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Employee Benefits Update

Identity theft threat puts plan participants and sponsors at risk

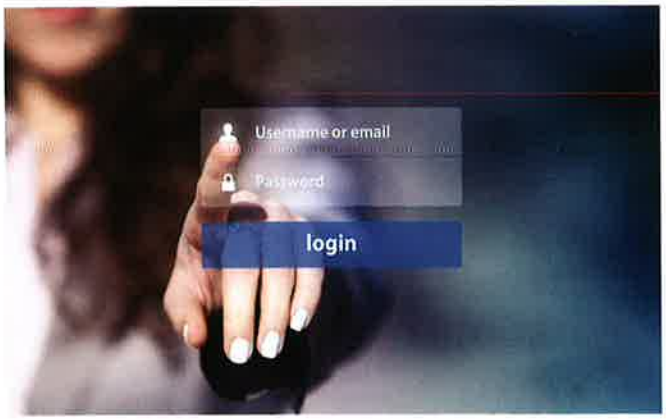
News of commercial database hackings involving millions of people's personal information seems commonplace. While many of these stories focus on bank and credit card accounts, many plan sponsors and participants don't realize that 401(k) plan assets may be at risk. Now isn't the time to let your guard down.

This can be a problem not only for participants, but sponsors as well. While no sponsor wants to see participants sustain financial hits, depending on how a cyber-theft unfolds, sponsors could be left holding the bag.

Importance of monitoring

Sponsors should not only take precautions from their end, but regularly educate and warn participants about safety measures they should be taking. Participants' infrequent monitoring of what's happening in their 401(k) accounts (at least compared to their bank accounts) makes these accounts vulnerable. Indeed, sometimes they're even encouraged to not worry about short-term fluctuations and volatility in their retirement accounts, and instead focus on the long run.

However, regular monitoring of accounts by participants is important. For example, one identity theft case tells the story of a plan participant who divorced his wife and moved out of the house, but didn't update his address with the plan administrator or review his account. In the meantime, his ex-wife cleaned out his more than $42,000 balance.



Plan sponsors must perform strict due diligence in assessing plan service providers' cyberfraud protection systems.

She managed to hijack the account after opening mail from the plan administrator addressed to her ex-husband and making a fraudulent password change enabled by confidential information contained in the purloined letter. The dispute was over whether the plan administrator could be held liable for the theft. The court ruled that the participant had to suffer the consequences of his failure to inform the plan of his change of address, as required by the plan and well documented in the summary plan description (SPD).

Limits of protection guarantees

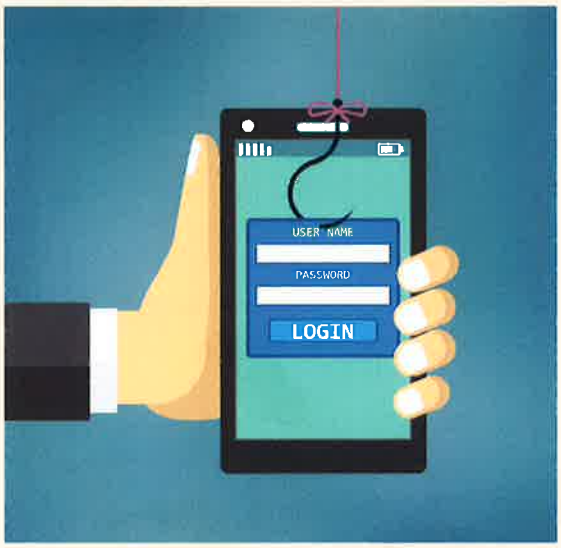
It's also critical for sponsors and participants not to be lulled into a false sense of security by plan service providers' customer protection guarantees. Be sure you and your participants understand the caveats that go with them. For example, one large bundled retirement plan service provider issues a broad warning that the company will "reimburse you for losses from unauthorized activity in covered accounts," but only when "occurring through no fault of your own."

What does that mean? For starters, the company, reasonably, assumes no responsibility for transactions on behalf of the participant carried out by the participant's own financial advisor. Those are deemed to have

Action steps for participants to avoid fraud

Besides monitoring their account regularly, what precautions should plan sponsors encourage their participants to take to safeguard their retirement savings from loss by hacking? Participants should take the same steps they use to protect other accounts accessible on the Internet, including:

- **Using strong passwords and changing them regularly,**
- **Not using the same log-in ID and passwords for multiple websites,**
- **Taking advantage of two-factor authentication for account access,**
- **Rejecting the option of having the Internet browser memorize login information, and**
- **Never sharing login information.**



While participants have probably read these kinds of pointers many times, hearing that they're vital to protect their retirement plan accounts might come as a surprise to some. Make this a regular part of your participant education.

been authorized by the participant — whether they were or not.

Participants must also "adopt [the service provider's] recommended security practices," as outlined on the firm's website. Those include checking account information "frequently" and reviewing correspondence from the administrator "promptly" but "no later than 30 days after that information is posted to your account or delivered to you."

In addition, the service provider reserves the right to determine the "applicability" of its customer protection guarantee "based on the facts of your situation." All of these combine to greatly limit the advisor's liability. Be sure to communicate this with your participants.

Role of sponsors

Plan sponsors also need to protect themselves from negligence on the part of participants. As noted in the case of the participant whose ex-wife stole his account balance, the plan sponsor wasn't held liable for the loss, thanks to its clear articulation of participants' obligations in the SPD. Review your SPD with your benefits specialist to make sure you're not left holding the bag in this type of situation.

Finally, sponsors must perform strict due diligence in assessing plan service providers' cyberfraud protection systems. This includes reviewing your own internal safeguards against plan administrative staff practices that could open the door to a breach.

Rewards of diligence

Without adequate vigilance, anybody can be a few clicks away from a retirement plan wipeout. Being prepared and diligent in reviewing your plan documents and educating your participants about their responsibilities for monitoring their accounts will help avoid losses and litigation for all parties. ◻

Fiduciary rule's tortured path to implementation

What this means for plan sponsors

Controversy, complicated legal wrangling and legislative maneuvering have been swirling around the Department of Labor's (DOL's) "fiduciary rule" governing financial advice given to retirement plan participants for years. Delays, modifications, phased effective dates, and the involvement of the Securities and Exchange Commission have left confusion and headaches in their wake. But essential elements are falling into place. Here's a brief review of what plan sponsors need to know.

Start date

July 1, 2019, is the current projected deadline for full implementation of the rule. Based on the path this rule has taken, some changes could be made between now and then.

At its core, the fiduciary rule requires that financial advisors act, as retirement plan fiduciaries must, in the best interests of those they are advising.

Opponents of the fiduciary rule who have been successful in delaying its implementation have warned that its upshot will be an exodus of brokers from the business of working with retirement plan participants. This may be true for advisors associated with small broker/dealer firms.

Brokers vs. RIAs

The fiduciary rule fundamentally governs the behavior of investment professionals in their dealings with retirement plan participants. This means that plan sponsors must understand the regulatory requirements covering such advisors. You'll need to determine whether any investment professionals providing information to your

participants meet the new regulations, and make sure participants are clear about the status of such advisors.

At its core, the fiduciary rule requires that financial advisors act, as retirement plan fiduciaries must, in the best interests of those they are advising. Investment advisors who work with relatively large retirement plans and their participants typically are registered investment advisors (RIAs). An RIA's compensation isn't based on selling investments to the plan or its participants. RIAs were minimally impacted by the fiduciary rule because they're already required to act in a fiduciary capacity.

Commission-based brokers, in contrast, will need to make some changes. Generally, advisors paid on a commission basis are thought to be financially motivated to recommend investments that pay the biggest commissions, which may or may not be in retirement investors' best interest. To work with retirement plan participants, commission-based brokers require an exemption from the fiduciary rule that would otherwise prevent them from doing so. It's known as a best interest contract exemption (BICE) agreement. Under a BICE agreement, brokers/advisors attest that, notwithstanding a theoretical conflict of interest with retirement plan participants, they'll still look out for participants' best interests.

Plan sponsor obligations

So what should plan sponsors have already done or do soon? First, know the regulatory status of financial advisors who work with you and interact with your plan participants. If the advisor is an RIA, your life is simpler. If the advisor's a broker/dealer, you'll need to make sure you obtain a BICE agreement. Before any interactions with the advisor, you and participants should read it carefully and sign the part in which you acknowledge that you have read it, understand it and accept its terms. This will give participants an important lens through which to consider any guidance the advisor gives.

Watch out for advisors providing plan asset distribution option recommendations to participants. A frequent practice that the fiduciary rule intends to curtail is having advisors recommend that participants roll their account balances into an IRA the advisor would manage, possibly using mutual funds with much higher fees than those in the 401(k) plan. If this were to occur and the participant harmed by it, he or she might be able to sue the plan. The rule sets an "impartial conduct standard" that, if satisfied, clears the way for advisor-recommended rollovers.

Finally, determine whether your plan's recordkeeper is affected by the rule. The key is whether any investment education services or materials the recordkeeper furnishes participants stray into the investment advice territory. If so, the recordkeeper might need to satisfy the fiduciary rule's requirements. The same applies to your own internal staff's interactions with plan participants.

The time is now ... really

Many employee benefit plans have watched the progress of this rule over the years. Whatever the ultimate fate of the fiduciary rule, it's important for plan sponsors to understand whether the advisors who are guiding them are acting in a fiduciary capacity or not, and assess their recommendations in light of their status. Be sure to consult with your benefits and legal advisors to confirm you comply with the rule. ◻

Compliance Alert

Upcoming compliance deadlines:

2/15 Quarterly benefit statements due for defined contribution plans with calendar year plans

2/28 Deadline for filing paper 2017 Form 1099 with IRS (electronic filing deadline is March 31)

3/15 Deadline for making corrective distribution for failed 2017 actual deferral percentage (ADP) / actual contribution percentage (ACP) tests without 10% excise tax penalty

3/15 Deadline for filing 2017 partnership tax return and making contributions eligible for deductibility without extension

4/1* Deadline for taking first required minimum distribution for participants attaining age 70½ or retiring after age 70½ in prior year

4/17** Deadline for corrective distribution of 2017 402(g) excess deferral failures

4/17** Deadline for filing 2017 individual and/or corporate tax returns and making contributions eligible for deductibility without extension

** The due date of April 1, 2018, falls on a Sunday. The IRS historically hasn't extended due dates for required disclosures, contributions or distributions.*

*** This date reflects an extension of the normal deadline, which falls on a Sunday this year, and includes Emancipation Day in Washington, D.C., on April 16.*

Tax cut law a mixed bag for retirement plan sponsors

Despite early indications that Congress was prepared to do much more, the Tax Cuts and Jobs Act (TCJA) that was passed in December largely left retirement plans unscathed, save for changes pertaining to plan loans and IRA conversions. Here's a quick review of areas that are affected, as well as what could be ahead.

Plan loan relief

The new law gives a break to plan participants with outstanding loan balances when they leave their employer. Ordinarily, participants with outstanding loans who fail to make timely payments after their separation from the employer are deemed to have received a distribution in the amount of that outstanding balance. Under pre-TCJA law, they could, however, roll that amount (assuming they have sufficient funds available) into an IRA without tax penalty if they do so within 60 days.

Under the TCJA, beginning in 2018, former employees in this situation will have until their tax return filing due date (including extensions) to move funds equal to the outstanding loan balance into an IRA or qualified retirement plan without penalty. They're given the same opportunity if they're unable to repay a loan due to the plan's termination.

Roth IRA recharacterization

The TCJA also restricts individuals' ability to recharacterize conversion contributions to a Roth IRA as if they were still making contributions to a traditional IRA. In other words, beginning in 2018, individuals can no longer convert a traditional IRA to a Roth IRA and then later recharacterize that Roth IRA contribution back to a traditional IRA contribution to essentially undo the conversion. However, taxpayers can still recharacterize new Roth IRA contributions as traditional contributions as long as they do it by the applicable deadline and meet all other rules.

While not immediately pertinent to plan sponsors, this provision may be a warning shot across the bow with respect to possible future restrictions on 401(k) plans. Roth 401(k)s are favored by revenue-seekers in Congress, because the after-tax nature of contributions to Roth plans — IRAs or 401(k)s — enables the federal government to collect more tax revenue in the present, pushing off into the future the drain on tax revenue due to the tax-free nature of withdrawals from Roth plans.

Beginning in 2018, former employees will have until their tax return filing due date (including extensions) to move funds equal to an outstanding 401(k) loan balance into an IRA or qualified retirement plan without penalty.

Higher costs for pass-through entities?

The American Retirement Association (ARA) expressed concern that the TCJA's tax-cutting features applicable to pass-through entities like S corporations could discourage 401(k) plan sponsorship. Specifically, allowing taxpayers to deduct 20% of qualified business income could make 401(k) plans, in effect, costlier to owners of S corporations on an after-tax basis, if they couldn't apply their tax deductions for their 401(k) contributions to their more highly taxed personal income instead of their qualified business income.

It's not clear, however, that increasing, by possibly a relatively small amount, the after-tax cost of maintaining a 401(k) plan to a business owner would warrant terminating a plan when weighed against other benefits to the business associated with sponsoring such a plan.

Looking ahead

The fact that several provisions detrimental to retirement plans made it to the debate stage and even into early drafts of tax reform bills could open the door to future efforts to restrict plans' tax benefits. The need for federal revenue will continue, with the government looking for places to collect that revenue.

One provision that cleared the Senate Finance Committee, but was ultimately dropped, would have required that all contributions to any defined contribution plan sponsored by the same employer (including mandatory employee contributions to a defined benefit plan) be aggregated when determining whether contributions to a participant's account satisfy IRC Sec. 415(c) limits. That change would have raised $1.7 billion over a 10-year period, the Committee's staff estimated.

Similarly, Congress considered imposing a low ($2,400) cap on pretax 401(k) contributions, requiring the balance of the total $18,000 limit on contributions to be made on an after-tax basis. Congress could revisit that concept and push employers to convert traditional 401(k) plans to Roth plans, if budget deficits balloon, the ARA warned, echoing the concerns also expressed by the American Benefits Council. ◻

2017 vs. 2018 retirement plan limits

Type of limitation	2017 limit	2018 limit
Elective deferrals to 401(k), 403(b) and 457(b) plans	$18,000	$18,500
Annual benefit for defined benefit plans	$215,000	$220,000
Contributions to defined contribution plans	$54,000	$55,000
Contributions to SIMPLEs	$12,500	$12,500
Contributions to IRAs	$5,500	$5,500
Catch-up contributions to 401(k), 403(b) and 457(b) plans	$6,000	$6,000
Catch-up contributions to SIMPLEs	$3,000	$3,000
Catch-up contributions to IRAs	$1,000	$1,000
Compensation limit for benefit purposes for qualified plans and SEPs	$270,000	$275,000
Minimum compensation for SEP coverage	$600	$600
Highly compensated employee threshold	$120,000	$120,000
Minimum income for "key employee" status for top-heavy calculation	$175,000	$175,000
Income subject to Social Security tax	$127,200	$128,700

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Our Story

We are committed to the success of our clients. As one of the largest California-based accounting and consulting firms, we have worked with plan sponsors and other fiduciaries to ensure their plans are fully compliant, for over 30 years.

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