TRANSAMERICA CENTER
FOR RETIREMENT STUDIES®

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TCRS 2015-01: Semi-Annual Summary of Regulatory Changes, Updates, and Guidance in 2015

This release summarizes certain regulatory changes, updates, and guidance (including court decisions) published during the first one-half of 2015. Following is a list of the topics summarized, as well as the sections of this release containing the summaries:

Section A: Change to the timing requirement applicable to annual participant fee disclosures under ERISA §404(c).
Section B: Changes and modifications to correction options for plan errors under the Internal Revenue Services' ("IRS'") correction programs.
Section C: Re-release of proposed fiduciary regulations by the Department of Labor ("DOL").
Section D: Guidance regarding hardship withdrawal and participant loan documentation.
Section E: Guidance regarding an on-going fiduciary duty to monitor plan investment alternatives.
Section F: Guidance regarding same-sex marriage.

Snapshot Summaries:

Section A: In March 2015, the DOL published a final rule regarding the requirement to annually provide a participant fee disclosure. To avoid a "creeping" deadline, the term "annually" (by which to provide annual participant fee disclosures) means at least once in any 14-month period. Prior to the final rule, the term "annually" meant at least once in any 12-month period.

Section B: In March and April 2015, the IRS and the Treasury Department published two revenue procedures that modified and/or expanded correction options under the Employee Plans Compliance Resolution System ("EPCRS"), which is a system of IRS correction programs for certain plan errors (currently described in IRS Revenue Procedure 2013-12).

One change included lowering the compliance fee under the Voluntary Correction Program ("VCP") to correct loan errors (basing the fee on the number of loans being corrected, versus the old method of using the number of participants in the plan). Another change expanded and modified correction options for late deferrals to a 401(k) or 403(b) plan with or without an automatic contribution arrangement (commonly referenced as an automatic enrollment feature). The changes/modification could result in no employer contributions, or reduced employer contributions, to correct the error.

Section C: In April 2015, the DOL re-released proposed regulations that would amend the definition of "fiduciary" under ERISA §3(21) and under the Internal Revenue Code. The proposed regulations would expand the definition to treat a fiduciary as one who provides investment advice or recommendations to an employee benefit plan, plan fiduciary, plan participant or beneficiary, IRA, or IRA owner.

Section D: In its April 2015 edition of the Employee Plans News, the IRS published documentation requirements for hardship distributions and participant loans.

The IRS noted that electronic self-certification from a participant is not sufficient documentation regarding the nature of the participant's hardship. Rather, the employer needs to receive (and retain in its records) something more substantial as documentation (e.g. a copy of an eviction notice, versus the participant certifying that he/she is about to be evicted).

For loan proceeds to purchase or to build a primary residence, the IRS noted that the employer needs proof that the loan proceeds were actually used to purchase/build the primary residence.

Section E: On May 18, 2015, the Supreme Court held in *Tibble v. Edison International* that a fiduciary has a continuing duty to monitor a plan's investment funds (and to make any necessary changes), separate from the fiduciary duties at the time the funds are selected as investment fund alternatives for participants.

Section F: On June 26, 2015, the Supreme Court held in *Obergefell v. Hodges* that all of the states, possessions, and territories of the United States are required to issue marriage licenses to same-sex couples and to recognize valid same-sex marriages. This decision would have impacted retirement plans, had it not been for the Supreme Court's previous decision in *Windsor*, decided on June 26, 2013.

Expanded Summaries:

Section A: Change to the timing requirement applicable to annual participant fee disclosures under ERISA §404(c).

Background:

Participant fee disclosures under ERISA §404(c) must be made at least annually. See TCRS 2010-07 and TCRS 2011-02 for more information.

In July 2013, the DOL provided temporary relief regarding the annual disclosure date (originally set at the end of August for most plans in existence at the time), allowing a "re-set" of the annual date to one coinciding with a date when a plan needs to provide other required annual disclosures to participants. The "re-set" allowed cost savings (to plan administrators, service providers, and possibly participants) by reducing multiple mailings to just one mailing. See TCRS 2013-03 for more information.

Change:

The DOL published a "direct final rule" in March 2015, replacing the definition of the term "at least annually" with respect to the time by which the participant fee disclosures must be made each year. The term "at least annually" now means at least once during any 14-month period (replacing the previous definition of "at least once during any 12-month period"), without regard to whether the plan operates on a calendar year or a fiscal year basis.

The change helps avoid the concern of a "creeping" deadline from one year to the next, caused whenever an annual disclosure is made earlier than 12 months from the prior year, which, under the previous definition of the term "at least annually," accelerated the deadline for the following year.

The effective date of the change was June 17, 2015. However, the DOL allowed a plan administrator to adopt the policy earlier (beginning on March 19, 2015), provided that the plan administrator reasonably determined that using the extended deadline benefited participants and beneficiaries.

Section B: Changes and modifications to correction options for plan errors under the IRS' correction programs.

In March 2015, the IRS and the Treasury Department published Revenue Procedure ("Rev. Proc.") 2015-27, and in April 2015, published Rev. Proc. 2015-28. These revenue procedures modified and/or expanded certain correction options under EPCRS.

Background:

Rev. Proc. 2015-27 modified and clarified certain corrections under EPCRS, including corrections for overpayments, excess annual additions, required minimum distributions, and participant loans.

Rev. Proc. 2015-28 provided new correction methods (and modified an existing correction method) for certain failures related to automatic enrollment and/or for brief periods of missed deferrals. The IRS and the Treasury Department published Rev. Proc. 2015-28 to encourage employers to adopt and/or to retain automatic enrollment features under a 401(k) or 403(b) plan, and to encourage the early correction of missed deferrals (even if the plan does not have an automatic enrollment feature).

Changes under Rev. Proc. 2015-27 (not inclusive):

- Overpayment corrections: Depending upon the facts and circumstances, a plan administrator may not need to request that an overpayment be returned to the plan by the participant/beneficiary who received the overpayment. Rather, the employer or other party may contribute the overpayment to the plan (with interest) in lieu of first seeking repayment, or the employer may adopt a retroactive amendment to conform the plan's documents to the plan's operation.
    - Examples where the plan administrator may choose not to seek reimbursement from the participant (who might now be long retired and on a fixed income) may include situations involving an error in calculating benefits that were paid to a participant in years past, and/or an error in calculating benefits that were paid over a lengthy period of time.
- Excess annual addition corrections: The Self-Correction Program ("SCP") is available for repeated corrections of excess annual additions, so long as the corrections return elective deferrals within 9 ½ months after the end of the plan's limitation year. Each year, a plan must ensure that no participant has received additions under the plan exceeding the limit under Internal Revenue Code ("IRC") §415, which for 2015, is generally $53,000. If a participant exceeds the limit, the allowed time-frame to make refunds had generally been within 2 ½ months after the end of the plan year. That time-frame has been extended to 9 ½ months following the end of the plan year, subject to the employer being eligible for self-correction.
- Required minimum distribution corrections: The compliance (filing) fee under VCP has been reduced. If the only failure being corrected is the failure to satisfy the required minimum distribution requirements of IRC §401(a)(9) and the failure would result in applicable excise taxes, the compliance fee is $500 if 150 or fewer participants are affected, and $1,500 if 151 to 300 participants are affected. If more than 300 participants are affected, the general compliance fees apply, which escalate, based upon the number of participants (for 300 participants, the fee is $5,000). This replaces compliance fees of $500 for 50 or fewer participants or escalating fees starting at $2,500 for more than 51 participants.
- Participant loan corrections: The compliance fee under VCP has been reduced, if the only failure being corrected is the failure to satisfy the participant loan requirements under IRC §72(p) and if the failure does not affect more than 25% of the participants in any year in which the failure occurred. Prior to the modification, the compliance fee was based upon the number of participants. Now, the compliance fee is based upon the number of participant loan failures being corrected under the filing. For example: Prior to the change, the compliance fee for a plan with 101 participants and with 13 loans needing correction under VCP was $5,000. Now, the compliance fee is $300.

Examples of loan failures that may be corrected under VCP include defaulted loans, and loans that exceeded loan limits, such as the amount of the loan or the allowed repayment term.

Changes under Rev. Proc. 2015-28 (not inclusive):

Preliminary comments:

- Prior to the new or modified corrections under Rev. Proc. 2015-28, the correction method for missed deferrals has generally been for the employer to make an immediately vested qualified non-elective contribution ("QNEC") to the plan for the affected employee, equal to 50% of the missed deferral, plus earnings. In addition, the employer must make matching contributions (if applicable), plus earnings, based upon 100% of the missed deferral. See Rev. Proc. 2013-12. *This correction method continues to apply if the requirements of the new or modified correction methods under Rev. Proc. 2015-28 are not met*.
- For purposes of the corrections, a "missed deferral" includes the following situations:
  - an eligible employee was not automatically enrolled
  - an eligible employee's deferral election was not properly implemented
  - an eligible employee's deferral percentage was not automatically increased
  - an employee was mistakenly excluded from the plan

New correction methods:

- Automatic enrollment "missed deferral" failures.
  No QNEC is necessary for the failure to automatically enroll or automatically increase the deferral rate of an eligible employee if correct deferrals begin by the earlier of:
  - 9 ½ months following the end of the plan year of the failure, or
  - If the employee notifies the employer of the failure, the first payroll of the second month following the notification.
- "Missed deferral" failures other than the above.
  No QNEC is necessary if the period of missed deferrals is three months or less and if correct deferrals begin by the earlier of:
  - The first payroll after the period of missed deferrals, or
  - If the employee notifies the employer of the failure, the first payroll of the second month following the notification.
- Besides starting correct deferrals by the deadlines above, the employer must provide a notice to the affected employee within 45 days after correct deferrals have started. The notice must include the following information:
  - General information about the failure, such as the percentage of compensation that should have been deferred and the approximate date deferrals should have begun;
  - An explanation that the participant may increase his/her deferrals to make up for the missed deferrals; and
  - If applicable, a statement that corrective contributions relating to matching contributions have been, or will be, made;
  - The plan name and plan contact information, including the name, street address, e-mail, and telephone number of a plan contact.
- In addition to starting correct deferrals and providing a notice, the employer must also make any matching contributions (if applicable) on the missed deferrals, plus earnings. Matching contributions, plus earnings, should be made as soon as feasible, but in no event later than the end of the second plan year following the plan year of the failure.

Modified correction method (if the employer cannot meet the requirements for the new correction methods):

- Under the modified correction method, the employer must make a QNEC equal to 25% of the missed deferrals (plus earnings) if correct deferrals begin by the earlier of:
  - The first payroll following the end of the second plan year following the year of the failure, or
  - If the employee notifies the employer of the failure, the first payroll of the second month following the notification.
  - In addition to the QNEC, the employer must provide a notice within 45 days after correct deferrals have started, and must also make any matching contributions on the missed deferrals, plus earnings. The notice is the same as described above, except must also include a statement that a QNEC has been/will be made.

If a new or modified correction method cannot be used, then the existing correction method under Rev. Proc. 2013-12 may be used (a QNEC of 50% of the missed deferrals, plus matching contributions, plus earnings).

Section C: Re-release of proposed fiduciary regulations by the Department of Labor ("DOL").

In April 2015, the DOL re-released proposed regulations that would amend the definition of "fiduciary" under ERISA §3(21). The proposed regulations "would treat persons who provide investment advice or recommendations to an employee benefit plan, plan fiduciary, plan participant or beneficiary, IRA, or IRA owner as fiduciaries under ERISA and the [IRC] in a wider array of advice relationships than the existing ERISA and [IRC] regulations." In addition to the proposed regulations, the DOL published related proposed amendments to certain prohibited transaction exemptions applicable to fiduciaries under ERISA and the IRC, and proposed two new exemptions.

Background:

In October 2010, the DOL published proposed regulations to amend the definition of "fiduciary" under ERISA §3(21). Due to feedback and criticism from a number of sources, the DOL announced in September 2011, that it would re-propose its rule on the definition of a fiduciary, and expected to do so in early 2012.

In April 2015, the DOL re-proposed the proposed regulations, in which the DOL also officially withdrew the regulations proposed in 2010.

As with the initial proposed regulations, the DOL has received considerable feedback and comments about the newest proposed regulations. Due to the feedback and public comments, the DOL expanded the comment period (about the proposed regulations and associated prohibited transaction exemptions) from 75 days to 90 days. The DOL will hold a public hearing August 11th – 12th (and possibly the 13th) to consider issues in finalizing the regulations and prohibited transaction exemption changes.

We will provide a summary once the DOL issues final regulations and prohibited exemption changes.

Section D: Guidance regarding hardship withdrawal and participant loan documentation.

Background:

In its April 2015 edition of the Employee Plans News, the IRS published documentation requirements for hardship distributions and participant loans. The Employee Plans News also noted that the employer is required to receive and to retain the documentation in its records, available for any IRS examination. If the records are not available, such is a qualification failure that would require correction under EPCRS.

Guidance:

- Hardship withdrawals: Electronic self-certification from a participant is not sufficient documentation regarding the nature of the participant's hardship. Rather, the employer needs to receive (and retain in its records) something more substantial as documentation. Example: If the participant requests a hardship withdrawal to prevent the eviction from his/her principal residence, the employer may need to receive proof that shows eviction from the participant's principal residence is imminent.
- Participant loans: For loan proceeds to purchase or to build a primary residence, the employer needs proof that the loan proceeds were actually used to purchase/build the primary residence.

More guidance and examples from the IRS are anticipated, including what should an employer do if the only documentation for previous hardship withdrawals was an electronic self-certification, and what must/should an employer do if the proof of loan proceeds to purchase a primary residence was not and/or cannot be obtained?

Section E: Guidance regarding the continuing obligation of plan fiduciaries to intermittently review investment funds offered under a plan, and if changes are necessary, to make changes.

Background:

In *Tibble v. Edison International* ("*Tibble*"), beneficiaries of the Edison 401(k) Savings Plan sued Edison International (in its capacity as a plan fiduciary) to recover damages as a result of three mutual funds added to the plan in 1999, and another three mutual funds added to the plan in 2002.

The six mutual funds were retail-class mutual funds, which were higher-priced than materially identical, lower-priced institutional-class mutual funds (apparently available to the plan at some point).

The beneficiaries claimed the damages were caused by their plan balances having been invested in the higher-priced mutual funds, which was a result of the plan fiduciaries' purported breach of the duty to exercise prudence (by not replacing the higher-priced mutual funds with the lower-priced mutual funds).

Edition International argued that any claim of fiduciary breach was barred under ERISA, which requires that a complaint of a breach of fiduciary be filed no more than six years after the date of the last action that constituted a part of the breach. Thus, Edison International claimed that since more than six years had passed since the addition of the six mutual funds to the plan, no claim could be filed, even had there been a breach.

Guidance - Brief summary of *Tibble*:

On May 18, 2015, the Supreme Court held that, separate from the fiduciary duties at the time funds are selected as investment fund alternatives for participants, there is a continuing fiduciary duty to monitor the investment funds (and to make any necessary changes).

Whether an actual breach occurred is not yet known. The Supreme Court remanded the case to the Ninth Circuit to consider the beneficiaries' claims in light of the fiduciaries' continuing duty to monitor the investment funds.

Impact: Fiduciaries who do not periodically review investment funds may be subject to a claim and possible liability for a fiduciary breach. To avoid a situation such as *Tibble*, plan fiduciaries should establish intermittent meetings during the year (including with financial advisors and/or investment managers, where applicable) to review the investment funds and to timely make any changes, if necessary. Even if it is determined no changes are necessary, the fiduciaries should document the meetings, such as the dates held, who attended, what was reviewed and discussed, and any decisions made.

Section F: Guidance regarding same-sex marriage.

Background:

The lawsuit of *Obergefell v. Hodges* ("*Obergefell*") involved James Obergefell and John Arthur, a same-sex couple residing in Ohio, married in Maryland. At the time, Ohio did not allow same-sex marriage, nor did Ohio recognize a same-sex marriage. Arthur was terminally ill and wanted the Ohio Registrar to recognize and name Obergefell as his (Arthur's) surviving spouse on his death certificate, but following Arthur's death, Ohio refused. Obergefell filed a lawsuit (naming then governor of Ohio as the defendant), alleging that Ohio discriminated against same-sex couples who have lawfully married out-of-state.

Guidance - Brief summary of *Obergefell*:

The Supreme Court held that the fundamental right to marry is a United States' Constitutional right. All of the states, possessions, and territories of the United States are required to issue marriage licenses to same-sex couples and to recognize valid same-sex marriages.

Impact: It appears there is no impact to retirement plans, because of the Supreme Court's previous decision in *Windsor* and subsequent guidance from the IRS and the DOL, which already required plans to recognize valid same-sex marriages. See TCRS Nos. 2013-02, 2013-04, and 2014-01.