THE 401(k) HANDBOOK

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New Ruling Provides Good Excuse to Review Anti-alienation Exceptions for Plan Assets

By Arris Reddick Murphy

Assets in a 401(k) plan are to be used exclusively to pay benefits to participants and to cover reasonable administrative expenses of the plan. As protection, Section 206(d) of ERISA contains a provision that provides that benefits under a qualified retirement plan may not be assigned or alienated. However, as with most rules, the anti-alienation provision has exceptions that may divert plan assets to purposes other than participant benefit payments. Therefore, plan sponsors and their administrators should be familiar with some of these instances.

In a recent court case that serves as a pertinent example, *U.S. v. Wilson,* No. 3:09-cr-00161-FDW-DCK (W.D.N.C., June 10, 2015), the Western District of North Carolina ordered a garnishment of plan assets for criminal restitution.

This column looks at the anti-alienation provision under ERISA and the exceptions that permit use of retirement plan assets for other purposes.

See *Murphy*, p. 2

DOL FAB Offers Guidance, Examples To Clarify Safe Harbor Annuity Selection

Confusion may lead defined contribution retirement plan sponsors or their advisers to overestimate or misunderstand the duration or extent of their fiduciary responsibilities when selecting a plan annuity provider, but the U.S. Department of Labor has provided some new guidance to add clarity.

In DOL Field Assistance Bulletin No. 2015-02, the agency reminds that choosing an annuity provider for DC plan benefit distributions for retirees and beneficiaries is a fiduciary function, subject to ERISA standards of prudence and loyalty. The agency said employers repeatedly have commented about the 2008 safe harbor regulation (29 CFR 2550.404a-4) designed to cover this service provider selection; they remain unclear about the scope of their fiduciary obligations related to annuity selection under DC plans.

In particular, DOL's Employee Benefits Security Administration said, questions continue to be raised about how to reconcile the "time of selection" standard in the rule, whose principle is that the prudence of a fiduciary decision is measured under ERISA based on information available at the time the decision was made.

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Facts of the Case

On April 21, 2011, Defendant Willard Edward Wilson was found guilty of conspiring to defraud the United States by facilitating a mortgage fraud scheme. Wilson was sentenced to 30 months in prison, two years' supervision and a $300 special assessment. On May 13, 2011, the court ordered restitution for fraud victims of $850,374 and amended the criminal judgment to reflect this restitution amount in December 2012.

In December 2013, the United States obtained a Writ of Continuing Garnishment against Wilson's assets in the United Brotherhood of Carpenters Pension Fund. On Feb. 4, 2014, the fund's counsel claimed in response that the defendant's pension benefits are exempt from garnishment under ERISA and the federal tax Code. So the government filed suit to recover the restitution. The issue before the court in the recent decision is whether the government may garnish Wilson's interest in his pension fund, despite ERISA's anti-alienation provision and the anti-alienation provision in the Section 401(a)(13) of the tax code.

Restitution for Criminal Act

Federal prosecutors argued that the Mandatory Victim Restitution Act of 1996 provides an exception to ERISA's anti-alienation provision when enforcing restitution against a criminal defendant. Also, they argued, the Federal Debt Collections Procedures Act of Code Section 3613 makes it clear that criminal fines are to be treated as if there were a liability for federal income taxes.

The rationale for these acts is that if delinquent taxpayers cannot protect their pension benefits, criminals owing a fine may not do so either. These exceptions essentially equate criminal fines with tax shortfalls, which may be paid from the participant's retirement plan assets.

In a private letter ruling, IRS said that the general anti-alienation rule under the federal tax Code does not preclude a court's garnishing the account balance of a participant's benefit in a qualified plan to collect a fine imposed in a federal criminal action.

It follows that in the *Wilson* case, the U.S. district court held that the Victim Restitution Act is an express statutory exception to the anti-alienation provision of ERISA, as well as the corresponding provision in the federal tax Code. Therefore, in order to enforce the criminal restitution order, the government was entitled to a writ of garnishment against Wilson's interest in the pension fund.

Anti-alienation Exceptions

In addition to allowing for criminal restitution payment in a federal government criminal case, the anti-alienation provisions under ERISA and the tax Code have a number of other exceptions:

- A participant may direct the plan to pay a benefit to a third party, such as a medical facility or a nursing home, if certain requirements are satisfied. For example, the participant may change the direction, and the third party acknowledges in writing that the participant has to agree to the arrangement.
- A federal tax charge can be exempted from anti-alienation rules. However, IRS has issued guidance confirming that a retirement plan does not have to honor an IRS levy for taxes to the extent that the taxpayer is not entitled to an immediate distribution of benefits from the plan. The item may be resubmitted at the time the participant is eligible for a distribution.
- A qualified domestic relations order, as described in Section 414(p) of the federal tax Code, can be exempted. A domestic relations order is a legal order, entered as part of a divorce or legal separation, that splits and changes ownership of a retirement plan to give an alternate payee all or part of the retirement plan assets. The alternate payee may be the divorced spouse or a child.

See *Murphy*, p. 11

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Value of Returned Contributions from Failed Nondiscrimination Tests Rose in Latest Year

A reminder that failed nondiscrimination tests can be costly: Returned elective 401(k) contributions from highly compensated employees mandated by these failed IRS tests rose in value in the latest annual study of this common defined contribution plan problem, even as the number of plans failing the tests declined.

Research by a retirement plan advisory firm on 2013 plan disclosures submitted to the U.S. Department of Labor, the latest complete set of annual filings available, found that 54,493 plans failed their tests of plan design fairness, down from nearly 60,000 in 2012 (see July 2014 story).

Tip Box

If the actual deferral percentage test is not satisfied, then amounts in excess of the permissible ADP for highly compensated executives are classified as "excess contributions," and must be returned to the HCEs.

But returning large amounts of excess contributions to HCEs from testing failures costs plan sponsors and their recordkeepers money and time to process.

A total of $820 million had to be returned because of imbalanced retirement plan coverage in the latest year's data reviewed, according to Judy Diamond Associates in a May press release. In the previous year, $794 million was returned — in paybacks known as corrective distributions.

These can be taxed as regular income for the affected participants by IRS. Such errors also can make it harder for HCEs to save as much pretax income for retirement as they desire. (See related April 2014 column.)

For example, the company that issued the largest corrective distribution for 2013, car rental company Enterprise Holdings Inc. of St. Louis, had to process excess returns totaling $7.7 million, Judy Diamond Associates said in the release.

What Is Nondiscrimination Testing?

Nondiscrimination tests involve dividing a workforce into groups of high-paid employees and low-paid employees. This process varies with the type of benefit being tested.

Some tests focus on HCEs, while others focus on "key employees," "highly compensated individuals" or "control employees."

Some of the tests require leased employees to be counted as employees for testing purposes; others do not. And finally, the rules are not uniform, nor do they provide clear guidance on how the tests should be applied to former employees, employees of related corporations or individuals who are employed in separate lines of business, according to the *Handbook.*

Specifically, to obtain the tax advantages associated with being a qualified plan, a 401(k) plan must cover a nondiscriminatory group of employees under the provisions of Code Section 410(b). In addition, contributions or benefits under the plan may not discriminate in favor of highly compensated employees under the provisions of Code Section 401(a)(4). In general, these requirements mean that a qualified plan may not provide higher-paid employees with a "better deal" than the plan provides rank-and-file employees.

The issuance of corrective distributions may "mean that the plan is not designed to encourage [all] workers to contribute sufficiently," thus leading to disproportionate HCE contributions that don't pass nondiscrimination testing,

Eric Ryles, managing director of ALM Financial Intelligence, a unit of the parent company of Judy Diamond Associates, said in the release. He suggests plans with corrective distribution problems work with a plan adviser to come up with better 401(k) savings incentives.

Finding out More

For more guidance on nondiscrimination testing for 401(k) plans, see ¶300- ¶364. ❖

New Economic Study Concludes Plan Loan Policy Shapes the Way Participants Borrow from 401(k)

Decades into reviewing the pluses and minuses of 401(k) defined contribution retirement plans, most employer plan sponsors have chosen to offer plan loans, with the dual role of attracting participants by giving early partial access to their retirement funds and threatening to erode those savings. A new paper published by two academic researchers and two Vanguard representatives suggests that plans' loan policy can shape participant borrowing, which may give sponsors a greater sense of control as a 401(k) lender.

The April paper (available with registration) from the National Bureau of Economic Research, "Borrowing from the Future: 401(k) Plan Loans and Loan Defaults," posited that when a plan allows participants to take out multiple loans, they are more likely to borrow in the first place — and more likely to default. The NBER researchers said no previous study has explored how employer loan policy affects participant behavior and resulting defaults.

The paper looks at who borrows with plan loans and why, and who defaults on those loans.

It also found that serial borrowers' individual loan amounts shrank, similar to what the researchers call the "buffer-stock approach to credit" that's been noted among credit card users, but that plan borrowing probability is twice as high with a multiple-loan policy.

Avoid 'Endorsement Effect'

Ninety percent of active contributors to 401(k) plans in the United States have access to plan loans, according to the study. Of that group, about one-fifth had a loan at any given time, an often-cited statistic that's held steady for several years. Almost 40 percent have held a plan loan over a five-year period.

Participants with access to a multiple-loan feature in their plans borrowed greater amounts in aggregate, which the researchers warn could be seen as an "endorsement effect" that the NBER researchers said plan sponsors might want to avoid.

In addition, the study said the probability of plan borrowing nearly doubles when plans permit multiple loans. The aggregate amount borrowed rises by 16 percent, "suggesting that employees perceive that easier loans are actually an encouragement to borrow."

For context, the study cited prior research that estimated aggregate premature withdrawals (or so-called account leakage) of all types from both 401(k)s and individual retirement accounts amount to 30 percent to 45 percent of annual total contributions. As such, these sizable outflows relative to inflows "raise the important question of how these liquidity features may influence future retirement security," the NBER study noted.

With that many participants involved, plan sponsors face concerns about defaults. The study estimated an aggregate effect of loan defaults valued at about $6 billion a year — an amount it called higher than others' previous estimates that relied on incomplete data, though it is still "much smaller than retirement plan leakage due to account cash-outs on job termination." A 2009 U.S. Government Accountability Office report based on 2006 data said $74 billion was lost that year to cashouts upon leaving a job (see related July 2014 story).

In reality, employer plan sponsors' worst loan default problems may lie with former employees.

The study offered several insights on loan default patterns, most strikingly that 86 percent of participants with an outstanding loan balance when they terminate employment don't repay it. Nine of 10 loans are repaid to plan sponsors, but the high default rate among terminated workers likely reflects that they may simply be surprised by an unanticipated job change and its effect on an outstanding 401(k) loan, the NBER paper said.

What Plan Sponsors Can Do

The researchers said, based on their results, concerns about out-of-control 401(k) loans that should be restricted by plans "seem overstated," citing greater damage to retirement savings from cashouts upon departure from companies.

The NBER researchers also suggested limiting the size and scope of plan loans in an effort to reduce the total dollars of loan default leakage. As an example, participant loans could be restricted to only a quarter of account balances, they said.

In the end, the study concluded that its findings underscore that DC retirement accounts are succeeding at offering pre-retirement liquidity for some of participants' consumption needs without disrupting the plans' intended purpose of providing old-age financial security. ❖

Employing Retirees? Take Steps to Avoid Problems With Your Plan

By Mary Jo Larson
Warner Norcross & Judd

As the workforce ages and retires, employers often seek to fill in gaps by hiring their own retirees as independent contractors or temporary or part-time employees. But this practice threatens the tax qualification of employers' retirement plans, both 401(k) plans and traditional pension plans.

Distributions from 401(k) and 403(b) plans are permitted only under narrow circumstances: death, disability, hardship, attaining age 59 1/2 or severance from employment.

Distributions from pension plans are even more constrained: All in-service distributions are banned until the participant reaches at least age 62. The plan document may restrict distributions even further, for example, by not allowing any in-service payouts. Distributions made before the law and the plan allow can disqualify the plan.

For example, if a participant "retires" at 57, takes a 401(k) distribution and returns to work for the same employer part-time, the retiree may be seen as not separated. The plan has then made an impermissible in-service distribution — a plan-qualification violation.

The employee may have a true severance if re-hired as an independent contractor rather than as an employee; the question is whether the re-hire truly *is* an independent contractor.

The ongoing skepticism that IRS and the courts have of "independent contractor" status doubly applies to former employees. Because the standard for "independent contractor" is whether the employer has a right to direct or control the individual, if the retiree is doing the same type of work, in the same place, with the same tools, what is the difference that suddenly creates an independent contractor status?

Recommendations Before Hiring a Retiree

We recommend the following steps before hiring a retiree:

1. Check your plan document. If your 401(k) plan permits in-service distributions at age 59 1/2, or your pension plan permits in-service payouts to begin at 62 or later (rare), and the employee took the retirement payout after the applicable age, then the plan is safe.
2. Prohibit any understandings with retirees before retirement that they will be re-hired in any capacity.
3. Require a minimum period before a retiree can be re-hired. Although no set time is safe-harbor, six months may be sufficient. Some employers use 90 days. This is not a substitute for Step 2.
4. If you re-hire the retiree as an independent contractor, make the position sufficiently different to support independent contractor status. Contract with the retiree to set goals, but turn control over to the retiree as to how the goals are to be accomplished. Let the retiree hire others; have him provide his own equipment and supplies and set his own hours. Allow him to work for other employers doing the same work. The less the work looks like the retiree's prior employment, the better.
5. If the retiree is safely re-hired, review the future effect of re-employment under the retirement plans. The retiree may be eligible for additional contributions or accruals. A pension may have to suspend monthly payments during re-employment and give notice to the participant of the suspension.

"If your 401(k) plan permits in-service distributions at age 59-1/2, or your pension plan permits in-service payouts to begin at 62 or later (rare), and the employee took the retirement payout after the applicable age, then the plan is safe."

— Mary Jo Larson
Warner Norcross & Judd LLP

Mary Jo Larson of law firm Warner Norcross & Judd LLP puts her more than 30 years of benefits experience to work on her clients' 401(k)s, pension plans, nonqualified deferred compensation plans and executive compensation. She also advises fiduciaries responsible for the investment of plan assets. ❖

Agency Roundup

Distribution Reporting Failure Fees Rise As Part of New U.S. Trade Preferences Law

A peripheral provision of the newly enacted U.S. Trade Preferences Extension Act (H.R. 1295) increases the penalty fees for late reporting of some retirement distribution failures. The measures are one of several ways the federal government aims to raise revenue from the trade act.

	Within 30 Days	More than 30 Days but Before Aug. 1	After Aug. 1
Per Return	$50	$100	$250
Maximum	$500,000	$1,500,000	$3,000,000
Small-business Maximum	$175,000	$500,000	$1,000,000

The bill, signed into law June 29 by President Barack Obama, increases the tiered penalties (see table above) for failing to file on-time information returns and payee statements for distributions required under the federal tax Code. It applies to reporting failures by plans or their service providers for:

1. distributions from retirement plans and individual retirement accounts on Form 1099-R; and
2. income distributions to some foreign persons based on their U.S.-sourced income on Form 1042-S.

The new fee amounts, which will be required on late statements and returns filled after Dec. 31, 2015, are significantly higher than current fines. The penalties apply to failures to furnish correct statements (Copy B) to distribution recipients in addition to IRS filing errors.

For Incorrect or Missing Information

"A penalty may apply if a financial organization fails to timely file these forms, fails to include the information required to be shown on the forms, or includes incorrect information," a June 30 press release about the act's retirement distribution provision from independent retirement services provider Ascensus said.

The new penalty amounts are based on how late a filing or correction are submitted, and the size of the business of the plan sponsor involved. Small businesses with average annual gross receipts of $5 million or less for the three most recent tax years ending before the reporting calendar year have a lower penalty cap.

The fees break down as follows for returns required to be filed after Dec. 31, 2015:

The passage of the Trade Preferences Extension Act, which continues the African Growth and Opportunity Act, the Generalized System of Preferences for some sub-Saharan countries and the preferential duty treatment program for Haiti, among others, lays the ground for potential agreement on the controversial 12-nation Trans-Pacific Partnership that Obama is still negotiating. It includes countries from Chile and Mexico to Japan and Australia, and would give the United States greater economic influence in Asia.

The Trade Preferences Extension Act includes Trade Adjustment Assistance programs, which provide federal job-training and other assistance to U.S. workers, companies and communities that have been adversely affected by foreign trade, including those in the United States who have lost jobs.❖

Catch-up Contributions Don't Help Many Accounts

The participants 50 or older who have taken advantage of contributing much more of their salary to 401(k) retirement plans through catch-up provisions already were among the highest savers — and so few workers overall are constrained by the annual IRS limits that catch-up contributions aren't a solution for low retirement savings rates.

Those conclusions come from an academic study released in July from the Center for Retirement Research at Boston College, which said only about 10 percent of 401(k) participants are blocked from saving more by the yearly limits set by IRS.

The escalation, starting in 2002, of higher limits for all and catch-up contributions for those 50 and older did increase contributions from 2002-05, the period studied, but only for those savers near the previous limits, the study said.

As part of this escalation by policymakers, total allowable contributions rose to $18,000 in 2005 from $10,500 a year in 2001 for those eligible to make

See *Catch-up,* p. 9

High Court Seeks Administration's View Of Aegon ERISA Venue Selection Case

The Supreme Court has asked the Obama administration for its view on whether ERISA's special venue provision, and a plaintiff's choice of venue under it, may be canceled out by a retirement plan's more restrictive clause on venue selection.

The High Court is considering whether to hear an appeal of the October 2014 decision by the 6th U.S. Circuit Court of Appeals that an employer-sponsored plan can limit the court venues in which it may be sued. A decision to uphold this ruling would give plan sponsors greater control over litigation brought against their plans.

The U.S. Solicitor General on June 1 was invited by the Supreme Court to file a brief on *Smith v. Aegon Cos. Pension Plan* (769 F.3d 922 (6th Cir. 2014), petition for cert. filed Mar. 13, 2015 (No. 14-1168)). In the earlier appellate court hearing, judges disregarded the U.S. Secretary of Labor's call for "ready access to Federal courts" for lawsuits against ERISA-covered plans, saying in their decision that DOL lacked experience in determining which federal statutes prohibit venue selection. The 6th Circuit accused DOL of "regulation by amicus" for the position presented in its friend-of-the-court brief.

Could Show Support for Plan Sponsors

A Supreme Court validation of the appellate court's ruling also would be seen as supporting the broad deference commonly given to plan sponsors to design and amend their plans as they see fit, following two recent retirement plan-related decisions from the Court that have been seen as unfavorable to plan sponsors.

In May, the Court in *Tibble v. Edison International,* 135 S. Ct. 1823 (May 18, 2015), potentially added to plan administrators' burdens when it unanimously vacated a federal appellate court ruling that employee retirement plan participants' claims about fees applied to their plan were time-barred. In doing so, the Court sent a clear message that plan fiduciaries have an ongoing duty to monitor investments, their expenses and other related claims within that duty's statute of limitations and sometimes beyond. (See May story.)

In June 2014, the Court had ruled that fiduciaries of employee stock ownership plans are not entitled to a presumption of prudence in a closely watched "stock-drop" suit over an offering of company stock as a defined contribution retirement plan investment option (see June 2014 story). The decision in *Fifth Third Bancorp v. Dudenhoeffer*, 134 S. Ct. 2459 (June 25, 2014), also was interpreted as a blow for plan fiduciaries, who have frequently used this presumption of prudence to defend their retirement plan asset selections.

The *Smith* Case So Far

As reported, in the *Smith* case, plaintiff Roger L. Smith sued over a request from Aegon, a successor plan sponsor to his employer's, to remit more than $150,000 in benefits the plan sponsor claimed had been erroneously overpaid in the 11 years since he retired in 2000.

In 2007, Aegon's board had amended the pension plan to add a "venue provision," which states that a participant or beneficiary could only bring an action in connection with the plan in federal district court in Cedar Rapids, Iowa, where the plan is administered. Following this provision, the district court in Kentucky where Smith sued dismissed the action.

In his suit, Smith argued that the 2000 plan document in force when he retired and his benefits accrued should control his case, rather than the 2007 amendment that included venue selection. But the district court said his benefits didn't accrue until 2011, after the venue selection amendment, when Aegon's plan committee told him it was reducing his payments.

After the dismissal, Smith filed a second suit against Aegon's plan in the same district court but it was also dismissed because of the plan's venue selection clause. The plaintiff then appealed and the case was heard by the 6th Circuit.

The appellate judges said that ERISA is built around reliance on written plan documents. Given the discretion commonly bestowed on plan sponsors under the act, the judges said, there is no reason the venue selection clause is invalid. They also cited previous case law in which courts faced with the same issue found that venue selection clauses in ERISA plans were enforceable. ❖

Agency Roundup

Confusion Over Roth 401(k) Tax Advantages Causes Lag in Contribution Rates, Researchers Say

Savers in employer-sponsored retirement plans haven't yet been enticed to put more of their contributions in taxable Roth 401(k) accounts since their inception in 2006, but some academic researchers think they may understand some reasons why. And Millennials may turn this trend around, based on early indications of their account choices.

The research findings underscore the importance of plan sponsors educating participants about 401(k) tax rules and ways to maximize their future retirement income as early as possible.

In a research report by four academics working with the National Bureau of Economics, no difference was found in sample data between contributions to traditional tax-deductible 401(k) plans and Roth 401(k)s, which are not tax-deductible at the outset but skip taxation when withdrawn in retirement. The researchers looked at four years of data from 11 companies that added a Roth contribution option when they first started, as part of the 2006 Pension Protection Act.

Millennials Get It

More recently, a new Wells Fargo survey noted that Roth 401(k) usage is rising slightly from four years ago, especially among the youngest workers. It found that Millennials are the biggest users of Roth accounts in 2015, with 16 percent funding one compared with 11 percent of Gen Xers and 7 percent of Baby Boomers. People early in their careers are often paying taxes at the lowest rate of their lives, so absorbing taxation at that point in a Roth account can be less expensive than for those nearing retirement.

The researchers noted that increasing the proportion of contributions channeled into a Roth account could help participants when retirement comes because a dollar of Roth balance carries more buying power later than a dollar of before-tax balance, if the marginal tax rate in retirement goes up. In other words, employees can contribute less to a Roth account to achieve the same amount of money for retirement, controlling for investment return fluctuation. But participants often interpret Roth accounts as being more costly because of their upfront taxation.

"If people neglect taxes in making savings decisions, the total dollars contributed to the 401(k) will not change when a Roth becomes available, causing effective retirement savings to increase … provided that some of those dollars are contributed to the Roth," the paper, titled "Does Front-Loading Taxation Increase Savings? Evidence from Roth 401(k) Introductions" said.

In the data taken from 2006 and 2010, they found no difference in total contribution rates of employees hired one year before a Roth option was available and those hired immediately after it was introduced. "If anything, contributions rise slightly when the Roth is available," the paper said.

To test some of their assumptions, the researchers also ran an online experiment that surveyed 7,000 defined contribution plan participants. They described a 401(k) retirement savings scenario for a fictitious married couple and gave respondents three choices from which to recommend a course of action, contributing to: (1) a before-tax 401(k) account only; (2) a Roth 401(k) account only; or (3) both before-tax and Roth 401(k) accounts. In addition, they asked a few questions to test the participants' knowledge of 401(k) tax rules.

Their responses showed that many lacked understanding of how traditional and Roth 401(k) accounts are taxed and how advantageous saving in a Roth account can be down the road.

"Our survey experiment suggests that employee confusion about and neglect of the tax properties of Roth balances … [drives] our finding that total contribution rates do not change following Roth introduction," the researchers said.

Employer Matching Influences Choices

Another factor that could be influencing choices about how to divide retirement contributions is the fact that employers' matching contributions must be made using pretax dollars, so that the entire principal and earnings are subject to tax upon withdrawal. As a result, participants are likely to be more attracted to devoting at least the minimum amount necessary to achieve an employer match — often 3 percent to 6 percent at many companies — to their traditional 401(k) than a Roth account.

Beyond that, the researchers pointed to a phenomenon called "partition dependence," a term defined by other academics in a 2005 psychology journal article, as

See *Roth Contributions,* p. 9

Catch-up (continued from p. 6)

catch-up contributions during that period. (That annual figure stands at $24,000 for 2015.)

The CRR researchers said this muted reaction to greater tax incentives for more retirement saving was consistent with earlier research.

Looking at various statistical scenarios, the researchers found that the 50-and-older group, which included a segment already saving near or at the annual limit, raised its dollar contributions by 3.5 percent from 2002 to 2005, about half the 6.8 percentage-point-higher ceiling these workers were allowed for contributions.

As no surprise, the highest contributors to 401(k) plans have the highest salaries, around $163,000 a year, compared with $57,000 for the full sample, the data showed.

"These results imply that for every 1-percentage-point increase in the tax-deferred limit, maximum contributors will increase their contributions by nearly one-half a percentage point," the CRR researchers wrote.

"While this group does not increase their contributions all the way up to the new limit, they appear to be quite sensitive to tax incentives" to boost 401(k) savings, the report continued.

The report notes that the CRR analysis does not take into account the extent to which the increase in 401(k) contributions among maximum earners represented an increase in their total saving.

Roth Contributions (continued from p. 8)

having an impact on the amount set aside in a participant's Roth account. Partition dependence is a psychological bias toward allocating an equal amount to each part when making choices about dividing something. So, for example, if a participant is contributing a total of 8 percent of her salary to her 401(k) and the employer match begins at 5 percent, the participant is not likely to devote more than 3 percent of the deferral to her Roth account, regardless of the long-term tax advantages of doing so.

The NBER paper said the slight increase in Roth contributions that it noted in the data studied is likely attributable to this partition dependence: If employees are given a new, second account option in the form of a Roth 401(k) in addition to their regular account, many will direct the same percentage of deferral to both, it said.

Finding out More

For more information about after-tax employee contributions to 401(k)s, see ¶222 in the *Handbook*. ❖

It's possible that these individuals merely shifted their planned savings from a non-tax-advantaged account into their 401(k)s, the researchers said.

Tip Box

Catch-up contributions are deemed to be amounts deferred into the 401(k) plan that exceed: (1) annual statutory limits on deferrals or additions; (2) an employer-imposed limit; or (3) the plan's actual deferral percentage nondiscrimination limit. Under the catch-up rules, an employee aged 50 or older by the end of the calendar year who is otherwise eligible for the 401(k) plan can make catch-up contributions as of Jan. 1 of that year, regardless of whether the employee survives to age 50 or terminates employment during the year, or whether the plan is a calendar-year plan.

They concluded that "further tinkering with the contribution limit for 401(k)s would likely affect only a very small group of people," and does not offer a broad cure for low U.S. retirement savings in general.

The CRR researchers used data from the U.S. Census Bureau's "Survey of Income and Program Participation," a panel survey that includes demographic and economic variables and is linked to Social Security earnings records.

Finding out More

For more information on catch-up contributions and their annual limit, see ¶244 in the *Handbook*. ❖

Is Your ERISA Fiduciary Liability Insurance Current?

Employer-sponsored retirement plans can obtain ERISA fiduciary liability insurance policies to protect their fiduciaries and trustees from personal liability. As fiduciary liability law changes, it is important to ensure that such policies cover the appropriate risks, and to evaluate whether the coverage plans are sufficient and complete. Newer and more comprehensive policies cover not only breaches of fiduciary duty and administrative errors, but also settlor and non-fiduciary functions and regulatory penalties.

Coverage Checklist

Law firm Haynes & Boone offers this checklist for companies to use to evaluate their fiduciary liability policies. They should consider, depending on their needs, whether the following items are covered, or should be:

- costs and expenses of U.S. Department of Labor and other regulatory audits/investigations;
- claims involving settlor/non-fiduciary functions;
- failures to comply with certain ERISA disclosure requirements;
- ERISA 502(a)(3) equitable-relief claims;
- non-exempt prohibited transactions under ERISA and the federal tax Code;
- plan benefit overpayments; and
- costs from corrections under the IRS Employee Plans Compliance Resolution System/Voluntary Compliance Program and Voluntary Fiduciary Correction Program.

DOL Sues Fiduciary Who Allegedly Sought To Transfer 401(k) Plan Assets to Self

Although the alleged breach may sound far-fetched, a new federal lawsuit accusing the CEO of a defunct software company of siphoning participants' retirement savings into his own account serves as a reminder that fiduciary performance at employer-sponsored plans is closely watched by the U.S. Department of Labor's enforcement division.

The suit, *Perez v. Rik Sanchez, ANTS Software Inc. and ANTS Software Inc. 401(k) Plan*, No. 1:15-cv-02388-WSD, N.D. Ga. (filed July 2, 2015), seeks to obtain penalties and unspecified relief for the actions of former ANTS Software Chairman and CEO and plan fiduciary Rik Sanchez. DOL alleges Sanchez tried to gain access to participants' retirement assets to shift them to an account he controlled.

Background of the Case

Sanchez was named CEO, president and secretary of ANTS Software, located in suburban Atlanta, in November 2012; it ceased operations on Feb. 25, 2013, the suit said. At that time, Sanchez was given authorization to terminate the plan and distribute its funds at his discretion, the lawsuit continued.

Less than three months after that date, Sanchez asked the plan's third-party administrator to release plan assets to the participants and end its servicing of the plan. In May 2013, the TPA refused to proceed with asset distribution because, the suit alleges, Sanchez used his plan login ID to gain access and switch the bank account information for participants to an account of Sanchez's own.

He then requested the TPA to transfer management of the plan to Renowned Holdings Inc., a company Sanchez controls, according to the court filing. At the time of the July 2 court filing, the TPA had not done so.

As a result of these several ERISA breaches, participants have not been able to get information about or access to their retirement funds since the company's closure in February 2013, DOL alleged.

As punishment, DOL seeks to enjoin Sanchez, ANTS Software and its 401(k) plan from engaging in further ERISA violations, serving as a fiduciary, administrator, trustee or other related roles at any employee benefit plan covered by ERISA.

The suit asks the federal district court in Atlanta to appoint an independent fiduciary at the defendants' expense to terminate the plan and distribute its assets to participants. The suit also requests unspecified equitable relief for participants, but it doesn't include details about the amount or distribution. ❖

Murphy (continued from p. 2)

- Up to 10 percent of any benefit being paid out may be voluntarily and revocably assigned or given to someone other than the relevant participant unless the assignment is for, or has the effect, of defraying plan administration costs.
- Criminal or civil judgments, consent decrees and settlement agreements may permit a participant's benefits to be offset under a plan and may require the participant to pay the plan if the participant commits a fiduciary violation or crime against the plan.

Plan Administration

Just as the plan establishes administrative procedures for making benefit payments to plan participants, it must also establish procedures for redirecting benefit payments, when that becomes necessary. While this may be rare, it is advisable for the plan administrator to set parameters for what legal documents are required to confirm the validity of the parties involved, which forms are needed to authorize releasing the assets, and to record retention procedures to handle any restitution or related requests for a plan participant.

Before payment of retirement plan benefits to a party other than a married participant, spousal consent is required. In a 401(k) plan, a lump-sum benefit option usually is available and will allow the participant to satisfy the garnishment order to pay a tax levy with a single payment. However, if the plan is subject to qualified joint and survivor annuity requirements, the only collection avenue available to IRS is monthly or quarterly annuity payments. That is, unless the plan provides for lump-sum distributions and IRS can obtain the spouse's consent to receive a lump-sum distribution to satisfy the garnishment or levy.

As seen in the *Wilson* case, the United States may enforce a judgment imposing a fine or an order of restitution in accordance with federal law as an exception to the ERISA anti-alienation provision that protects retirement plan assets.

It is important to note that when complying with court orders, the plan administrator must adhere to the plan terms. This means delaying any distributions on behalf of a participant until the participant is eligible for a distribution under the plan terms. ❖

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Annuity (continued from p. 1)

This confusion could put plan sponsors off providing an annuity option for lifetime income (see related March 2014 story), EBSA said. Federal agencies that regulate retirement savings increasingly have been encouraging plan sponsors and easing rules to promote lifetime income options as traditional pensions that offered these streams wane.

Definition of 'Time of Selection'

The FAB explains that the safe harbor rule defines "time of selection" as the time that the annuity provider:

1. and the contract are selected for distribution of benefits to a specific participant or beneficiary; or
2. is chosen to provide annuities as a distribution option for participants or beneficiaries to pick at future dates.

As part of the second provision above, the fiduciary must periodically review the conclusion that the annuity provider is financially able to make all future payments under the annuity contract, as well as the reasonableness of the cost of the contract in relation to the benefits and services to be rendered.

"The fiduciary is not, however, required to review the appropriateness of its conclusions with respect to an annuity contract purchased for any specific participant or beneficiary," the FAB continued.

This means the prudence of a fiduciary decision tied to plan annuities is evaluated based on the information available when the decision is made — not based on facts that come to light later.

Limitations of New FAB

EBSA cautions that the FAB's guidance is limited only to the selection and monitoring of annuity providers for benefit distributions from DC plans.

Another initiative to encourage consideration of, offering and use of lifetime income alternatives, which include annuities, is being conducted by DOL and the U.S. Treasury Department. ❖

HSA Isn't Retirement Plan, So Assets Can't Be Shielded From Creditors, Colo High Court Rules

A new ruling by Colorado's state supreme court that health savings accounts are not retirement plans in the state underscores HSAs' lack of ERISA coverage in most cases, and limits the shelter from debt collectors that is granted to pension participants.

A debtor may not classify his or her HSA as a retirement plan to protect his assets from creditors, Colorado's Supreme Court ruled on June 1, affirming a state appeals court ruling.

The state high court said an HSA is not intended to replace income lost in retirement; instead, it is meant to cover medical costs incurred at any point during a person's lifetime, and therefore is not exempt from the state's statutes on garnishment to settle creditors' claims.

Background of the Case

In *Roup v. Commercial Research LLC*, 2015 WL 3452615 (Colo. 2015), the creditor, Commercial Research, filed a judgment in a Colorado court to begin collection proceedings against plaintiff Gary Roup's assets. Included in the creditor's claim was $3,729.24 held by Roup in an HSA. Roup asserted the HSA was a retirement plan, which under Colorado law would exempt it from taxes or sale. Historically, Colorado's statutory exemptions' purpose has been to preserve a debtor's means of support, Justice Gregory J. Hobbs Jr. wrote in the state supreme court's decision.

The state high court said repeatedly in its decision that the term "retirement plan" is unambiguous and must be interpreted according to its ordinary meaning, which excludes savings plans for medical costs that can be tapped before retirement.

In the trial court, it was determined the HSA was not a retirement plan, with the court reasoning that an HSA merely allows individuals to defer income on a tax-exempt basis to pay medical expenses associated with high-deductible health plans at any time, not only in retirement. The court ordered the funds to be released to the creditor.

On remand, the trial court ruled that even though the bankruptcy discharged the underlying judgment, that did not end the creditor's right to garnishment because Roup had not taken any steps toward ending the lien on his assets, a requirement based on previous case law. ❖