BCG Retirement News Roundup

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Boomershine Consulting Group, 3300 North Ridge Road, Suite 300, Ellicott City, Maryland 21043

www.boomershineconsulting.com **410-418-5525**

Boomershine Consulting Group (BCG) provides this monthly news roundup of highlighted significant articles from the retirement industry – for clients and friends. Retirement plan news has become increasingly pertinent for many audiences these days, including:

- Retirement Plan Sponsors – addressing both private and public sector issues
- Employers – dealing with complicated decision making for their plans
- Employees – educating the Boomer generation that is nearing retirement
- Industry Practitioners - helping to understand and resolve today's significant challenges

We review numerous industry news services daily and will include a collection of timely and significant articles each month concerning compliance, actuarial plan costs (including assumption debates), plan design change issues and benefit trends, as well as other related topics. If you would like to discuss any of these issues, please contact us.

Inside This Issue

Public Sector/Government Plans

Puerto Rico gov defies board, rejects reform, pension cuts

The powers of a federal control board overseeing Puerto Rico's finances could soon be tested as the U.S. territory's governor on Monday defied its calls to implement more austerity measures amid an 11-year recession.

Gov. Ricardo Rossello rejected demands that his administration submit a revised fiscal plan to include a labour reform and a 10 per cent cut to a pension system facing nearly $50 billion in liabilities. He said the plan he will submit Thursday also will not contain any layoffs.

"The board does not have the power to implement issues of public policy," Rossello said. "It's that simple."

The board has not responded publicly yet to Rossello's comments, which came just hours after he sent the board a seven-page letter Sunday night outlining why he will not implement those and other changes.

"The people of Puerto Rico, in the aftermath of Hurricane Maria, have suffered a great deal in terms of reduced government services and economic loss," Rossello said in the letter. "Now the board is attempting to enforce additional cuts on government employee and retirement benefits at the worst possible moment, as Puerto Rico attempts to recover."

The Category 4 storm caused more than an estimated $100 billion in damage when it hit on Sept. 20 at a time when the territory was struggling to emerge from an economic crisis and restructure a portion of its more than $70 billion public debt load. Roughly 80,000 power customers remain in the dark more than six months after the hurricane.
Board spokesman Jose Luis Cedeno did not respond to a request for comment.

The board has the authority to approve its own fiscal plan with the changes it seeks, but Rossello said it does not have the power to force his administration to implement them.
"If the board certifies some of those measures, we won't execute them," he said.
The board has said it will approve the government's fiscal plan by April 20.

On Sunday, the board posted letters in which it revealed that it also has rejected a fiscal plan for Puerto Rico's largest public university and its Highways and Transportation

Authority. It said the University of Puerto Rico should increase its per-credit tuition from $57 to $157 by next year, a proposal that local officials have rejected. In addition, it said the transportation authority's fiscal plan does not set aside funding for key projects and needs a debt sustainability analysis.

Rossello's administration did not immediately respond to the board's letters. It has until Thursday to amend and submit those two fiscal plans.

Rossello initially submitted a labour reform bill to Puerto Rico legislators that would have eliminated a Christmas bonus and increased the minimum wage from $7.25 an hour to $8.25 by 2021, among other things. He then withdrew the bill last week in response to the board's demands.

Rossello also criticized a letter sent to the board last week by Utah Republican Rep. Rob Bishop, chairman of the House Natural Resources Committee. The governor said that it was full of errors and that it seemed the U.S. government was more interested in helping creditors obtain part of the money they invested in local government bonds than in helping Puerto Ricans recover.

Katie Schoettler, a spokeswoman for Bishop, said Rossello was not in office or involved in any negotiations when Congress approved a law in 2016 that created the board, which also is overseeing Puerto Rico's debt restructuring.

"Perhaps the governor has a different interpretation of the actual law," she said.
Bishop said in his March 29 letter that he was frustrated with the board's "inability and unwillingness" to reach consensual restructuring deals with creditors and what he called a "lack of respect" for congressional requirements of Puerto Rico's fiscal plan.

On Monday evening, Rossello issued a 13-page letter to Bishop in which he said that his administration has been working closely with the board and that ultimately Puerto Rico's government is the only one with the power to implement public policy.

"Your letter is truly disturbing in its reckless disregard for collaboration and co-operation in favour of an anti-democratic process akin to a dictatorial regime," Rossello wrote.

"Regrettably, your letter embodies everything that is wrong with this process and only serves to reinforce the dismissive and second-class colonial treatment Puerto Rico has suffered throughout its history as a territory of the United States, which undermines our efforts to address the Island's fiscal, economic, and humanitarian crises."

Kentucky attorney general sues to stop pension bill

Kentucky's Democratic attorney general says he's filed suit to stop changes to public employee pensions in the commonwealth.

For at least one Northern Kentucky teacher, it might be too late.

Attorney General Andy Beshear alleged Senate Bill 151, which Republican Gov. Matt Bevin signed Tuesday, breaches the state government's "inviolable contract" with its workers.

"That's a promise the General Assembly made to teachers, social workers, police officers, firefighters decades ago that said if you dedicate your life to public service -- teaching our children, protecting our families, serving the neglected -- that while we wouldn't pay you enough, we would guarantee you a good and safe retirement," Beshear said.

He also argued the way lawmakers passed pension changes -- by amending a sewage bill at the last minute -- violates multiple provisions of Kentucky's constitution and multiple state statutes.

Beshear wants the bill thrown out entirely. He is seeking a temporary injunction to prevent the changes from becoming law until the lawsuit gets a full hearing.

The Fraternal Order of Police and Kentucky Education Association joined him in the suit, filed in Franklin County Circuit Court in Frankfort.

Brittany Terry, a substitute teacher for Boone County Schools and Erlanger-Elsmere Schools, already turned in her resignation notice. On the line that asks her reason, she wrote: "leaving the state for one with teacher benefits/pension."

"It's heartbreaking," she said. "I wanted nothing more than to work with Boone County Schools. I love the kids here, I love the teachers here. I hate to leave it."

Terry spoke by videocall Wednesday from South Carolina, where she's looking for a new home. She said her family has already put their home in Hebron up for sale.

It's been tough on her three kids, she said.

"Our youngest was born here. This is the only home they know. They understand why we're moving, but they're equally devastated," she said.

Beshear thinks Terry's path could be one many more teachers take if the pension bill stands.

"It will cause massive retirements at a time when our schools can't handle it. Some schools and school systems will lose a large percentage of their employees that have the most expertise, that they won't be able to replace in time," he said.

Teachers rallied at the Capitol last week over Bevin's proposed cuts to education funding and the pension bill. They plan to be back again Friday, when lawmakers try to override Bevin's veto of budget and revenue measures that would have avoided most school cuts.

Court strikes down Chicago Park District pension plan

A Chicago Park District pension fund overhaul that Mayor Rahm Emanuel once held up as a model of city-union cooperation has been struck down by a judge, in a ruling that could produce more vexing financial challenges for both the mayor and taxpayers.

Circuit Court Judge Neil Cohen ruled that a January 2014 state change to the district's pension system was unconstitutional because it diminished benefits by raising the retirement eligibility age and reducing both cost-of-living increases and disability benefits.

Cohen then ordered that the district return to workers the higher retirement contributions they've made as a result, with 3 percent interest tacked on. He also ordered the district to make payments covering reduced disability payments, plus interest. The ruling came in March, receiving scant attention during the primary election season.

How much it will cost the district — and ultimately taxpayers — remains to be calculated, but the cost won't be the extent of the Park District's woes. Despite increased contributions from employees, district reserves and taxpayers, the pension fund's finances have grown worse in recent years.

The fund only has about 39 percent of the money it needs to make future benefit payments. It's about $611 million short, said Sarah Wetmore, vice president and research director of the Civic Federation budget watchdog group.

That compares to a debt of $507 million and 44 percent funding in October 2015, when workers backed by Service Employees Union International Local 73 filed the lawsuit.

Once the district makes ordered payments to workers, its pension funding status will get worse. “It puts into question the sustainability of the fund going forward,” said Wetmore, who noted that when the legislation passed, the fund was at risk of going broke within a decade.

Emanuel spokesman Matt McGrath released a statement calling the judge’s decision “disappointing.”

“But we will work to find another responsible and fair funding plan that allows for the Park District to continue its core mission while still meeting the district’s pension obligations,” McGrath said.
Park District Chief Financial Officer Steve Lux called the ruling “detrimental for the thousands of former and current employees who depend on the fund for their livelihood.”

“We still hold firm in our belief that pension reform is critical to ensuring the financial security for our retirees," he said in a statement, which also noted the Park District will work with “labor partners” to craft pension reform legislation.

But SEIU Local 73 official Eliseo Medina heralded the court decision, saying in a statement that it means district “employees will have the same rights to retire and enjoy cost of living benefits in retirement as they had before the law was passed.”

Under the judge’s order, the fund will keep an additional $25 million in supplemental district contributions to the pension fund made from cash reserves. It also will be able to keep an additional $12.8 million that came from higher property taxes authorized under the state changes to the fund.

The property tax hike that was part of that deal will be collected this year but reversed going forward, so the district will have to find other ways to fix the retirement system.
If history is a guide, the inability to require higher worker pension contributions or diminished benefits could mean an even bigger tax increase down the road. That’s what happened when an adverse court ruling left Emanuel and the City Council looking for ways to fix four city worker pension funds.

When the Park District pension legislation was enacted, it had buy-in from some unions, and Emanuel repeatedly cited it as an example of the city and unions agreeing on a way to restore financial health to an underfunded pension systems.

But then the courts struck down city worker pension changes, based on an Illinois state constitutional clause that states public pension benefits "shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired." After initial rulings in that case, which later was upheld by the Illinois Supreme Court, the district workers filed their lawsuit.

San Diego County sues pension fund to implement new benefit formula

San Diego County has sued the county pension plan to force it to lower benefits for new, non-safety employees hired on or after July 1.

In a lawsuit filed on April 17 at a California trial court in San Diego, the county wants the court to order the $12.4 billion San Diego County Employees Retirement Association to implement a new benefit formula — called Tier D — without the county first obtaining legislative approval of the formula as required by state law.

Under the new benefit formula adopted by the San Diego County Board of Supervisors on Jan. 9, the pension benefit for non-safety employees hired after July 1 would be based on 1.62% of their final annual salary for every year of county employment, down from 2.3%. The new rate would result in a gradual long-term reduction of the county's contribution rate to 6.02% from 8.27% under the current plan, according to minutes of the pension fund board's Jan. 9 meeting that is attached to the complaint. The new tier is not expected to have an impact on SDCERA's unfunded liability.

The county argues that an earlier 2006 state law preapproved the Tier D formula. SDCERA officials argue that under another state law, the 2013 pension reform act, the state Legislature still has to approve a new formula.

"SDCERA has a fiduciary duty to administer the plan according to the law … By requiring the county to satisfy all the requirements of PEPRA (California Public Employees' Pension Reform Act) prior to implementing Tier D, SDCERA is following its constitutionally mandated duty to the plan and its members and beneficiaries," SDCERA said in a written statement. "SDCERA's fiduciary responsibilities require it to insist upon full compliance with PEPRA before it can lawfully administer Tier D."

SDCERA will respond to the county's complaint and "looks forward to resolution of this issue," according to the statement.

WHEN A CITY GOES BROKE; PENSIONS, RETIREES AND MUNICIPAL BANKRUPTCIES

In recent years, a significant number of cities, towns and other municipalities in the United States have found themselves increasingly unable to pay their debts, according to Kevin M. Lewis, Legislative Attorney. In order to offer municipalities relief from many types of debts they cannot repay, Chapter 9 of the Bankruptcy Code authorizes certain municipalities to file for bankruptcy. However, filing for bankruptcy may adversely affect the municipality's creditors, especially beneficiaries of underfunded municipal retirement plans (who, along with bondholders, often hold "the lion's share" of a municipality's financial obligations). Because a number of municipalities face a "dramatic and growing shortfall in public pension funds," many "firefighters, teachers, police officers, and other public employees" who purportedly have "a right to pension benefits at retirement" face a significant risk that their pensions will ultimately not be fully repaid.

The fact that public pensions, unlike their private counterparts, are neither subject to the "vesting and funding rules imposed by" the Employee Retirement Income Security Act of 1974 nor "protected by the federal pension guarantee program operated by the Pension Benefit Guaranty Corporation" could, according to some commentators, further exacerbate that risk. Moreover, because courts presiding over municipal bankruptcy cases have generally been "amenable to modifying pension debt in bankruptcy," retirees' pension benefits may potentially be significantly curtailed when a municipality declares bankruptcy. Although many Chapter 9 debtors have ultimately opted not to cut pensions "for political or practical reasons," courts and commentators generally accept that, under certain circumstances, municipalities "have the legal ability to shed pension debt" in bankruptcy if they so choose. Under current bankruptcy law, Chapter 9 debtors have significant freedom to modify their outstanding pension obligations through the bankruptcy process.

There are proposals to alter the legal principles governing the adjustment of municipal pensions in bankruptcy. Background on Municipal Bankruptcy Chapter 9 of the Bankruptcy Code authorizes municipalities to file for bankruptcy if they satisfy certain eligibility requirements. A Chapter 9 case is designed to culminate in "a plan for the adjustment of the debtor's debts" that alters the financial relationships between the municipality and its creditors. Chapter 9 thereby affords a subset of municipal debtors relief from many types of burdensome debts so that they may continue to provide certain services that have been viewed as "essential" to their residents, like police protection, fire protection and garbage removal. Filing for bankruptcy under Chapter 9 confers many benefits upon a municipal debtor. Most relevantly, Section 365 of the Bankruptcy Code generally gives a Chapter 9 debtor the power to reject an "executory contract"—that is, a contract that the parties have yet fully to perform—subject to the bankruptcy court's approval. Rejecting a contract under Section 365 effectively constitutes "a court authorized breach" of the agreement that generally "free[s] [the debtor] from future performance under the rejected contract." "The claims arising from this breach" are then generally "subject to compromise in bankruptcy" pursuant to a Chapter 9 plan that modifies the debtor's obligation to pay those claims. This authority to reject executory contracts "is a particularly powerful tool" because it allows the debtor to effectively "disavow" certain contracts "that it no longer wishes to maintain." One such contract could be a municipality's commitments to provide pension benefits to its employees.

Pensions in Municipal Bankruptcy

As noted above, "many municipal debtors" face "overwhelming and seemingly unassailable pension obligations." However, several bankruptcy courts presiding over high-profile municipal bankruptcies (such as the Chapter 9 cases filed by the City of Detroit and the City of Stockton) have agreed that a municipality's pension obligations "may be adjusted as part of a chapter 9 plan" by using Section 365's rejection power described above. As a result, filing for bankruptcy under Chapter 9 thereby "provide[s] a means of reducing the unfunded liability portion of a municipality's pension obligation or otherwise compromising a municipality's pension debt." That is not to say that "public pensions can be rejected or unilaterally modified willy-nilly," however. Some bankruptcy courts, most notably the court presiding over the City of Stockton's Chapter 9 case, have stated that a court must "balance the interests of the affected parties—debtors, creditors and employees"—to determine whether a debtor may permissibly "us[e] chapter 9 to force changes in municipal pension plans." Specifically, the bankruptcy court "must consider the consequences of the alternatives" to adjusting the municipality's pension obligations "on the debtor, on the value of creditors' claims and any ensuing hardship and the impact on employees.

The court also must consider the degree of hardship faced by each party and must consider any qualitative differences between the types of hardship each may face." Moreover, even when a bankruptcy court might otherwise be inclined to permit a municipality to adjust its pension obligations, "political or practical" concerns may nonetheless deter municipalities from using Chapter 9 to adjust their pension obligations. "For example, it may be politically unpopular to treat debts owed to public workers in the same manner as sophisticated commercial lenders, or it may be difficult to continue the essential work of the city if employees feel that their employer's promises cannot be trusted." The fact remains, however, that municipalities potentially "have the legal ability to shed pension debt." Possible Considerations for Congress Given that multiple bankruptcy courts have concluded that the Bankruptcy Code gives Chapter 9 debtors significant (albeit not unlimited) power to modify their pension obligations, commentators have debated whether current bankruptcy law correctly balances the competing interests of debtors, retirees, and other creditors. Some have argued that municipalities presently enjoy too much freedom "to set aside collective bargaining agreements and retiree protections" to the detriment of workers "who have devoted their lives to public service."

Others, by contrast, have cautioned that affording pensioners favorable treatment in municipal bankruptcy cases could make lenders—who often "battle [with] retirees over the municipality's scarce resources" in Chapter 9 cases—"more wary about loaning money to struggling cities," which could, in turn, "increase borrowing costs for cities already in debt." Responding to this debate, some Members of the 115th Congress have introduced bills that would change how pensions are treated in municipal bankruptcy cases. For instance, the Protecting Employees and Retirees in Municipal Bankruptcies Act of 2017 (H.R. 139) aims to "strengthen protection for employees and retirees under chapter 9 municipality cases" by (among other things) (1) making it harder for debtors to modify pensions and other retiree benefits over the objection of retirees and employees; and (2) imposing stricter eligibility requirements upon would-be Chapter 9 debtors, thereby narrowing the universe of municipalities that are eligible to modify their pension obligations through the bankruptcy process. As of the date of this publication, the bill is pending before the House Judiciary Committee's Subcommittee on Regulatory Reform, Commercial & Antitrust Law.

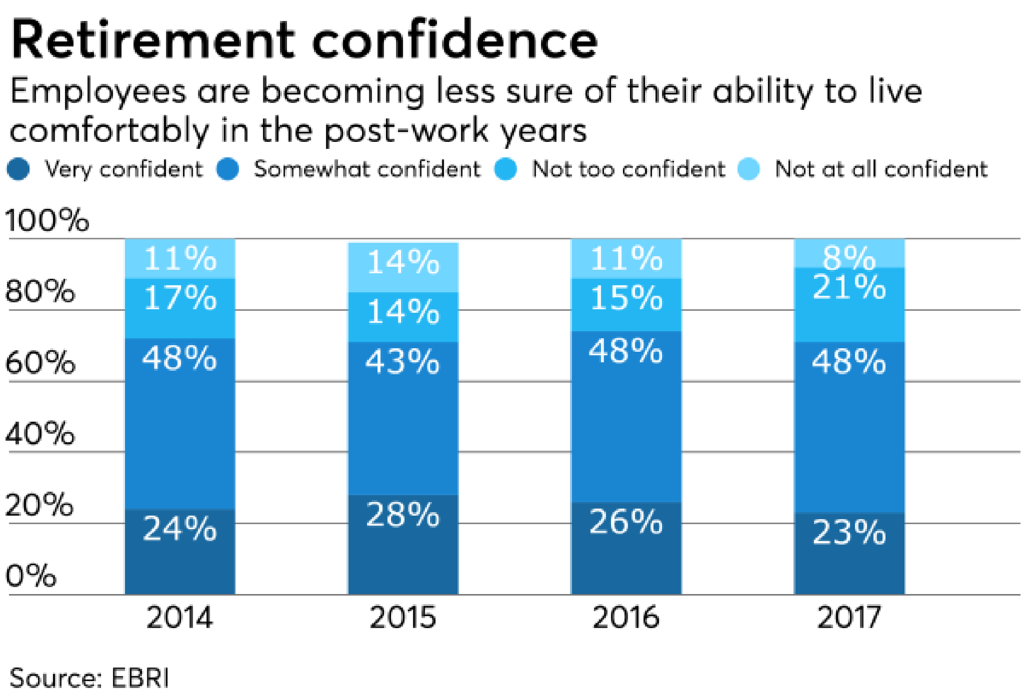
Private Sector

Defined benefit plans are showing new signs of life

Advisers and plan sponsors who have written off the defined benefit plan as a relic of the past may want to reconsider. While the number of participants in DB plans has declined somewhat in recent years, the number of DB plans has been rising.

Specifically, the number of single-employer DB plans with fewer than 100 participants rose for the third consecutive year in 2015, up 2% from 2012, according to recently published data from the Department of Labor’s Employee Benefits Security Administration (EBSA). The growth rate was more robust among plans with at least 100 participants, rising by 4% with four consecutive years of growth. Total participant head count for single employer DB plans stood at around 270,000 in 2015, per the EBSA data.

Although defined contribution plans have also been growing over the same period, and their total numbers dwarf the DB market, the number of DC plans hasn’t been growing any more rapidly.



One reason, says John Lowell, a partner with the October Three actuarial consulting firm, is that the rate of DB plan termination has slowed. “A lot of the larger plans have been doing risk transfers to insurance companies,” he explains.

By shifting funding liability to carriers, sponsors haven’t felt the urgency to pull the plug on those plans. With fewer terminations to statistically offset the creation of new DB plans, the result is net growth for the category.

Another factor that comes into play, Lowell says, is increased regulatory relief for stressed DB sponsors. This too has eased any pressure to terminate those plans.

Yet another contributor to the uptick in DB plan sponsorship is a delayed effect of the Pension Protection Act (PPA) enacted a dozen years ago. Cash balance plans, a DB hybrid design, were allowed to credit participants’ notional accounts based on investment returns actually achieved by the underlying pension portfolio. That change removed an element of risk for cash balance plan sponsors, says Lowell.

High contribution limits

Contribution limits for conventional DB plans are based on the dollars required to fund the highest allowable pension benefit at retirement. That means, for example, that a 50-year-old who could afford it might be able to put $147,000 aside in a DB plan in one year. Even a 40-year-old could set aside approximately $88,000, by Lowell’s calculations.

When employers have both a DB and a DC plan, the opportunities for owners and executives to set aside tax-deferred funds are even greater. And as long as contributions of 7.5% of compensation are made on behalf of lower paid employees, “you don’t need to worry about ERISA anti-discrimination tests,” Lowell says.

Independent pension consultant Robert C. Lawton reports that small profitable companies with small ownership groups often turn to DB plans as a source of tax deductions, as much as a vehicle for retirement funding. This often occurs after they have already contributed the maximum allowable amounts to a DC plan. Medical practices and law firms, for example, are often good candidates for a DB plan.

One knock on DB plans is that they are more expensive to set up and administer than 401(k) plans. For that reason, Lawton only encourages companies whose key executives plan to stay together for a relatively long period of time to consider a DB.

Some DB plan sponsors incur greater costs than they need to. Specifically, Pension Benefit

Guaranty Corp. (PBGC) premiums--often the highest administrative cost of a DB plan—can avoid being required to pay variable risk-based premiums and pay lower fixed PBGC premiums instead. A study by October Three outlined a number of “best practices” DB plan sponsors can adopt to reduce their PBGC premium and tax burdens.

“The PBGC premium burden remains a major threat to effective pension management,” the report states. Other tactics, such as making funding contributions by September 15 to generate tax savings that “can be worth almost four times as much as the premium savings themselves,” are also outlined in the report.

Headcount reduction and “split plan” strategies can also contribute substantial savings, the report states. Knowledge of such techniques, disseminated by advisers, could further contribute to the growth of DB plans.

DOL increases fines, conducts fewer retirement plan audits

The Department of Labor’s Employee Benefit Security Administration — the division that regulates and enforces policies that protect employee retirement plans — is recovering more from missing employee contributions to retirement plans despite conducting fewer audits last year.

EBSA recovered more than $1.1 billion in missing employee contributions in the latest government fiscal year, which ended Sept. 30, 2017, compared to $777.5 million in total recoveries in fiscal year 2016.

EBSA slightly reduced the number of cases it closed in fiscal year 2017 compared to the year before. In fiscal 2017, it closed 1,707 cases with 1,114 civil cases closed “with results” or monies recovered, 134 civil investigations referred for litigation, and 50 civil cases where litigation filed. In fiscal 2016, EBSA closed 2,002 civil investigations with 1,356 of those cases (67.7%) In 2017, fewer cases — 65.3% — closed with monetary results for plans. In DOL-provided figures for the past five years, EBSA reached a peak of 3,928 civil cases closed in 2014.
EBSA has been able to achieve these higher fines with fewer audits mainly due to two factors, according to EBSA experts and attorneys who represent retirement plan sponsors. One is an increase in the amount for fines. The other is EBSA’s use of data algorithms that can scour Form 5500s, the benefit documentation that employers must provide to the government, and other sources (such as filings for bankruptcy, news reports of companies going out of business and complaints from plan participants) to find discrepancies that raise red flags for an audit, according to EBSA.

EBSA conducts ERISA audits of employee retirement plans for a variety of reasons. The team of auditors and investigators look for missing funds, ensure that a recently closed business is still offering retirement benefits to former employees, that employers have made every "reasonable" effort to find employees that have moved or changed their names so that they can receive their retirement funds, or to inspect the status of current retire plans. The investigation can focus on the employer, the plan administrator, and in some cases both parties depending on the scope of the inquiry.

"We are trying to get the money back to the employees," says a Department of Labor spokesperson.

Of the 2017 $1.1 billion recovery figure, $682.3 million was recovered from enforcement actions, $418.7 million came from what DOL calls "informal complaint resolution," $27.9 million were part of EBSA's Abandoned Plan Program, and $10 million from EBSA's Voluntary Fiduciary Correction Program, which allows employers to avoid ERISA penalties if they comply with regulators.

See also: ERISA class action settlements reach $1.1 billion
The DOL fines have also increased. Starting Aug. 1, 2016, the penalty for a business that fails to furnish statement of benefits to former plan participants rose from $11 per employee to $28 per employee. Failure or refusal to file an annual Form 5500 benefit report climbed from $1,100 per day to $2,063 per day.

Along with the 14 other upgraded DOL fines, the largest penalty is for employers that prohibited payment from DB plan during the period when the plan has a liquidity shortfall. It rose from $10,000 per prohibited payment to $15,909.

Triggering an audit
The EBSA division employs two teams to look into potential ERISA violations: so-called "benefit advisers" that look into possible irregularities and investigators who conduct the actual investigation into suspected malfeasance. (These "benefit advisers" is an in-house term used by EBSA and they are not to be confused with the benefit advisers who sell and establish insurance plans for employers).

The size of the company offering the retirement plan does not matter. According to ERISA experts, an audit can be random or targeted, and can cover Fortune 100 companies to small businesses with as few as two employees. If a company has a retirement plan and a healthcare plan with benefits, that company is a candidate for review of its books by the U.S. government.
However, according to a regional EBSA director who works on ERISA audits in the Northeast,

the number of audits is actually diminishing. “We are opening fewer cases and trying [them]. What we discovered over the years is we need to be smarter in how we investigate cases and make sure what we are doing is impactful,” says an EBSA regional office director. For this story, the DOL asked that he not be named.

A DOL spokesman says the agency is focused on recovering funds for the plan, not on fining the plan, per se. “The desired outcome is never a civil suit, unless it is absolutely necessary. If we can get something corrected informally it is to everyone's benefit. If there is an obvious crime, then yes, of course,” says a DOL spokesman.

That said, the DOL is emboldened to cast a wider investigatory net thanks to access to data from Form 5500s and now that it is auditing plan administrators as well. According to Thomas E. Clark Jr., an ERISA attorney for the Boston-based Wagner Law Group, EBSA investigators no longer have to search plan by plan; by investigating plan sponsors they can see the documents on hundreds of employer retirement plans at a time.

“They have algorithms and software that sifts through the data and looks for bell curves, really crazy statistician stuff, and they are already crunching numbers with the 5500s,” says Clark. He adds that if the numbers do not add up — such as an interruption in employer contributions to a retirement fund — that employer will be audited.

The DOL declined to discuss in detail its algorithms and other software.

Clark adds sometimes an error is so obvious that the DOL doesn’t even need an algorithm to spot a “red flag.” If an employer has been late two years when it comes to contributing to a retirement plan, for example, they can pretty much guarantee an audit because they are doing something wrong, he says. “Today I can send you $10,000 with my iPhone if I had to. There is no reason you can’t get payroll money to the 401(k) provider these days. It’s a click of a button in an internet browser.”

These DOL innovations as well as updating reporting requirements for service provider fees and expense information is a clue of the direction the DOL is taking.
“I see this all as just part of one big arc of the DOL redefining itself for the new century and redefining their mission and figuring how they can help the constituents that they are asked to support,” Clark says. “Not just enforce the law, but they truly believe that they’re helping the people in the ERISA plans that they regulate.”

What to Do with Missing Participants and Required Minimum Distributions

These days, problems related to missing and nonresponsive retirement plan participants are causing more problems and creating more uncertainty for plan sponsors and administrators.

For example, Lines 4l of Schedules H and I of Form 5500 and line 10f of Form 5500-SF ask, "Has the plan failed to provide any benefit when due under the plan?" When retirement distribution checks – including required minimum distributions (RMDs) – are returned uncashed because a participant can't be found, the plan is deemed to have failed to provide the benefit.

Originally, IRS instructions in connection with the 2015 and 2016 Form 5500 and Form 5500-SF included unpaid RMDs to 5% owners age 70½ and over and non-5% owners age 70½ and over who have retired or separated from service as reportable failures.

But hold your horses. In response to comments received after issuing a Paperwork Reduction Act notice regarding the 2016 Form 5500 and Form 5500-SF, the IRS has since offered clarification. Specifically, the agency announced that in the absence of other guidance, filers do not need to report unpaid RMD amounts (on Lines 4I of Schedules H and I on Form 5500 and 10f on Form 5500-SF) for participants or their beneficiaries who meet the following criteria:

- Retired or separated from service
- Cannot be located after reasonable search efforts
- The plan has begun making reasonable efforts to locate the participants or beneficiaries at the end of the plan year reporting period

Recommended Search Procedures

The Department of Labor's (DOL) Field Assistance Bulletin (FAB) 2014-01, which outlines recommended search procedures for missing participants, specifically applies to terminated defined contribution (DC) plans. However, the IRS website states that employers and plan administrators of ongoing plans may want to consider periodically using one or more of the search methods described in the FAB, as this can provide evidence of making a reasonable effort to locate RMD-eligible missing participants.

The DOL FAB 2014-01 reminds us that the employer has a fiduciary duty to attempt to locate missing participants, and that 100% withholding is not permitted. Plan administrators and employers should also review their plan documents for written procedures on locating missing participants. The DOL recommends the following steps when searching for a missing participant:

1.Use Certified Mail. Certified mail is an easy way to find out, at little cost, whether the participant can be located in order to distribute benefits. Do not use the DOL model notice because it states that the funds from the terminating DC plan will be rolled to an IRA, which is not permitted with RMDs.

2.Check Related Plan and Employer Records. Other types of employer plans, such as a group health plan, may contain more up-to-date information. Plan fiduciaries can ask representatives from other plans to search their records to determine if there is a more current address available. When privacy concerns arise, a fiduciary can ask a provider to forward a letter to the missing participant or beneficiary. The letter would request that the missing participant or beneficiary contact the searching plan fiduciary.

3.Check With the Designated Plan Beneficiary. A plan fiduciary must try to contact individuals named by the missing participant on his or her beneficiary form to obtain updated contact information. If privacy concerns arise, the fiduciary can request the designated beneficiary contact to forward a letter to the missing participant or beneficiary.

4.Use Free Electronic Search Tools. Plan fiduciaries must make reasonable use of free Internet search tools, such as search engines, public record databases (such as those for licenses, mortgages and real estate taxes), obituaries and social media. The National Registry of Unclaimed Retirement Benefits, a nationwide listing of unclaimed retirement plan account balances, offers a free search tool for employers, employees and service providers looking to conduct searches.

Keep in mind that the FAB's concept of rolling terminating DC plan funds to an IRA is not available for the processing of missing participant's RMDs, as RMDs are not eligible for rollover.

Optional Additional Search Methods

If none of the above result in locating the missing participant, optional search methods are provided in the FAB. Before using these methods, fiduciaries must compare the costs of such services against the value of the participant account, as they may charge reasonable expenses to the account. Optional search methods include commercial locator services, credit reporting agencies, information brokers, investigation databases and analogous services that may involve charges.

Searching for missing participants can be a time-consuming activity that often fails to achieve the desired results. However, it can absolve you of the requirement to report unpaid RMDs for missing participants, and provide evidence that you are making a reasonable effort to uphold your fiduciary responsibility.

Updated IRS Guidance for Employee Plan Examinations Provides a Safe Harbor

In October, 2017, IRS Acting Director of Employee Plans Examinations Thomas J. Petit issued a memorandum that provides much-needed clarification and authoritative relief from a retirement plan’s liability for not paying an RMD for a missing participant,

Entitled “Memorandum for Employee Plans (EP) Examinations Employees,” the memorandum provided similar guidance to the IRS website for EP examiners to rely on when auditing qualified plans. According to the memo, the plan is not subject to a 401(a)(9) violation if it has taken the following steps:

Attempted to contact the missing participant (via United States Postal Service certified mail) to the last known mailing address and through appropriate means for any address or contact information (including email addresses and telephone numbers)

Searched through appropriate means for any address or contact information (including email addresses and telephone numbers)

Searched plan and related plan, sponsor, and publicly-available records or directories for alternative contact information

Used any of these search methods:

Commercial locator service

Credit reporting agency

Proprietary internet search tool for locating individuals

If a plan has not completed the steps above, EP examiners may challenge a qualified plan for violation of the RMD standards for failure to commence or make a distribution to a participant or beneficiary to whom a payment is due. Note that in February 2018, the IRS issued a memorandum with identical safe harbor steps to locate missing participants who are due

RMDs from a 403(b) plan.

RMDs and missing participants aren't going away any time soon, so why run the risk of a 401(a)(9) violation to your plan? Although a bit laborious, these search steps are not difficult. If you don't have the time or personnel, you can always outsource them to service providers like PenChecks Trust who specialize in missing and nonresponsive participant searches. And the cost of these services can be charged to the account.

As someone who has worked with many plans to defend a 401(a)(9) violation, I consider the ability to avoid this situation by conducting a few simple search steps to be real authoritative relief.

PBGC Pays Out $5.6 Billion to Retirees of Failed Plans in 2017

Total amount paid remains the same as the number of retirees rises.

The Pension Benefit Guaranty Corporation (PBGC) reported that in 2017, it paid out more than $5.6 billion to 868,000 retirees in failed, single-employer plans in all 50 states and US territories.

The PBGC, which is the government-sponsored lifeboat for struggling pensions, noted that the amount paid has remained the same over the past three years, while the number of retirees receiving the benefits has risen. In 2016, the agency paid out approximately $5.6 billion to nearly 861,000 retirees in failed plans, while the same amount was paid to 840,000 retirees in 2015.

For the second straight year, Ohio, Pennsylvania, and Florida had the most benefits paid. Retirees in failed plans in those states alone accounted for more than $1.4 billion, or 25% of all benefits paid out by the PBGC.

In 2017, the PBGC paid 78,109 Ohio retirees $543.9 million, compared to the $557 million paid to 78,929 Buckeye retirees in 2016. It paid 79,325 Pennsylvania retirees $462.2 million, versus last year, when it paid just under $465 million to 79,687 Keystone state retirees; and it paid a little under $419 million to 58,740 Florida retirees in 2017, only slightly up from the 57,874 Sunshine State retirees who received $414.9 million in benefits the previous year.

Following Florida was Michigan, which had 48,852 retirees receiving $397.6 million; California, which had 44,247 retirees being paid $351.3 million; New York, which had 51,871 retirees receiving $339.9 million; and Illinois, where 43,698 retirees were paid $304.6 million. The PBGC also paid $290.8 million to 33,082 Indiana retirees in failed plans, and $202.1 million to 43,400 North Carolina retirees.

Combined, the top nine states receiving benefits accounted for $3.2 billion, or nearly 60% of all the benefits paid by the PBGC last year.

According to the agency, the total number of PBGC-insured single-employer pension plans has declined to approximately 22,500 from 112,208 in 1985; it also covers about 27.5 million people, as opposed to 28.4 million people in 2016. The PBGC said it is likely this decline will continue as sponsors are increasingly interested in so-called risk transfers, where retirees are offered lump sums or annuities, instead of lifetime income, or benefits are frozen and new entrants barred.

Although the PBGC projects the agency's multiemployer program (run by unions) will run out of money by the end of 2025, it expects the single-employer program, whose deficit shrank to $10.9 billion in 2017 from $20.6 billion the previous year, will turn into a surplus over the next 10 years.

Court Affirms DB Plan Sponsor Owes Excise Taxes on Non-Deductible Contributions

A federal appellate court agreed with the Commissioner of Internal Revenue that Pizza Pro Equipment Leasing incorrectly calculated the limitation on the plan's annual benefit and therefore made non-deductible contributions to the plan.

The 8th U.S. Circuit Court of Appeals has affirmed a tax court's decision that Pizza Pro Equipment Leasing owes excise taxes and additions to tax related to its defined benefit (DB) plan.

The Commissioner of Internal Revenue concluded that from 2002 to 2006, Pizza Pro incorrectly calculated the limitation on the plan's annual benefit and therefore made non-deductible contributions to the plan. The Commissioner charged the plan an excise tax of 10% of the non-deductible contributions and then imposed additions to tax for Pizza Pro's failure to file a return of excise taxes and timely pay the excise tax.

The appellate court noted that, in finding that the plan's annual benefit exceeded the applicable limitation, the tax court applied a Treasury Department regulation that states a plan benefit beginning before the normal retirement age is adjusted to the "actuarial equivalent" of a benefit beginning at normal retirement age. According to the 8th Circuit's opinion, Pizza Pro has not challenged the validity of this regulation.

Because the regulation does not define actuarial equivalence, the tax court looked to general practice in the field of actuarial science to determine the proper method for determining the limitation on the annual benefit. It found that the Commissioner's report, which was prepared by an actuary, was in line with actuarial practice, while Pizza Pro's report, not prepared by an actuary, was not. The appellate court agreed with this.

The 8th Circuit also agreed that Pizza Pro did not make an election under Internal Revenue Code Section 4972(c)(7), which says, "in determining the amount of non-deductible contributions for any taxable year, an employer may elect for such year not to take into account any contributions to a defined benefit plan except to the extent that such contributions exceed the full-funding limitation." Pizza Pro points out that two actuarial groups suggested to the Internal Revenue Service (IRS) that a taxpayer's failure to file the excise tax form should be considered sufficient evidence that it made such an election, but the appellate court noted that the IRS did not adopt this suggestion and the 5th U.S. Circuit Court of Appeals rejected a similar argument in a different case.

The 8th Circuit agreed with the Commissioner of Internal Revenue's conclusion that Pizza Pro's failure to file the form stemmed from its belief that it made no excess contributions and owed no excise taxes.