (there is a seven-day safe harbor for small plans with fewer than 100 employees).	Change procedures to remit more quickly and correct late deposits by providing lost earnings (use the DOL online calculator to determine the amount of interest) and document corrective actions taken. Reconsider sweep accounts to authorize a sweep of transfers at a minimum of twice per month to ensure timely deposits.
Summary Plan Description	
Issue	Resolution
Failure of the summary plan description (SPD) to be consistent with the plan document and operations.	The SPD should be written to align with the plan document and plan operations. The SPD must be written so that the average plan participant can understand the terms. The plan sponsor must ensure actual receipt of the SPD by all participants within 90 days of their participation date. SPDs should generally be updated and redistributed every five years.
Summary of Material Modifications	
Issue	Resolution
Failure to distribute a summary of material modifications (SMM) when there is a plan amendment.	An SMM should be distributed to participants and beneficiaries to notify them of a change in the plan no later than 210 days after the plan year in which the plan amendment was adopted.
Summary Annual Report	
Issue	Resolution
Failure to distribute the summary annual report (SAR).	The SAR should be distributed to participants and beneficiaries within two months after the IRS Form 5500 is filed with the Department of Labor and the IRS.

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This chart was originally published in a BNA Insight, *Fiduciary Tool Kit for Compliance Common Errors in Qualified and Nonqualified Retirement Plan Administration*, 247 Pens. & Ben. Daily, Dec. 27, 2013 (247 PBD, 12/27/13).

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457(b) Chart (printable)

Nonqualified Section 457(b) Eligible Deferred Compensation Plan

Common elements of nonqualified tax code Section 457(b) eligible deferred compensation plans that frequently lead to compliance issues are listed below. For each item on the list, guidance on how to resolve the issue is provided.

Compliance With Agreement's Provisions and IRS Limitations	
Issue	Resolution
Failure to follow the provisions of nonqualified Section 457(b) eligible deferred compensation plan agreement.	Create a master checklist and process to assure key provisions are reviewed on a regular basis.
Eligibility	
Issue	Resolution
Failure of the governing board to adopt a resolution approving new participants' eligibility to participate in the plan.	Establish a process for enrolling newly eligible participants.
Top Hat Group	
Issue	Resolution
Failure to limit eligibility to a select group of management and highly compensated employees.	Establish a process for selecting top hat plan employees and annually confirm that participants remain eligible and that the top hat group remains selective.
Payroll Taxes	
Issue	Resolution
Failure to report the employer contribution on behalf of a participant for payroll taxes (i.e., FICA and Medicare).	The employer's contribution on behalf of a participant is a "compensation related transaction." While not eligible for federal, state or local taxes, as applicable; to the extent that all, or a prorated, share of the contribution is vested, the employer must report such amount as W-2 wages and collect payroll taxes.
Titling of 457(b) Plan	
Issue	Resolution
Failure to title the investment account in the name of the employer.	If the investment account is titled in the name of the individual plan's participants utilizing the participant's Social Security number, the account will violate the 457(b) regulations and could result in immediate taxation to the participant (unintended consequence). The account should be renamed and titled in the name of the employer as plan sponsor to avoid taxation to a plan participant.
Failure to Report 457(b) Plan on Financial Statement	
Issue	Resolution
Failure to report the assets and liabilities of deferrals and contributions into the 457(b) plan on the employer's financial statements.	<p>In many situations, the elective deferrals and/or employer contributions are automatically transferred (via a "sweep account") to the investment house and deposited into the participant's account. As a result of this automatic transfer, the employer often fails to report the asset and liability on its financial statements. All invested account balances of the respective plan participants must be reported on the employer's financial statement as an asset and liability to delay taxation by federal, state and/or local regulatory agencies.</p> <p>NOTE: Nonqualified 457(b) plans are generally self-directed and the employer should at the close of the calendar or fiscal year be "marked-to-market" to reflect the asset and liability due to the respective participants.</p>

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Nonqualified Section 457(b) Eligible Deferred Compensation Plan—Continued

Election Forms	
Issue	Resolution
Failure to provide appropriate election forms.	<p>Create and maintain in master participant file the following forms:</p> <ol style="list-style-type: none"> 1. Payment election form (e.g., initial and subsequent). 2. Compensation deferral election form (e.g., initial, subsequent and special catch-up election). 3. Beneficiary election form (i.e., initial and subsequent). 4. Deemed investment election form (i.e., initial and subsequent).
Filing With Department of Labor	
Issue	Resolution
Failure to file a top hat compliance statement with the Department of Labor.	<p>There is a <u>one-time notice</u> filing requirement in order for the plan to qualify for exemption from ERISA's reporting and disclosure, vesting, funding, participation and fiduciary responsibility requirements.</p> <p>The letter to the DOL should be filed within 120 days of the establishment/approval of the plan. A copy of the letter should be sent via registered mail/return receipt to the plan administrator.</p> <p>If the compliance statement was never filed, there is a DOL correction program that counsel can file for the plan.</p>
Distribution of 457(b) Plan	
Issue	Resolution
Failure to recognize that a distribution from a 457(b) plan is a W-2 transaction.	<p>The 457(b) plan's distribution at a triggering event (such as retirement, separation from service, death or disability) is a W-2 transaction. As a result, the distribution should not be made directly to the participant and instead should be run through the employer's payroll system. It is important to note that the employer is the party ("payer") responsible to collect federal, state and local taxes <u>only</u>. Note payroll taxes should have been deducted when the benefits became vested and do not need to be taxed again at distribution.</p>
Reporting on the IRS Form 990	
Issue	Resolution
Failure to report correctly on Form 990 and/or Schedule J elective and/or employer contributions on Form 990 Schedule J.	<p>Employers must report contributions to a Section 457(b) plan on IRS Form 990:</p> <ol style="list-style-type: none"> 1. IRS Form 990, Part VII—or those officers, directors, trustees, key employee, and/or highly compensated employees whose W-2 is \$100,000 or more, the tax-exempt filing organization must report certain compensation information (e.g. cash compensation and noncash qualified and nonqualified benefits, including, but not limited to deferrals, employer contributions and earnings thereon) received from the tax-exempt as well as related organizations (i.e., an organization including a nonprofit organization, stock corporation, partnership, or limited liability company, trust and governmental unit or entity).

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Nonqualified Section 457(b) Eligible Deferred Compensation Plan—Continued

Reporting on the IRS Form 990—Continued	
Issue	Resolution
	<p>2. IRS Form 990, Schedule J—Part II, Column “B” (iii)—Other Compensation for Officers, Directors, Trustees, Key Employees, and/or Highly Compensated Employees whose W-2 is \$150,000 or more, the tax-exempt filing organization must report certain compensation information (e.g., current year payments earned in prior years, payments under severance plans, payments as a result of change of control, deferred amounts and earnings or losses in nonqualified defined contribution plans subject to Section 457(f), which become substantially vested and awards based upon longevity of service) received from the tax-exempt as well as related organizations (i.e., an organization including a nonprofit organization, stock corporation, partnership, or limited liability company, trust and governmental unit or entity).</p>
Tax Code Section 409A Regulation	
Issue	Resolution
<p>Failure with respect to application of Section 409A.</p>	<p>If the employer believes that the 457(b) plan has to be written and operated in compliance with Section 409A when it does not, the employer may be creating restrictions and obstacles it does not need to have in place. Section 409A does not apply to a 457(b) plan under a statutory exception.</p>

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The following chart identifies common Section 457(f) plan errors and what employers and plan sponsors should do to maintain compliance with applicable law. The best practice is to monitor plan compliance with internal controls to avoid mistakes from occurring in the first place. But, if the plan sponsor identifies an error, the mistake should be fixed as soon as feasible because the cost to correct an error that is identified on audit by the Internal Revenue Service or examination by the Department of Labor will be more severe.

457(f) Chart (printable)

Nonqualified Section 457(f) Ineligible Supplemental Retirement Compensation Plan

The following list contains common elements of nonqualified Section 457(f) ineligible supplemental retirement compensation plans that frequently lead to compliance issues. For each item on the list, guidance on how to resolve the issue is provided.

Compliance With Agreement's Provisions and IRS Limitations	
Issue	Resolution
Failure to follow the provisions of the nonqualified Section 457(f) ineligible supplemental executive retirement plan operates according to the plan agreement or agreement in the participant employment agreement, as applicable.	Create a master checklist and process to assure key provisions are reviewed on a regular basis.
Eligibility	
Issue	Resolution
Failure of board to approve a resolution approving new participants' eligibility to participate in the plan.	Establish a process for enrolling newly eligible participants.
Top Hat Group	
Issue	Resolution
Failure to limit eligibility to a select group of management and highly compensated employees.	Establish a process for selecting top hat employees and annually confirm participants remain eligible and that the top hat group remains selective.
Substantial Risk of Forfeiture	
Issue	Resolution
Failure to recognize that once the employer contributions vest and the benefits are no longer subject to "substantial risk of forfeiture," the benefit is immediately taxable to the participant without any ability to correct, irrespective of whether the benefit is distributed to the employee or retained in the plan.	Monitor the vesting schedule to comply with the plan document and IRS requirements for a substantial risk of forfeiture.
Titling of the 457(f) Plan	
Issue	Resolution
Failure to title the investment account in the name of the employer.	If the investment account is titled in the name of the individual plan's participants utilizing the participant's Social Security number, the account will violate the 457(f) regulations and could result in immediate taxation to the participant (unintended consequence). The account should be renamed and titled in the name of the employer as plan sponsor to avoid taxation to a plan participant.
Failure to Report 457(f) Plan on Financial Statement	
Issue	Resolution
Failure to report the assets and liabilities of deferrals and contributions into the 457(b) plan on the employer's financial statements.	<p>In many situations, the elective deferrals and/or employer contributions are automatically transferred (via a "sweep account") to the investment house and deposited into the participant's account. As a result of this automatic transfer, the employer often fails to report the asset and liability on its financial statements.</p> <p>All invested account balances of the respective plan participants must be reported on the employer's financial statement as an asset and liability.</p> <p>NOTE: Nonqualified 457(f) plans are self-directed, and the employer should at the close of the calendar or fiscal year be "marked-to-market" to reflect the asset and liability due to the respective participants.</p>

A BNA Graphic/pn351g7

Non-Qualified Section 457(f) Ineligible Supplemental Retirement Compensation Plan—Continued

Election Forms	
Issue	Resolution
Failure to provide election form.	<p>Create and maintain in master participant file the following forms:</p> <ol style="list-style-type: none"> 1. Payment election form (e.g., initial and subsequent). 2. Compensation deferral election form (e.g., initial, subsequent and special catch-up election). 3. Beneficiary election form (i.e., initial and subsequent). 4. Deemed investment election form (i.e., initial and subsequent).
Filing With Department of Labor	
Issue	Resolution
Failure to file a top hat compliance statement with the Department of Labor.	<p>There is a <u>one-time notice</u> filing requirement in order for the plan to qualify for exemption from the vesting, funding, participation and fiduciary responsibility requirements.</p> <p>The letter to the DOL should be filed within 120 days of the establishment/approval of the plan. A copy of the letter should be sent via registered mail/return receipt to the plan administrator.</p> <p>If the compliance statement was never filed, there is a DOL correction program that counsel can file for the plan.</p>
Distribution of the 457(f) Plan	
Issue	Resolution
Failure to recognize that a distribution from a 457(f) plan is generally a W-2 transaction unless the benefit was taxed in an earlier year.	<p>The assets of the plan are general assets of the employer. As such, the distribution should not be made directly to the participant and instead should be run through the employer's payroll system. Important to note that the employer is the party ("payer") responsible to collect federal, state and local taxes only. Note payroll taxes should have been deducted when the benefits became vested and do not need to be taxed again at distribution.</p>
Reporting on the IRS Form 990	
Issue	Resolution
Failure to report correctly on Form 990 and/or Schedule J employer contributions on Form 990 Schedule J.	<p>Employer must report contributions to a Section 457(f) plan on IRS Form 990:</p> <ol style="list-style-type: none"> 1. IRS Form 990, Part VII—for those officers, directors, trustees, key employee, and/or highly compensated employees whose W-2 is \$100,000 or more, the tax-exempt filing organization must report certain compensation information (e.g. cash compensation and noncash qualified and nonqualified benefits, including, but not limited to deferrals, employer contributions and earnings thereon) received from the tax-exempt as well as related organizations (i.e., an organization including a nonprofit organization, stock corporation, partnership, or limited liability company, trust and governmental unit or entity).

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Non-Qualified Section 457(f) Ineligible Supplemental Retirement Compensation Plan—Continued

Reporting on the IRS Form 990—Continued	
Issue	Resolution
	2. IRS Form 990, Schedule J—Part II, Column “B” (iii)—Other Compensation for Officers, Directors, Trustees, Key Employees, and/or Highly Compensated Employees whose W-2 is \$150,000 or more, the tax-exempt filing organization must report certain compensation information (e.g., current year payments earned in prior years, payments under severance plans, payments as a result of change of control, deferred amounts and earnings or losses in nonqualified defined contribution plans subject to Section 457(f), which become substantially vested and awards based upon longevity of service) received from the tax-exempt as well as related organizations (i.e., an organization including a nonprofit organization, stock corporation, partnership, or limited liability company, trust and governmental unit or entity).
IRC 409A Regulation	
Issue	Resolution
Failure to comply with Section 409A along with Section 457(f) regulations.	Employer may have to comply with Section 409A unless the short-term deferral exception under 409A applies (which generally occurs when the benefits are paid within a short amount of time after the benefits become vested).

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Source: Checklists: Pensions & Retirement > Common Errors and Fixes for 401(k) Plans: Checklist

Common Errors and Fixes for 401(k) Plans: Checklist

Susan E. Bernstein, special counsel, Schulte Roth & Zabel LLP, Mark E. Brossman, partner, Schulte Roth & Zabel LLP and Hugh A. Mallon III, president and chief executive officer, Executive Compensation Concepts Ltd., contributed this chart.

The following chart identifies common Section 401(k) plan errors and what employers and plan sponsors should do to maintain compliance with applicable law. The best practice is to monitor plan compliance with internal controls to avoid mistakes from occurring in the first place. But, if the plan sponsor identifies an error, the mistake should be fixed as soon as feasible because the cost to correct an error that is identified on audit by the Internal Revenue Service or examination by the Department of Labor will be more severe.

401(k) Chart (printable)

Qualified 401(k) Retirement Plan

The following items are common elements of qualified 401(k) retirement plans where errors frequently occur.
For each item, guidance on how to resolve the issue is provided.

Compliance with Provisions in the Plan Document Including Adoption Agreement	
Issue	Resolution
Failure to follow the terms of the qualified 401(k) retirement plan or adoption agreement and monitor the plan's annual operation based upon the terms of the plan document and adoption agreement.	Create a master checklist and process to assure key provisions are reviewed regularly and that the plan's operations match the terms in the plan document. Read and understand the terms of your plan documents.

Definition of Compensation—Eligible Wages and Exclusions	
Issue	Resolution
Failure to properly define compensation that is used. For example, selecting W-2 Wages which includes taxable fringe benefits, but not taking into account elements that are excluded in operation.	Identify what is included and excluded from eligible wages and properly define the exclusions in the plan document for determining benefits under the qualified retirement plan (i.e., are stipends, bonuses and overtime included in the definition of compensation). Severance pay should be excluded from eligible wages. The plan definition and payroll procedures need to match.

Definition of Plan Year	
Issue	Resolution
Failure to confirm that the plan is administered utilizing the correct Plan Year (i.e., Calendar or Fiscal) and application of the appropriate annual IRS contribution limitations.	Recognize that there are differences in annual IRS limitations depending on whether the Plan Year is based upon a calendar year or fiscal year. The annual IRC limitations for a fiscal year plan are based upon the calendar year limitations as of the first day of the qualified plan year (i.e., July 1).

Employer Contributions	
Issue	Resolution
Failure to make contributions when the plan document requires non-discretionary contributions.	Understand the difference between non-discretionary and discretionary contributions, which can be decided on an annual basis by the Plan Sponsor.

Contribution Limitations	
Issue	Resolution
Failure to limit elective deferrals and/or employer contribution as defined in the following IRS limitations: ✓ Eligible Compensation (IRC § 401(a)(17)(A)) ✓ 402(g)(1)(B) Limit ✓ Maximum Addition by Employer and Employee Maximum Annual Addition by Employer and Employee Threshold (IRC § 415(c)(1)(a)) ✓ Impact of mandatory employee contribution ✓ Impact of Age 50+ Catch-up Contributions	Create procedures to monitor that limits are not exceeded and that refunds are made where necessary prior to April 15. Maintain a checklist and confirm that the payroll provider/system maintains the correct plan year limits: ✓ Eligible Compensation (IRC § 401(a)(17)(A)) (i.e., \$260,000 in 2014-indexed) ✓ 402(g) Limit (i.e. \$17,500 in 2014-indexed) ✓ Maximum Addition by Employer and Employee (IRC § 415(c)(1)(a)) (i.e., \$52,000 plus Age 50 Plus contribution of \$5,500 in 2014 - indexed)

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Qualified 401(k) Retirement Plan—Continued

Contribution Limitations—Continued	
Issue	Resolution
<p>√ "ADP" Non-Discrimination Test Impact – the Average Deferral Percentage Test limitation (IRC § 401(k)(3))</p>	<p>√ The ADP Non-Discrimination Test limits the annual elective deferrals by highly-compensated employee's (HCE's) that are eligible for the employer match. The Plan must satisfy one of the following tests:</p> <ol style="list-style-type: none"> a. The ADP for a plan year for participants who are HCE's for the Plan Year shall not exceed the prior year's ADP for Plan participants who were non-highly compensated employee's (NHCE's) for the prior Plan Year by 1.25; or b. The ADP for a plan year for participants who are highly HCE's for the plan year shall not exceed the prior year's ADP for Plan participants who were NHCE's for the prior Plan Year multiplied by 2, provided that the ADP for participants who were HCE's does not exceed the ADP for participants who were NHCE's in the prior Plan Year by more than 2 percentage points.
Fiduciary Committee	
Issue	Resolution
<p>Failure of employer to establish a Committee within the governing Board. Responsibilities could include, but are not limited to:</p> <ol style="list-style-type: none"> 1. Monitoring the plan investment decisions 2. Developing an Investment Policy Statement for the plan 3. Reviewing annual report on the status of plan (i.e., pension audit and investment performance) 	<p>Create formal pension committee, duties and responsibilities to assure the plan is in compliance with the provisions of the plan, ERISA and IRS regulatory updates, etc. If a committee is not appointed, (i) the employer or Board of Trustees by default will be the named fiduciary and this may include individuals who are not aware of their duties; (ii) the employer may not meet regularly to address its responsibilities whereas a named committee could be set up to meet each quarter to monitor and oversee its duties).</p>
Eligibility	
Issue	Resolution
<p>Failure to determine an employee's eligibility.</p>	<p>Create master eligibility checklist based upon date of hire and meeting 1,000 hours per year test. Be careful with misclassifying employees as "part-time" when they work more than 20 hours per week.</p>
Safe Harbor 401k notice	
Issue	Resolution
<p>Failure to provide 401k Safe Harbor Notice.</p>	<p>Implement new procedures to ensure that timely notice is provided. If any participant was prevented from making a timely informed election, then that participant needs to be made whole with a corrective contribution.</p>
Nondiscrimination	
Issue	Resolution
<p>Failure to pass the ADP nondiscrimination test.</p>	<p>Distribute excess deferrals within 12 months; reallocate as catch up contributions for participants over age 50; re-characterize as after-tax contributions if the plan allows; or make qualified non-elective contributions for the non-highly compensated employees to raise the ADP to the percentage necessary to pass the test.</p>

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Qualified 401(k) Retirement Plan—Continued

Excess Employer Contribution	
Issue	Resolution
Failure to limit employer contribution to the amount set forth in the plan.	Reduce the account balance of the affected participant by the excess allocation and adjust for earnings. Place the forfeited amount in an unallocated account and use that amount to reduce future employer contributions.
Loans	
Issue	Resolution
Failure to follow requirements of loan program and enforced repayment as required under IRC section 72(p).	Create a checklist to determine that each participant meets the requirements of the loan program and loan repayment is enforced to prescribe repayment agreement. Understand that loans taken in the prior 12 months reduce the total amount of available for loan. If there is more than one vendor, the totals must be coordinated.
Hardship Distribution	
Issue	Resolution
Failure to have adequate documentation ensuing that in-service and hardship distributions until requirements are met.	Implement procedures to assure that the all in-service and hardship requirements are met.
Timely Deposit of Employee Deferrals	
Issue	Resolution
Failure to remit employee deferrals into the Plan on a timely basis. The Department of Labor requires that contributions be deposited as soon as possible (there is a 7-day safe harbor for small plans with less than 100 employees).	Change procedures to remit more quickly and correct late deposits by providing lost earnings (use the DOL online calculator to determine amount of interest) and document corrective actions taken. Reconsider sweep accounts to authorize sweep of transfers at a minimum of twice per month to ensure timely deposits.
Summary Plan Description	
Issue	Resolution
Failure of the Summary Plan Description ("SPD") to be consistent with the plan document and operations.	The SPD should be written to align with the plan document and Plan operations. The SPD must be written so that the average plan participant can understand the terms. The Plan Sponsor must ensure actual receipt of the SPD by all participants within 90 days of their participation date. SPDs should generally be updated and re-distributed every five years.
Summary of Material Modifications	
Issue	Resolution
Failure to distribute a Summary of Material Modifications ("SMM") when there is a plan amendment.	An SMM should be distributed to participants and beneficiaries to notify them of a change in the plan no later than 210 days after the plan year in which the plan amendment was adopted.
Summary Annual Report	
Issue	Resolution
Failure to distribute the Summary Annual Report ("SAR").	The SAR should be distributed to participants and beneficiaries within two months after the IRS Form 5500 is filed with the Department of Labor and Internal Revenue Service.

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