ERISA ROUNDUP

A quarterly recap of recent publications from BDO's ERISA Center of Excellence.

Q2 2018

A NOTE FROM BDO'S NATIONAL ERISA PRACTICE LEADER

A central mission of BDO's ERISA Center of Excellence is sharing knowledge and best practices with the industry. We believe in the power of education to fuel growth and people development.

This quarter, many of our publications centered on this mission–to inform not only on current events, but to inspire plan sponsors to take a deeper look and identify creative solutions for the welfare of their employees.

We saw a number of newsworthy topics last quarter – GDPR went into effect; the DOL made announcements around their fiduciary rule enforcement policy; and Congress took a hard look at ESOPs. Changes to the employee benefit plan landscape make it challenging for you to stay ahead of regulations and requirements. Our ERISA practice is proud to play a role in that effort.

Sincerely,

BETH GARNER
National Practice Leader, ERISA

IN THIS ISSUE

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Loans and Hardship Withdrawals: New Rules for Employees Dealing With Natural Disasters and Other Financial Emergencies

Natural disasters including Hurricanes Harvey, Irma and Maria, as well as the California wildfires, caused a record-breaking $283 billion in damage to homes and other property in 2017, according to the National Oceanic and Atmospheric Administration.

Meanwhile, more than a third of participants surveyed in the 2017 Global Benefits Attitudes Survey by consulting firm Willis Towers Watson said they suffered a moderate to severe financial hardship last year. About 80 percent of the survey respondents said they were living paycheck to paycheck.

Whether due to a natural disaster or otherwise, it's clear that many participants need access to cash to pay for unexpected expenses. Two new laws—the Tax Cuts and Jobs Act (TCJA) and the Bipartisan Budget Act of 2018 (BBA)—coupled with new Internal Revenue Service (IRS) rules for victims of natural disasters have helped broaden defined contribution loan and withdrawal options for participants who find themselves in financial distress.

There are key nuances to the rules affecting loans and hardship withdrawals, so it's important that plan sponsors familiarize themselves with the changes. In many cases, the new rules provide flexibility not only for participants but for plan sponsors too. Reporting requirements for plan sponsors have been eased, but it's important to gather the necessary materials as soon as possible, because federal regulators have up to three years to look back on the transactions.

To help plan sponsors understand how these changes affect them and their employees, BDO outlines the old procedures and identifies the notable differences for loans and withdrawals made to victims of natural disasters, as well as participants needing access to their defined contribution plans.

CHANGES TO LOANS FROM DEFINED CONTRIBUTION PLANS

Participants in 401(k), 403(b) and 457(b) plans can take loans under normal conditions if the plan document specifies that as an option. In general, the total amount allowed is the lesser of 50 percent of the participant's present vested amount or $50,000. The loan needs to be repaid within five years (except if, as permitted by the plan, used and documented for the purchase of a primary residence), and payments must be made quarterly at a minimum. In some cases, spouses must sign off on the loan and its amount.

For "qualified individuals" living in specified areas affected by 2017's hurricanes and wildfires, the loan limit increases to the lesser of 100 percent of the participant's present vested amount or $100,000. These loans are available only through December 31, 2018. Again, in some cases, spouses must give approval of the loan and its amount.

For "traditional" loans, participants must repay the amount borrowed within five years. For disaster victims, the loan repayments can be suspended for one year, but interest on the loan will accrue during that time. If a participant chooses to use the one-year suspension, the participant has five years to repay the amount. Like traditional loans, loans for disaster victims must have a reasonable interest rate.

Plan sponsors can start these loans immediately, but plan documents must be amended to show the new terms. Plan sponsors have until the last day of the first plan year beginning on or after Jan. 1, 2019 to submit the changes.

Additionally, the TCJA extended the loan repayment schedule for advances under normal, non-disaster circumstances. Previously, employees who had an outstanding loan when they left a job had 60 days to pay off the loan. If the participant failed to do this, the loan would be considered a withdrawal and would be subject to income tax plus a 10 percent penalty. For loans taken on or after Jan. 1, 2018, the TCJA changes the deadline to repay loans to the participant's tax filing date, which could be as late as October of the following year if the extension is taken.

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CHANGES TO HARDSHIP WITHDRAWALS FROM DEFINED CONTRIBUTION PLANS

Under the previous rules, participants had to take a loan out before moving to the hardship withdrawal. If the plan permitted hardship withdrawals, participants needed to offer proof that there was a severe financial hardship resulting from an extraordinary circumstance—such as an accident or to avoid eviction from a home—to qualify. Participants could take out what was necessary to pay for the expense, and they would not be allowed to contribute to 401(k) and 403(b) plans for six months after the withdrawal. (Participants to 457(b) plans, however, could continue contributing to the plan without delay.) In some cases, spousal consent would be required. The distribution was subject to income tax in addition to a 10 percent withholding tax.

The BBA has loosened some of the old withdrawal rules and has made those changes permanent for all hardships. For plan years beginning after Dec. 31, 2018, participants with hardship withdrawals can contribute to their defined contribution plan without having to wait six months. In addition, participants don't have to take out a loan first; they can use the hardship withdrawal as their first option.

Participants with 401(k), 403(b) and 457(b) plans who lived in specified natural disaster areas during the time of the event are now allowed to take "Qualified Hurricane Distributions" and "Qualified Wildfires Distributions" (Special hardship withdrawals above the IRS allowed safe harbor hardship withdrawals). Distributions are available through December 2018. Both laws specify that participants can ask for up to $100,000 in total from all of their plans. Qualified disaster distributions are not subject to the 10 percent tax on early withdrawals. Participants are allowed to take out what they've contributed, plus interest earned and employer contributions to their accounts, not to exceed the total amount limits.

Participants may, but are not required to, repay the special hardship distribution tax-free. If participants want to take advantage of the opportunity to repay the withdrawal tax-free, they must repay the funds within three years of the withdrawal. There are some exceptions to this rule.

As with the changes to the rules related to normal hardship withdrawals, disaster victims can make contributions to their defined contribution plan during the six months after the distribution. In addition, if the participant is unable to use the distribution to purchase a home prior to the disaster event, the amount withdrawn can be recontributed to an eligible retirement plan.

Plans sponsors are allowed to rely on a reasonable representation of need from the participant to make the loan or distribution. The IRS requires that the plan sponsor make realistic attempts to obtain the missing information as soon as possible. For example, if a spousal consent is required, and the spouse dies, the plan sponsor can make the loan or distribution if there is a reasonable belief that the spouse has died. As soon as possible, though, the plan sponsor must collect a death certificate confirming the event.

Plan sponsors must amend the plan to show the new terms. **Form 8915B** is available on the IRS website, along with instructions explaining the details of the form.

BDO INSIGHT: PLAN AHEAD TO HELP PARTICIPANTS DEAL WITH HARDSHIPS

The federal government is providing more flexibility to defined contribution loans and hardship withdrawals and is making a considerable effort to help victims of disasters and their plan sponsors in expediting access to funds needed to rebuild lives. Plan sponsors that want to help their participants gain access to their funds should review plan documents to make sure loans and hardship distributions are allowed. In addition, plan sponsors may consider checking in with their service providers to see whether there are any limitations on making timely loans or distributions when natural emergencies occur. Please contact your BDO representative for help with evaluating plan documents and processes for loans and hardship withdrawals.

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Uncashed Distribution Checks: Best Practices for Plan Sponsors

Defined contribution plan sponsors face numerous challenges when workers change jobs, and the Department of Labor (DOL) is paying close attention to how employers are dealing with these situations.

Often, outgoing workers don't provide instructions or forwarding information, leaving it up to the plan sponsor to figure out what to do with the assets that are left behind.

From 2004 to 2013, more than 25 million participants in workplace plans left at least one retirement account behind when changing jobs, according to a January **report** from the Government Accountability Office (GAO). Meanwhile, the DOL estimates that $15 million in distribution checks goes unclaimed each year.

While the DOL offers guidance for dealing with missing participants in terminated plans, the same is not true for ongoing plans. As fiduciaries, plan sponsors must account for all assets in a plan—whether those checks have been cashed or not.

Plan sponsors should realize that plan participants can be deemed missing because they have not cashed their check. Terminated vested plan participants can also be deemed missing if they simply walked away from the plan and did not request a distribution.

In many cases, searches for missing participants are conducted by plan service providers, such as record keepers, trustees or custodians. But this doesn't relieve plan sponsors from their fiduciary obligation to make sure procedures are being followed. Not dealing with the issue properly can be considered a breach of fiduciary duty and can entail harsh penalties and other liabilities.

According to an October 2017 **letter** sent by the American Benefits Council to the DOL, the DOL's regional offices have been aggressive in investigating plan sponsors' processes for dealing with terminated vested plan participants. Terminated vested participants are workers who qualify to receive matching contributions, but have left the company and may not be of retirement age. In some cases, regional offices determined that plan sponsors breached their fiduciary duties—even when plan procedures have been followed. In light of the DOL's aggressive investigations into these issues, plan sponsors should have procedures in place to handle the uncashed distribution checks of missing participants.

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CURRENT GUIDANCE AND BEST PRACTICES

After leaving a company, many plan participants forget to roll over their 401(k) assets into an Individual Retirement Account (IRA) or their next employer's retirement plan. This doesn't absolve plan sponsors from their duties, however. It's critical that plan documents outline policies so plan sponsors can appropriately handle these situations. At a minimum, plan documents should articulate:

- The process to be followed in searching for an unresponsive participant
- A timetable for plan providers (if applicable) to report progress
- The framework for charging fees and moving assets to an outside IRA, as well as a process for documenting these practices
- Next steps for unsuccessful searches

While rules allow plan sponsors to cash out small accounts, the GAO report found that more than 13 million accounts of $1,000 or less were left by participants from 2004 to 2013, amounting to $1.2 billion. It may seem like a small amount compared to the trillions of dollars in defined contribution plans today, but many experts agree that the numbers are only going to increase as the workforce continues on its trajectory of greater mobility.

To date, the DOL and the Internal Revenue Service (IRS) haven't issued direction on how plan sponsors should handle uncashed checks from ongoing plans. Many plan sponsors have relied on **Field Assistance Bulletin (FAB) 2014-01**, which is meant for finding participants in terminated defined contributions plans.

In August 2017, a DOL official offered four best practices for plan sponsors to follow until further guidance is issued:

1. Send a certified letter to the missing participant using their last known address
2. Keep detailed and up-to-date records on the attempts to reach the missing participant
3. Ask co-workers if they know how to find the missing participant
4. Try calling the missing participant's cell phone (since most people keep their number when moving to a new residence)

If these four steps don't successfully locate the missing participant, plan sponsors should consider continuing their efforts. Possible alternatives include hiring a locator service or conducting other Internet searches. It's important to reiterate that the DOL is placing special emphasis on investigating these issues, and just because plan sponsors made a good faith effort to find someone, it doesn't mean they're relieved of certain responsibilities.

Meanwhile, U.S. Sens. Elizabeth Warren (D-Mass.) and Steve Daines (R-Mont.) have reintroduced legislation aimed at creating a national database to help American workers find their missing retirement accounts. The Retirement Savings Lost and Found Act would allow employers to move abandoned accounts to target date funds as opposed to money market accounts. It would also transfer uncashed checks under $1,000 to Treasury securities, which would be logged into the database for workers to find. Lastly, the legislation clarifies the role employers and plan sponsors play in finding workers who have abandoned their retirement accounts. The bill has been referred to the **Senate Finance Committee**.

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BDO INSIGHT: REEVALUATE YOUR PROCEDURES AND COORDINATE WITH SERVICE PROVIDERS

As the DOL continues its focus on investigating plan sponsors' practices related to missing participants, plan sponsors should review—and possibly revise—their policies regarding how they handle uncashed distribution checks and other issues related to missing participants. If applicable, plan sponsors should discuss the topic with service providers to make sure everyone is on the same page regarding the processes and availability of information.

If they haven't done so already, plan sponsors should develop, document, and implement procedures for whenever a worker terminates employment. Creating these procedures should be a priority for plan fiduciaries and committees.

In addition, plan sponsors may want to consider doing to following to strengthen their controls related to missing participants:

- Maintain and regularly update a list of outstanding checks
- Monitor account balances for terminated plan participants
- Cash out small account balances—but realize that doing so could increase the number of outstanding checks
- Regularly update employees' contact information

Interested in developing a strategy for dealing with missing plan participants and their assets? Please **contact** a member of BDO's ERISA practice.

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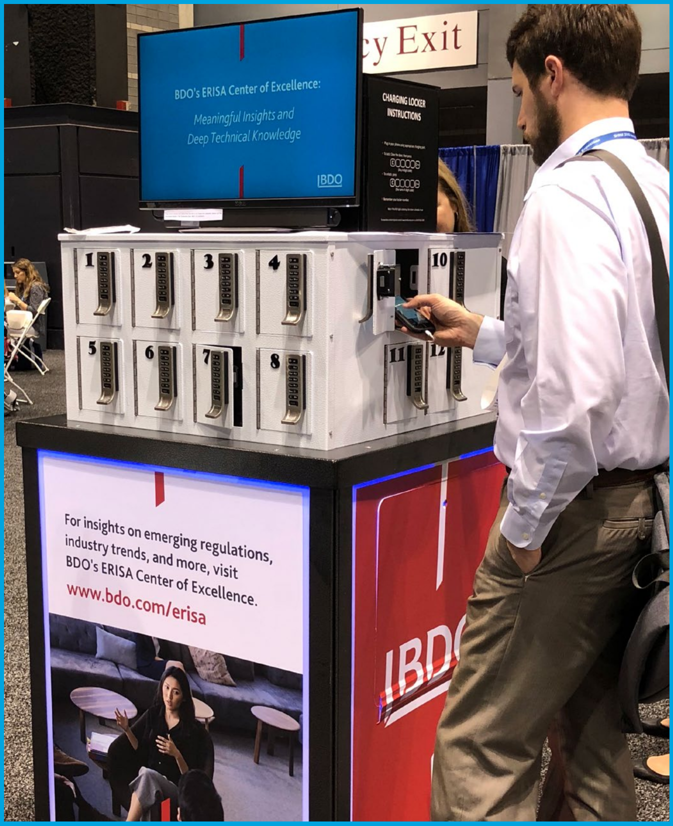
EVENTS AND NOTABLE DATES

SHRM Conference 2018

Members of BDO's ERISA team recently returned from the annual Society for Human Resource Management (SHRM) Conference & Exposition in Chicago where we helped attendees power up with BDO charging stations during breaks. BDO is proud to be a sponsor of this fantastic event geared to strengthen and develop HR practices.

We learned so much attending sessions and met a lot of great HR folks. If we missed you this time around, we hope to see you next year!



Upcoming Filing Deadline

The first filing deadline for the Form 5500 is Tuesday, July 31. Extensions should be filed if the filing deadline cannot be met.

Important Deadlines to Establish a Qualified Plan: Qualified plans must be implemented by December 31, 2018 in order to take advantage of the tax return deductions available for employers and participants. The time to start planning is now in order to have sufficient time before year end. It's too late to start a qualified plan for 2017, but employers may consider funding a SEP, Simplified Employee Pension Plan, for the 2017 year which must be implemented by the due date of the corporate return including extensions. Note Safe harbor 401(k) plans for new businesses must be in place for at least 3 months of the year.

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DOL Announces Temporary Fiduciary Rule Enforcement Policy

The Department of Labor (DOL) announced a temporary enforcement policy on May 7th explaining that it would not pursue legal action against investment advice professionals who rely on the Obama Administration's definition of fiduciary.

According to **Field Assistance Bulletin 2018-02** (FAB 2018-02), the DOL said it would not "pursue prohibited transactions claims against investment advice fiduciaries who are working diligently and in good faith to comply with the impartial conduct standards" set in the fiduciary regulation crafted by the Obama Administration.

That regulation was vacated in March by the 5th Circuit Court of Appeals in the case brought by plaintiffs led by the U.S. Chamber of Commerce against the DOL (case **17-10238**). In the decision, the court said that the Obama Administration's fiduciary requirements were excessive, arbitrary and capricious.

The DOL said it plans to provide guidance in the future, but until then financial institutions should be allowed to rely on the Obama rule. The May 7th FAB recognized that providers have devoted significant resources to comply with the Obama definition of fiduciary and that there may be uncertainty to the rule as a result of the 5th Circuit Court of Appeals decision.

"*Of course, investment advice fiduciaries may also choose to rely upon other available exemptions to the extent applicable after the Fifth Circuit's decision, but the Department will not treat an adviser's failure to rely upon such other exemptions as resulting in a violation of the prohibited transaction rules if the adviser meets the terms of this enforcement policy,*" the FAB said.

BDO is committed to keeping plan sponsors and their service providers updated on the latest guidance from the DOL regarding the fiduciary standard. In the meantime, if you have questions about what the latest guidance could mean for your retirement plan, please contact your BDO representative.

Employee Stock Ownership Plans Gain Attention in Congress

Congress is paying more attention to Employee Stock Ownership Plans (ESOPs) this session, with two New York legislators shepherding through bills aimed at promoting this type of defined contribution plan.

The U.S. House of Representatives passed by voice vote H.R. 5236, known as The Main Street Employee Ownership Act, on May 8. The bill, introduced in March by Rep. Nydia Velazquez (D-NY), eases rules to help the Small Business Administration (SBA) provide loans and other support to companies interested in creating an ESOP.

The bill's companion piece, S. 2786, was introduced in late-April by Sen. Kirsten Gillibrand (D-NY). This bill gives $500 million to the Small Business Administration for similar purposes. It was referred to the Committee on Small Business and Entrepreneurship.

Shortly after the voice vote, Velazquez tweeted that the bill "will help employee-owned businesses such as co-ops secure access to capital through [the SBA]. After seeing the popularity of food co-ops in NYC, this will help the business model expand to other sectors."

According to the National Association of Employee Ownership, there are nearly 7,000 ESOPs operating nationwide. To date, ESOPs hold about $1.3 trillion in assets and have 14.4 million participants.

BDO will provide further updates on these bills, as well as other new legislation and regulations affecting ESOPs and other types of retirement plans. In the meantime, if you have questions about how current laws and regulations affect your company's defined benefit or defined contribution plans, please contact your BDO representative.

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Financial Well-Being for Women: Empowering Employees by Helping Them Prepare for Retirement

The growth of women's influence in U.S. workplaces has been remarkable over the last several decades. Female labor force participation rates have increased from 43% in 1970 to 57% in 2018, according to the Federal Reserve Bank of St. Louis. As of 2016, women held 52% of all management, professional and related positions, according to the Bureau of Labor Statistics. But there are still many areas where a significant gap remains between men and women employees, including when it comes to preparing for retirement.

According to a recent Merrill Lynch study, Women and Financial Wellness: Beyond the Bottom Line, women may make $1 million less than men by the time they reach retirement. This disparity has many causes. Women are much more likely than men to experience multiple work interruptions to take care of children, parents and spouses. Combining this with lower pay, part-time or freelance jobs with little to no access to retirement savings plans, longer lifespans, and health care needs, a bleak financial retirement picture for women emerges.

Furthermore, women's attitudes and priorities may add additional obstacles to financial well-being. The 18th Annual Transamerica Retirement Survey of American Workers showed that only 12 percent of women are very confident they will retire comfortably, compared to 24 percent of men. Only 51 percent of women say that saving for is a priority, compared to 62 percent of men, according to the survey.

The good news is that women and men want help from their employers to improve their financial well-being. Mercer's Healthy, Wealthy and Work-Wise study showed that 79 percent of Americans trust their employer to give sound financial retirement assistance. In addition, 85 percent say they are interested in using online financial tools. This high level of trust, along with the increased comfort level to get online support, puts employers in a unique position to help women break many of the barriers that prevent them from having a successful financial well-being plan.

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WHERE TO START?

That is a question many women ask when it comes to finances. While women are at ease talking about parenting, health and work issues, financial topics like budgeting, investing and savings are taboo. In fact, the Merrill Lynch study found that 61 percent of women would rather talk about the details of their own death than money issues.

1. Acknowledge the issue and talk about it

Given the unique issues facing women about retirement, it's time to give it higher priority by initiating the conversation. Raising women's comfort levels in talking about financial issues can be a great first step for employers. Lunch-and-learn sessions or small-group gatherings can be useful opportunities to start a financial conversation. If the live gatherings are inconvenient, offering online webinars can be just as effective.

Initiating a conversation about finances can often lead to creating a plan. In many cases, women know how much they can spend on groceries each week, but they haven't calculated how much money they will need for retirement, emergency savings or other financial essentials. Helping women recognize the need to answer these questions can help lower stress levels, which will allow them to become more productive at work.

2. Build on strengths

There are a lot of things women already do well, so use those natural strengths to spring into other financial areas. Often women are in charge of balancing the family checkbook, managing budgets and initiating other planning strategies. Recognizing these strengths can be a way to boost a woman's confidence in managing other financial issues.

Meanwhile, when it comes to investing, women are more conservative than men. While being overly aggressive is certainly problematic, being too conservative carries dangers of its own—especially considering that women should be investing for a longer time horizon than men. Women who reach age 65 are expected to live an additional 20 years on average. Women, by and large, also could benefit from being more aggressive when it comes to the amount that they put away for retirement. The Transamerica survey showed that while 73 percent of women are saving for retirement at work, they are only contributing about 7 percent of pay. Most experts recommend participants save 15 percent of pay each year to reach a healthy retirement savings amount. In addition, Transamerica data showed women's median account balance at $42,000.

3. Encourage good savings behavior through plan design

Employers can play an important role in improving savings rates of all workers by using automatic features like auto enrollment and escalation. These combined strategies can help eliminate the conservative thinking and guesswork. In general, participants are automatically enrolled into a qualified default investment account, like a target-date fund. Target-date funds are diversified investment accounts that are often tailored to a participant's retirement age, and not to what a participant might guess would be appropriate for their time horizon.

4. Technology is key

Technology can also play an important role in helping employees become more comfortable and confident when it comes to investing and long-term planning. Today, many providers are offering more than just calculators that factor interest and contribution rates to help figure out finances. Women can gain financial confidence by exploring tools that let them see how changes to their spending, savings and investing behavior—such as increasing Health Savings Account contributions, accelerating debt repayments or taking on more risk in their investment portfolio—are projected to play out of multiple decades.

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BDO INSIGHT: REDUCE EMPLOYEES' FINANCIAL STRESS BY INCREASING RETIREMENT PREPAREDNESS

Women's lack of retirement preparedness is a major problem for society, especially as millions of baby boomers near retirement age. It also presents a powerful opportunity for employers to engage with this segment of their workforce in a productive and empowering way.

While the need to address retirement planning may seem to be most urgent for older employees who are nearing retirement, the topic is relevant for employees of all ages. In fact, given the power of compounding, the benefits of establishing a retirement savings strategy could be greatest for millennials and other younger workers. Plan sponsors should account for generational differences in attitudes and expectations about retirement when developing a plan for engaging with their employees on this important topic.

In addition to helping women have long-lasting, healthy retirements, raising financial well-being among female workers can have significant benefits for employers as well. The Mercer study showed that 67 percent of women are feeling financial pressures compared to 60 percent of men. Not saving enough for retirement is stressing out 44 percent of women and 36 percent of men. By helping women feel more confident about their long-term financial futures, companies can help their workforces be happier and more productive in the near term.

Offering unique ways for women to talk about their financial issues, giving them tools to quantify and explore different long-term scenarios and increasing participation by using automatic enrollment and escalation features are ways employers can positively impact women's financial well-being and preparedness for retirement. To discuss ways you can help address this within your own workforce, contact a member of BDO's ERISA practice.

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Carpe Diem! Accelerating Defined Benefit Funding to the 2017 Tax Year can Generate Tax Savings

Last year's tax reform law has created a rare opportunity for defined benefit plan sponsors to take advantage of the tax rate difference by accelerating deductions to the year with the higher tax rate. The lowering of the corporate tax rate makes pension plan contributions for the 2017 plan year significantly cheaper on an after-tax basis than contributions for the 2018 plan year.

The Tax Cuts and Jobs Act (the Tax Act), passed in December 2017, implemented a flat corporate tax rate of 21 percent, shifting from a tiered system in which the top marginal rate for corporations was 35 percent. Even though the Tax Act also eliminated some common deductions for businesses, most corporations will face a lower effective tax rate in 2017 than in 2018. For these companies, accelerating deductions into 2017 could result in significant tax savings.

One of the more powerful opportunities to do this has to do with contributions to qualified retirement plans. A for-profit business with a December 31, 2017 tax year end and an extended income tax return can deduct contributions to its qualified retirement plan if they are made before September 15, 2018. The 14 percentage-point difference between 2017's top rate of 35 percent and 2018's rate of 21 percent can create significant savings for qualified retirement plan sponsors who act before the September extended deadline.

This accelerated funding technique is especially attractive for sponsors of defined benefit plans because the funding does not have a direct impact on the amounts of benefits owed or paid under the plan. Pre-funding of a defined benefit plan simply increased the cash set aside in the pension trust to meet the plan's future benefit obligation. It does, of course, put the cash out of reach of the business and its creditors which is a consideration when projecting the business cash flow requirement. The higher funding levels can lower variable-rate premiums owed to the Pension Benefit Guaranty Corp. (PBGC), increase the plan's projected assets, and lower future funding requirements. This approach also makes de-risking strategies more viable.

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DO THE MATH

Accelerating defined benefit plan contributions to the 2017 plan year can create a positive ripple effect. For example, Company A in the top corporate marginal tax bracket decides to contribute an extra $1 million to its pension plan for the 2017 plan year rather than wait to make that contribution for the 2018 plan year. As a result, the company will receive an additional $140,000 in tax savings because it's able to deduct the contribution at the 35 percent rate instead of the 2018 rate of 21 percent.

Meanwhile, the PBGC—the government's insurance agency for defined benefit plans—charges two different kinds of premiums: a flat rate and a variable rate. The flat-rate premium for single employer plans is based on the number of participants in the plan. The 2017 rate is $69 per participant; it will go up to $74 in 2018. It's an annual charge, so plan sponsors simply pay this. There's no real savings in this premium, except in the case of a company that de-risks using an annuitization or lump-sum strategy, which would leave it with fewer participants in the plan.

The variable rate is set at a certain percentage for each $1,000 of unfunded vested benefits (UVBs). In 2017, plan sponsors pay 3.4 percent, or $34 per $1,000, in UVBs; this is capped at $517 per participant. The rate will go to 3.8 percent in 2018, or $38 per $1,000, in UVBs, with a cap of $523 per participant. The PBGC estimates the cost will go to $42 per $1,000 in UVBs in 2019.

Clearly, a better-funded plan will pay a lower variable rate premium. The bonus is that extra contributions will not only lower the UVB for 2017, but they will be invested and could be expected to compound in the future. Higher overall earnings can reduce prospective funding obligations.

Another potential benefit from the new law: the mandatory tax on overseas foreign earnings was lowered from 35 percent to 15.5 percent. The extra cash companies will see as a result could go directly toward many corporate objectives, including improving pension funding levels.

Before jumping to take advantage of these potential benefits, though, it's important to work with your BDO expert to make sure overfunding doesn't occur. While excess assets can go back to an employer when the plan terminates and all benefits are paid out, such asset reversions are subject to regular taxes and hefty penalties.

TIME TO DE-RISK?

The financial crisis of 2008 delivered a heavy blow to defined benefit plan funding levels. As a result, many companies decided to implement various de-risking strategies. Some changed the asset management approach, but others chose to reduce plan obligations by purchasing annuities or offering lump sum amounts for plan participants. With the latter two actions, plans became smaller, but more manageable in terms of ongoing costs.

Ten years later, plan sponsors have a similar opportunity to de-risk again. Plan sponsors wanting to get off the rollercoaster when dealing with liabilities, variable premiums, investment returns, interest rate assumptions, regulations, and other moving targets that deeply impact a pension plan's bottom line, might consider the various options available to reduce or eliminate risk in a company's defined benefit plan.

BDO INSIGHT: CONSIDER TAKING ADVANTAGE OF A RARE OPPORTUNITY

While the Tax Cuts and Jobs Act didn't directly address defined benefit plans, the law's shift in the corporate tax rate, as well as the tax rate for unrepatriated foreign earnings, has presented plan sponsors unique opportunities to boost plan funding levels. Plan sponsors should work with their BDO expert to set goals, understand risks and benefits, determine the best funding strategy, as well as to see how this strategy integrates with other employer offerings.

There are many factors to consider. While the September 15 extended deadline is still months away, it will get here sooner than you think. Much thought and planning should go into a well-executed defined benefit funding plan, so please take the time to work with your BDO advisor to weigh the possible benefits for your company.

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GDPR: What Plan Sponsors Need to Know About the EU's New Data Protection Rules

The European Union's (EU) **General Data Protection Regulation** (GDPR) goes into effect May 25, and its impact reaches across the pond to many U.S.-based businesses that collect, use or store data from EU residents.

Many U.S.-based companies are still trying to figure out whether the regulation applies to their organization. More than half (52 percent) of 400 U.S.-based companies **surveyed** by The Computing Technology Industry Association in April of this year reported that they are still exploring the applicability of GDPR to their businesses, have determined that it is not a requirement for them, or are unsure. Of the remaining businesses, only about one-in-four (27%) said that they are fully compliant – and that was just one month shy of the deadline.

Although the rule does not directly address 401(k) or other benefit plans, it should be of particular interest to plan sponsors because of the personal information that their organizations and service providers possess for each participant. Even U.S. companies that do not have any EU employees or clients, and do not market to EU residents, may still want to consider following GDPR guidelines because many experts believe that the regulation will eventually become the standard for data privacy across the globe.

Here, we will explain the main points of GDPR and what it means for benefit plans.

WHAT IS GDPR?

The EU passed GDPR in April 2016 and the rule is effective as of May 25, 2018. It updates and unifies the 28 implementations from the 1995 Data Protection Directive and gives EU citizens unified and broad control over their personal data and information. It sets new, stricter standards of accountability for companies that collect, process and use data gathered from EU citizens. There are also strict breach notification and data documentation requirements. In addition, EU citizens can ask an organization how their personal information is used, stored, protected, and transferred.

DO U.S. COMPANIES NEED TO PAY ATTENTION?

It depends. GDPR applies to every organization that houses personal data of, provides products or services to, or markets to, EU residents. Companies do not necessarily need to have a physical presence in the EU; if they have EU resident data, the rule applies. For example, if a U.S.-based plan sponsor has employees who are EU citizens living in the U.S., GDPR applies to that company. If a company collects information from EU citizens via their website, GDPR applies to that company.

Additionally, companies will now be responsible for showing that they are complying with the regulation—or face severe penalties. For instance, certain organizations that do not report a data breach within 72 hours of discovery can face the maximum fine of up to 4 percent of their global annual revenue or €20 million, whichever is greater. GDPR can also force an organization in violation of its rules to stop collecting personal data. There are many factors that will impact the level of penalty.

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WHAT IS CONSIDERED DATA UNDER THE RULE?

The definition of data under GDPR is rather broad. The regulation says "personal data" means any information relating to an identified or identifiable natural person. That means any kind of information that can identify a person either directly or indirectly. This includes email addresses; pictures on Facebook or other social media websites; browser cookies; human resource information that connects names to job titles; and internet searches and other online activity that can be traced back to the user are all considered personal data.

Benefit providers or plan sponsors need to understand what data they have and how it is used by the organization so it can be identified, monitored and protected. Further, organizations will need processes in place to respond to data subject access requests, such as the right to be forgotten.

It is important for plan sponsors to understand that GDPR requirements extend beyond data stored at their companies; GDPR requirements cover data collected and stored by an organization's service providers, as well as any sub-contractors. Organizations need to determine the types of personal data they store, where it resides, who can access it, and what it's being used to do. Recordkeepers, plan attorneys, consultants, payroll companies, and third-party administrators are the types of service providers who may have access to personal data. The organizations engaging these service providers have obligations under GDPR and should be thinking about how to structure or amend contracts to address standards for data collection, storage and usage.

WHAT ARE INDIVIDUALS' RIGHTS UNDER GDPR?

One of the main tenets of GDPR is that EU residents have certain **rights** related to their personal data. Companies must ascertain an individual's consent to use their data. In addition, companies must inform individuals, in clear and plain language, of their rights to their personal information, including the right to know what of their data the organization is storing, why the organization is storing it, and the right to be notified of a breach. Under Article 17, individuals have the right to request to be forgotten (deleted) from an organization's records and systems.

BDO INSIGHT: DATA PROTECTION IS A CORE COMPETENCY

Successful businesses must constantly respond to new threats, and in today's environment, cyberattacks and data breaches have emerged as a high priority for businesses of all sizes. While GDPR has raised the stakes and codified the requirements for data handling and protection for many companies, it is simply the next step in what will be an evolving journey for companies and regulators.

Regardless of whether GDPR applies directly, plan sponsors have a fiduciary responsibility to act in the best interests of their plan participants. In addition to creating significant legal liability to plan sponsors, data breaches can pose a major threat to participants' financial well-being and peace of mind. Conducting careful reviews of procedures used by the company or its providers to collect, store and use personal data should be an essential part of a company's retirement plan and benefits offering.

Building data privacy considerations into business functions is a competency that organizations must develop and continually strengthen. Your BDO representative can help you assess your current practices and implement a global plan to address data protection requirements.

HOW CAN BDO HELP?

Most companies that conduct business with EU residents, have EU resident employees, or market to EU residents require a GDPR action plan. GDPR readiness is not a one-time event; it necessitates an ongoing strategy to identify, monitor and protect personal information and to design systems and processes with data privacy in mind. No matter where your organization is on its road to GDPR compliance, BDO can help.

Learn more about BDO's GDPR compliance **services**.

View our GDPR compliance **checklist** to help determine whether your organization is prepared.

Learn about our partnership with IntraEdge, a technology talent, services and training leader to deliver a GDPR blockchain-based solution called **GDPR Edge**.

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Auto-Enrollment and Auto-Escalation: Right for Your Retirement Plan?

When it comes to saving for retirement, getting started can be the hardest part for many employees. This challenge, however, is being solved for many American workers by the dramatic increase over the past decade in the percentage of 401(k) plans that use automatic enrollment and automatic escalation features to encourage participation.

Nearly 60 percent of plan sponsors automatically enroll workers in their defined contribution plans today, according to the Plan Sponsor Council of America's 60th Annual Survey of Profit Sharing and 401(k) Plans. That's nearly double the amount from a decade ago, and up from 46 percent in 2011. More than 73 percent of plans with automatic enrollment also automatically increase deferral rates, an increase of more than 18 percentage points over the past 10 years. PSCA also reports that 89 percent of eligible workers participate in a company defined contribution plan.

Despite the growing popularity of automatic enrollment and escalation features, determining whether to adopt them is far from being a decision that plan sponsors can put on cruise control. While automatic enrollment and escalation offer many benefits to employees as well as plan sponsors, sponsors need to consider and manage them effectively to ensure a successful program.

BACKGROUND AND LATEST DATA ON AUTOMATIC ENROLLMENT

The Pension Protection Act of 2006 (PPA) created a safe harbor for plan sponsors to automatically enroll workers into 401(k) plans. Instead of requiring employees to choose to join a plan, automatic enrollment flips the decision to start saving and requires them to opt-out if they don't want to participate. With automatic enrollment, employers elect a default contribution rate and can use a Qualified Default Investment Alternative (QDIA), such as a target date or lifestyle fund, to relieve employers of any fiduciary liability for this initial investment choice. The PPA also allows plan sponsors to automatically increase employee contributions over time. Once in the plan, participants can reallocate the assets out of the QDIA to whatever investments they see fit within the plan's eligible investment options.

The PPA has paved the way for workers' inertia to work for them, not against them, when saving for retirement. Studies have shown that automatically enrolling workers into defined contribution plans and boosting their contribution rates on an annual basis has helped more people to save for retirement than if left on their own to do the work. In addition, Wells Fargo Institutional Retirement and Trust's 2017 Driving Plan Health study showed that there is little difference in opt-outs when deferral rates are set at 3 percent versus a higher 6 percent contribution rate.

Automatic enrollment is most common in large plans (i.e., plans that have 5,000 or more employees); 70 percent of large plans use automatic enrollment. Industry-wise, 84 percent of insurance and real estate companies use the strategy, followed by non-durable goods manufacturing at 82 percent. Industries with lower usage rates include utility and energy companies (39 percent) and service businesses (46 percent).

So why are nearly 40 percent of plans not following suit and using automatic enrollment? And why are t nearly a quarter of companies currently using auto enrollment not pairing it with annual contribution escalations? For those not using auto enrollment, nearly half of the respondents to the PSCA survey said they were happy with their participation rates while a third said auto features don't line up with corporate thinking.

UNDERSTANDING THE BENEFITS

As with any element of plan design, there are important items to consider when - using automatic enrollment and escalation. Various types of automatic contribution arrangements can meet safe harbor provisions and exempt plans from certain non-discrimination testing requirements. Even though auto features are increasing in popularity, there is not a one-size-fits all program for every retirement plan. As companies consider whether to adopt these features—or amend their use of them—they need to evaluate the potential benefits and costs from both the employees' perspective and the company's perspective.

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BENEFITS OF AUTOMATIC ENROLLMENT AND ESCALATION

For Plan Sponsors:

- Defaults employees into an investment vehicle that is pre-approved by the Department of Labor
- May streamline and simplify the new employee on-boarding process
- May lead to lower administrative fees and/or the ability to offer additional tools and services to participants thanks to higher cumulative assets under management
- Puts employees on an automatic savings track, which may help improve employee retention and help them feel more secure about their financial futures
- Adds a benefit that can be used to attract and retain top talent
- Aids in non-discrimination testing
- Certain auto enrollment plans allow highly compensated employees to contribute the maximum amount and relieves the plan sponsor from anti-discrimination testing
- Reduces employer payroll taxes because funds are being contributed pre-tax
- Generates certain tax credits and deductions, such as matching contributions, for employers

For Employees:

- Increases plan participation among all incomes and age groups
- Allows many participants to save for retirement who might not do so if left on their own
- For traditional plans, participants defer paying income tax until they withdraw funds at retirement
- Allows participants to take advantage of company match or "free money"

NECESSARY CONSIDERATIONS FOR A SUCCESSFUL AUTOMATIC ENROLLMENT AND ESCALATION PROGRAM

For Plan Sponsors:

- Requires administrative oversight, particularly in regard to ensuring all eligible participants are properly and timely enrolled and escalation amounts are properly aligned with payroll withholdings
- Requires coordination and controls with record keepers and other third-party service providers
- Requires amending plan documents
- Certain auto enrollment plans need to start at the beginning of the plan year
- May call for more robust communication campaigns with employees to help them understand new plan features
- If mistakes are made, corrective measures can be costly and time consuming
- May cause employer contribution amounts to rise as more employees participate in the plan
- May result in more accounts with lower balances, especially for plans with lower default contribution rates and adds more burden on administrator to clean out balances when participants terminate

For Employees:

- May give employees a false sense of security, especially if the default rate is set too low and no automatic escalation is paired with the enrollment
- May increase the risk that employees end up with suboptimal asset allocations across their entire portfolios if they don't fully understand the holdings in their target date or lifecycle funds

BDO INSIGHT: CONSIDER LEVERAGING THE POWER OF AUTOMATION TO IMPROVE FINANCIAL WELLNESS

As Americans' retirement savings rates continue to be lackluster and as companies become increasingly focused on their employees' financial wellness, automatic enrollment and escalation features may be useful tools in managing your workforce and getting employees prepared for their financial futures. In addition to helping put employees on track for a successful retirement, implementing these features can have powerful benefits for employers, as well, by streamlining the enrollment process and serving as a tool to attract and retain talented workers.

Before adopting automatic enrollment or escalation, plan sponsors should work closely with their internal teams, as well as with their third-party service providers, to ensure that the proper controls and procedures will be put in place.

To better understand the benefits and administrative requirements of automatic enrollment and escalation and to assess how these features could be adopted in your plan, contact a member of BDO's ERISA team.

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Cash Balance Plans: An Effective Strategy to Maximize Retirement Savings for Key Employees

Competition for talent is fierce today, and many employers are searching for solid benefit strategies to attract and retain top employees. One approach that can accomplish these goals is the cash balance plan. These plans have been growing in popularity in recent years despite the fact that many in the benefits industry once considered cash balance plans to be nearly extinct.

Cash balance plans—also known as hybrid plans—are a type of defined benefit plan where employees see their accounts just like they would in a defined contribution plan. Unlike 401(k)s, however, employers—not employees—contribute to an account. These accounts are known as hypothetical accounts because cash balance plans are ongoing, not finite like a 401(k). Contributions to the accounts comprise two calculations: one that is based on a pay credit (which is typically based on a percentage of pay or a flat dollar amount) and the second is a fixed or variable rate interest credit.

Defined contribution plans are certainly eclipsing defined benefit plans in number and assets under management. But cash balance plans are bucking this larger trend. According to Kravitz's 2017 National Cash Balance Research Report, the number of new cash balance plans increased 17 percent, while 401(k) plans grew only 3 percent in 2015, the most recent year for which data are available. In addition, cash balance makes up more than a third (34 percent) of all defined benefit plans. Most of this growth has come from smaller companies; Kravitz's report shows that 92 percent of plans are found at companies with 100 or fewer employees.

Despite the growing popularity of cash balance plans, it's important for companies to analyze whether they are a good candidate to adopt these strategies. BDO finds that cash balance plans work best in companies that have the following qualities:

- Consistent cash flow and/or profit margins
- Desire to give key employees the opportunity to accrue higher retirement savings than what would be expected with a 401(k) and/or profit sharing plan
- Desire to take advantage of significant tax savings to help fund other plans

RELIABLE ANNUAL CASH FLOW

It's important for a company that adopts a cash balance plan to have consistent cash flow because the plan sponsor is responsible for funding the plan annually. When investments do better than the guaranteed interest credit, the plan sponsor usually gets a reduced contribution rate. Conversely, if investments underperform, the plan sponsor has to make up the shortfall. In general, plan sponsors should expect to contribute between 5 percent and 7.5 percent of pay for staff employees for their retirement plan. In addition, companies generally should consider making a 3- to 5-year commitment to the cash balance plan before considering amending plan documents.

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KEY RETENTION AND FUNDING TOOL

Unlike many retirement plans today, cash balance plans are a powerful way to significantly boost retirement savings for key employees. This approach also creates considerable tax savings that can be used to fund other plans. In general, cash balance plans are typically used for top talent while a 401(k) or other type of defined contribution plan is offered to all employees.

Employees who are included in the cash balance plan are allowed significantly higher contribution rates. Each participant is allowed to accumulate up to around $2.5 to $3.0 million under current law; the actual contribution limit each year depends upon the participant's age and progress toward accumulating that maximum amount. Beyond that, adding a cash balance plan can make a significant difference for key employees of all ages who are behind in saving for retirement, not just those who are age 50 or older, as is the case with 401(k) and profit sharing plans.

Listed below are the 2018 contribution limits allowed by the Internal Revenue Service for employees of various ages, along with the potential federal tax savings (assuming a 37 percent federal income tax rate for pass-through entities).

Age	401(k) only	401(k) w/ Profit Sharing	Cash Balance	Total	Tax Savings
70	$24,500	$61,000	$329,000	$390,000	$120,990
65	$25,500	$61,000	$266,000	$327,000	$127,280
60	$24,500	$61,000	$254,000	$315,000	$117,290
55	$24,500	$61,000	$194,000	$255,000	$96,200
50	$25,500	$61,000	$148,000	$209,000	$79,920
45	$18,500	$55,000	$113,000	$168,000	$65,120
40	$18,500	$55,000	$87,000	$142,000	$55,130

In many cases, the tax savings generated from employer contributions to a cash balance plan for key employees can help fund other retirement plans sponsored by the company. This is one of the primary benefits of the strategy and an important consideration. Assuming a 37 percent federal tax rate for pass-through entities, companies can realize tax savings ranging from $120,990 to $55,130 per employee for the age groups listed above. State and local tax savings may also apply. The tax savings alone from cash balance plans can easily pay for the employer contributions needed for 401(k) and profit sharing plans.

Another point to keep in mind is that IRS requires plan sponsors to retain an actuary to certify the funding of the plan. This can be done in-house or by a service provider.

OTHER BENEFITS

In addition to the tax savings and ability to provide significant retirement contributions to key employees, other benefits of cash balance plans include:

- **Portability.** Like 401(k)s, most cash balance plans are set up to allow employees to take their vested assets should they decide to leave the company. Those assets can be rolled into an Individual Retirement Account (IRA) or other qualified retirement plan, such as a 401(k).
- **Flexibility.** The plan sponsor can decide who to include in the plan as well as how much should be contributed to each hypothetical account. Of course, the plan needs to pass IRS non-discrimination testing rules, so employers need to cover a sufficient number of employees of the company and contribute at least 5 percent to 7.5 percent of pay for employees to achieve desired testing results.
- **Relatability.** Most employees have a general understanding of how 401(k) plans work, and this base of understanding helps them grasp cash balance plans. Cash balance plans' hypothetical accounts work quite similarly to 401(k) plans, so it's usually not overly difficult for sponsors to gain buy-in from employees when introducing a cash balance plan.
- **Protection.** Cash balance plans are qualified plans. That means that in a financially troubled business, the assets are protected from creditors.

BDO INSIGHT: CASH BALANCE PLANS ARE WORTH A LOOK

While most employers assume that 401(k) plans should be the primary retirement benefit they offer employees, cash balance plans can add significant value to a company as well. In the race to attract and retain top talent, cash balance plans can be an important tool. In addition, the tax savings realized by implementing cash balance plans can help fund other company retirement plans. Contact an ERISA Compensation and Benefits team member to learn more about whether cash balance plans are right for your organization.

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Financial Well-Being for Men: Helping Them Prepare for a Successful Retirement

Many sitcoms and comedians have played with the stereotype that male drivers are notoriously reluctant to stop and ask for directions. According to research, this reluctance to ask for help also affects men as they head toward retirement—and what that means for employees' financial well-being isn't anything to joke about.

MassMutual examined **gender financial issues** and found that men are less interested than women in receiving financial planning services, budgeting assistance, debt counseling and other financial education programs from their employers. Fidelity conducted research specifically for BDO and found that at the end of the first quarter of 2018, 41 percent of men didn't have their investments allocated appropriately for their age group.

This statistic should grab the attention of men and their employers, because it directly impacts the financial wellbeing of employees. Those employees who are worried about their finances, may negatively affect workplace productivity. In fact, a recent **survey** by consulting firm Mercer found that financial stress is costing employers about $250 billion in lost wages each year. As a result, companies should identify ways to improve their employees' financial well-being, and part of this effort should involve understanding their male employees' retirement savings habits.

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MEN ARE SAVING FOR RETIREMENT, BUT…

It's true that men, on average, have larger retirement account balances and prioritize saving for retirement more highly than women. But that doesn't mean that men are doing just fine when it comes to retirement saving.

In its **How America Saves 2018** report, The Vanguard Group found that men and women participate in their defined contribution plans at similar levels overall, however, disparities appear when this data point is analyzed by income levels. For example, only 74 percent of men earning between $50,000 and $74,000 annually participate in their defined contribution plan, compared to 86 percent of women. Meanwhile, men are contributing a lower percentage of their pay to defined contribution accounts, Vanguard found. For example, in that same earnings bracket, women saved 7 percent of pay compared to men saving 6.8 percent.

Fidelity Investments looked at the disparity between how **men and women** save for retirement and had findings similar to Vanguard. The research found that women tend to save a higher percentage of their salary than men (9.0 % vs. 8.6%) and generated a higher annual rate of return (6.4% vs. 6.0%).

HOW EMPLOYERS CAN HELP

As employers look for ways to improve financial well-being across their entire workforce, a good place to start is by gaining a better understanding of the saving and investing habits of various demographic groups of employees. Many record keepers and other service providers can offer information to help plan sponsors better understand their employees' needs. Providers can analyze segments of a company's workforce to pinpoint gaps, learn what motivates employees and offer possible solutions.

For example, plan sponsors may want to look to see if there are differences in the risk profiles of their employees' retirement portfolios across genders, age groups or income levels. With this information, plan sponsors can tailor communications strategies to address any suboptimal investment practices by each group.

Employers also may want to harness some of the recent findings from the burgeoning field of behavioral finance. Rather than simply assuming that humans will act rationally, behavioral finance looks at some of the cognitive biases that affect people's decision-making when it comes to finances. By understanding these biases and tendencies, plan sponsors can better identify some of the traps that employees may fall into and communicate with employees in a way that aligns with how they actually make decisions.

Behavioral finance has found that inertia is a powerful force when it comes to preparing for retirement. Plan designs like automatic enrollment and auto escalation take advantage of the power of inertia and can help put employees on a successful path to retirement. Also, online tools that prepopulate with data from healthcare and retirement plan providers, which remove some of the friction and barriers to good decision-making, can make it easier for employees to take action to improve their financial well-being.

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BDO INSIGHT: EDUCATE EMPLOYEES ABOUT INVESTMENT OPTIONS AND ENCOURAGE FAMILY CONVERSATIONS

The lack of preparedness for retirement is certainly not a gender-specific issue. According to MassMutual's study, nearly three-fourths of both genders (74 percent of women and 71 percent of men) aren't saving enough for retirement.

When it comes to men specifically, Fidelity's finding that 41 percent of men didn't have their investments allocated appropriately for their age group actually represents a positive trend. The figure has decreased 13 percentage points over the last five years. This improvement can most likely be largely attributed to the increased use of target-date funds, which are professionally managed accounts that are tailored to the retirement age of users.

To continue building on this positive trend, employers should educate employees on the importance of developing an appropriate asset allocation strategy, as well as on the tools and investment options that are available for implementing this strategy. This education, along with finding ways to reduce the friction and make it easier for employees to save for retirement, should be an important part of companies' financial well-being programs.

Also, plan sponsors should encourage employees to realize that a family's long-term financial planning shouldn't be the responsibility of just one family member. Rather, all of the adults in the family should be involved in the big picture discussions about saving for retirement, budgeting and insurance.

To learn more about how you can help your employees prepare for retirement and improve their financial well-being, BDO's ERISA team is here to help.

Read more ▶

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