



The Retirement Advisor

“A Newsletter for Retirement Plan Sponsors”

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How Does Your Plan Compare?

Keeping up with trends in the retirement plan industry can help a company gauge how competitive its plan may be as an employee retention and recruitment tool. The Profit Sharing/401(k) Council of America’s most recent annual survey,* which reflects 2008 plan year experience, offers some interesting insights into current practices.

- Companies contributed an average of 4.1% of payroll (9.3% of pay in profit sharing plans and 2.9% of pay in 401(k) plans).
- In more than a third (37.1%) of plans, matching contributions were immediately vested. Immediate vesting was less common for non-matching contributions (26.1% of plans).
- Roth 401(k) contributions were permitted in 36.7% of plans, but only 15.6% of eligible employees chose to make Roth contributions.
- On average, plans offered 18 funds for the investment of participant contributions.
- Investment advice was available to participants in more than half (51.8%) of plans. ■

*52nd Annual Survey of Profit Sharing and 401(k) Plans, 2009

Paying Expenses Out of Plan Assets

With the continued economic uncertainty, many companies are looking at ways to cut the costs of providing retirement benefits as a means of lowering overall business expenses. Some employers have reduced or suspended matching contributions. Some are charging more of the expense of maintaining a plan to the plan itself. Take care if you’re thinking about combining these two cost-saving measures.

Not all plan-related expenses can be charged to the plan. It’s important for all employers to know what can and cannot be paid by the plan. Otherwise, you run the risk that the payment could be deemed a prohibited transaction. Subject to certain exceptions, plan fiduciaries, including plan sponsors, may use plan assets only to provide benefits to plan participants and beneficiaries and to pay reasonable expenses of administering the plan.

Business or “Settlor” Expenses

Employers sometimes confuse plan-related business expenses — which aren’t payable from plan assets — with plan administration expenses. The U.S. Department of Labor (DOL) has long held that costs incurred to design, establish, and terminate plans — so-called “settlor functions” — are not reasonable expenses of administering a plan. These expenses are incurred for the benefit of the employer and involve services the employer can reasonably be expected to pay in the normal course of its business operations.

Plan Amendments

While the costs of designing a plan can’t be charged to the plan, fees related to maintaining the plan’s tax-qualified status, including drafting amendments required by tax law changes, generally can be paid out of plan assets — with some exceptions. (Continued on Page 3)



Quotes of the Quarter

*"Invest in
yourself, in
your
education.
There's
nothing
better"*

Sylvia Porter

*"Economy is
the method by
which we
prepare today
to afford the
improvements
of tomorrow"*

Calvin
Coolidge

Talking to Pre-retirees

In 1999, 17.2 million American workers were age 55 or older. By mid-2009, this number had increased to 27.1 million. With this aging of the U.S. work force, it's important for employers to take care that their retirement education programs meet the needs of pre-retirees as well as those of younger employees. Below we answer some questions about providing pre-retirees with the information they need to make the transition from work to retirement.

How are the communication needs of older employees different? Most retirement education materials focus on encouraging employees to enroll in the company's plan and contribute as much as they can to their plan accounts. Increasing the number of younger and lower paid plan participants to help the plan meet nondiscrimination testing requirements is often one goal of these materials. Communications concentrate on plan basics: how the plan works; the advantages of pretax contributions, tax-deferred compounding, starting early, and contributing regularly; and how to invest plan contributions to reach retirement goals. Investment education stresses "growing your account." This is important information for most plan participants. But, as employees move closer to retirement age, they need additional information about their plan distribution options and how to invest their accounts to preserve their assets.



With all the statistics on the "baby boomers" not having saved enough for retirement, don't older employees need to be encouraged to contribute, too? Yes, they do. But you may want to customize some "contribute more" messages to appeal specifically to preretirees. If your plan allows catch-up contributions, send annual reminders to workers age 50 and older. Many of these employees are in their highest earning years. Consider participant newsletter articles or other communications that remind participants that they can really focus on retirement "now that the kids are through college" or "now that your home mortgage is paid off." Online tools that help older workers project their retirement budgets and calculate the gap between current retirement savings and the amount of savings needed at retirement may be particularly helpful.

What kinds of distribution information do these employees need? Before they are actually ready to retire, employees need to be aware of the types of retirement distributions available from your plan and how each option works. One survey* of participants age 50 to 64 found that, when asked whether they could withdraw their account balances as a life annuity rather than a lump-sum distribution, fewer than half answered correctly. An employee's distribution options can have an impact on retirement planning. Older participants also need to know that they generally must begin taking annual required minimum distributions from their plan accounts after they turn age 70½. (Continued on page 3)

"Banking" Vacation Time for Retirement

SITUATION: Our company has a paid time off (PTO) plan. At the end of the year, employees forfeit any vacation days they have not used. We are short-staffed and have several employees who generally do not use all of their allotted vacation time.

QUESTION: Can we amend our 401(k) profit sharing plan to allow us to contribute the dollar equivalent of the unused vacation days to these employees' accounts?

ANSWER: Yes. Contributions of the dollar equivalent of unused paid time off are permissible. The contributions will not jeopardize a plan's tax-qualified status as long as the plan meets all relevant tax law requirements. (Continued on page 4)



Quotes of the Quarter

"If you don't have integrity, you have nothing. You can't buy it. You can have all the money in the world, but if you are not a moral and ethical person, you really have nothing."

Henry Kravis

"In this business if you're good, you're right six times out of ten. You're never going to be right nine times out of ten."

Peter Lynch

Paying Expenses Out of Plan Assets Cont'd

For example, if maintaining tax-qualified status involves the employer having to analyze and choose from several options for amending its plan, the expenses incurred in that analysis would be settlor expenses that cannot be paid out of plan assets.

What does this mean for employers that have amended or are considering amending their plan documents to reduce or suspend matching contributions? Because such an amendment benefits the employer and not the plan participants, these employers would be well advised to pay the costs of the amendment (and any other amendment that reduces employees' benefits) themselves and not out of plan assets.

Allowable Administration Expenses

So what expenses can the plan pay? Generally, plan assets can be used to pay these and similar administration expenses incurred in operating the plan:

- Fees paid to maintain a plan's tax-qualified status
- Trustee fees
- Annual accounting of trust assets
- Recordkeeping expenses
- Costs of valuing assets
- Certain investment management fees and expenses
- Employee communication expenses for participant disclosure statements
- Costs of computing participant benefits
- Fees for participant enrollment/election changes
- Fees for participant investment changes/elections
- Expenses for participant loan administration
- Costs of administering qualified domestic relations orders
- Certain legal fees ■

Talking to Pre-retirees Cont'd

What about investment education? Targeted communications can help older employees understand the need to review their asset allocations periodically as they move closer to retirement and, in many cases, gradually shift some of their growth investments into more conservative investments that can help them preserve their savings. The impact inflation can have on retirement expenses and the resulting need to keep some growth investments to stay ahead of inflation is another important topic for both pre-retirees and retirees.



How about communicating with retirees who stay in the plan?

Along with providing statements, you should communicate to retirees the importance of keeping the plan informed of changes in their lives, such as residential or e-mail address changes and family changes that may require them to update their beneficiary designation(s). ■

* U.S. Survey of Older Employees' Attitudes Toward Lump Sum and Annuity Distributions from Retirement Plans, May 2007, Watson Wyatt



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“Banking” Vacation Time for Retirement Cont’d

DISCUSSION: A recent IRS revenue ruling* gives two examples. In the first, a company’s PTO plan provides that employees forfeit any paid time off they haven’t used by the end of the year. At that time, the company allocates the dollar equivalent of the forfeited time to the employee’s plan account to the extent applicable tax law limitations are not exceeded.

At the close of business on December 31, 2009, an employee has unused paid time off equal to \$500 (number of unused PTO hours multiplied by pay rate). After applying the tax law’s limitation on annual additions, the company can contribute only \$400 to the employee’s account. The company makes the contribution in February 2010 and pays the employee the remaining \$100. The employee includes the \$100 in his gross income for 2010, the year he receives the payment.

Since the employee wasn’t given the option of receiving the \$500 in cash, the plan contribution is a non-elective employer contribution instead of an elective deferral. The contribution is considered made in 2009, the year it is allocated to the employee’s account.

What happens if employees have a choice of receiving a cash payment for their unused paid time off or having the dollar equivalent contributed to the employer’s 401(k) plan? The second IRS example illustrates this scenario.

In the situation described, the employee defers only a portion to the 401(k) plan and receives the rest in cash. The plan contribution is considered an employee elective deferral and is subject to both the annual additions and deferral limitations. The amount not contributed is taxed to the employee in the year paid.

The ruling does not provide a nondiscrimination safe harbor. Plans offering contributions of unused paid time off need to test to ensure they do not discriminate in favor of highly compensated employees.

* Rev. Rul. 2009-31 (9/4/2009)



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