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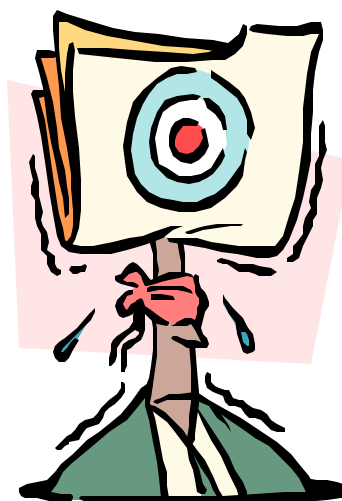
DOL INCREASES PRESSURE ON LATE 401(k) DEPOSITS

Over the past several years, the Department of Labor ("DOL") has devoted more resources to enforcing the rule regarding the timing of the deposit of 401(k) elective deferrals and loan payments. One of the methods the DOL uses to regulate this requirement is the Form 5500. Question 4a on Schedules H and I inquires as to whether the employer has failed to deposit participant contributions in accordance with the time period prescribed by the regulations. The regulations require an employer to deposit the contributions on the earliest date the employer can reasonably segregate the contributions from its general assets, but in no event later than the 15th business day of the month following the month

in which the employer withheld the contributions from the employee's paycheck. Unfortunately, many employers have erroneously interpreted the regulation to permit them to have until the 15th business day of the following month to deposit the participant contributions, even if they could have segregated the funds sooner. We recommend the deposit of 401(k) elective deferrals be made within two business days after payroll.

The DOL has now added language to the 2003 Schedule H and I instructions requiring a plan auditor to confirm the accuracy of the employer's response to question 4a. The auditor will now be required to look at the

Don't be late with those 401(k) elective deferral deposits



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RETAINING EMPLOYEE BENEFIT PLAN RECORDS

Plan sponsors often ask "How long do we have to keep records for our retirement plan?" There are two different record retention requirements under the Employee Retirement Income Security Act of 1974 ("ERISA"). The first requirement involves records to verify the accuracy of any reports filed under Title I of ERISA. The second requirement involves records relating to benefits payable to plan participants.

Verification of Annual Reports

Under Title I of ERISA, a plan administrator must file an annual report (IRS Form 5500) with the Department of Labor ("DOL"). In addition, service providers to the plan may be required to certify some of the information contained in that report. Both the plan administrator and any person who must certify information in the report

are required to maintain records that can be used to verify the accuracy of the information contained in the Form 5500. These records must be maintained **for at least six years** from the date the report is filed. The types of records that should be maintained under this requirement include:

1. Records of contributions to and distributions from the plan, trust statements, in-

- voices documenting plan expenses and other disbursements, and other records regarding plan investments such as loans to participants or unrelated entities, and investment committee minutes;
2. For defined benefit plans, records used by the actuary to calculate the value of assets and liabilities and plan expenses and funding status,

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RESOLVING THE LOST PARTICIPANT PROBLEM

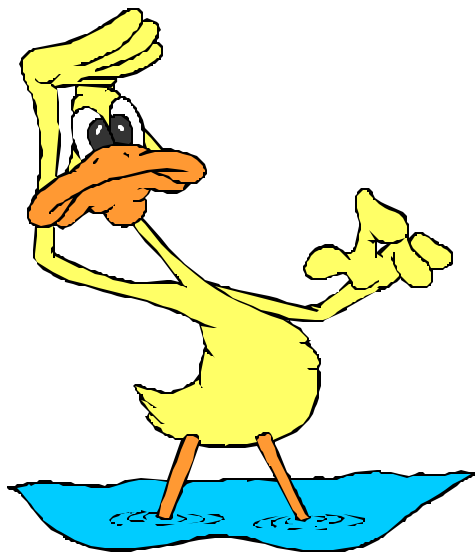
One of the most troublesome issues facing employers is that of lost participants. Lost participants: (i) increase the plan's annual administrative expenses and fiduciary responsibility; (ii) may cause the plan to be subject to the audit requirement because the number of participants exceeds the large plan threshold; and (iii) can cause substantial delays in terminating a plan. Therefore, employers need to be aware of the methods available to resolve or minimize the lost participant problem.

After many years of ignoring the issue, the Internal Revenue Service ("IRS"), Department of Labor ("DOL"), and Congress have provided some options to assist employers in dealing with lost participants.

Options currently available:

1. **IRS Missing Participant Program.** The IRS will assist a plan in locating lost participants. The program is a letter-forwarding program. The plan sends to the IRS the name and social security number of the lost participant, along with a distribution notice enclosed in an envelope. The IRS then forwards the letter to the last known address the IRS has on file. However, the IRS will not provide the plan with the address of the lost participant nor with the results of its efforts. If the plan sends 50 or more letters for the IRS to forward at one time, the IRS imposes a fee. The Social Security Administration also offers similar program.
2. **Private Locator Services.** There are now several private locator services that plan administrators may retain to assist in locating lost participants. Generally, these companies advertise and communicate via the Internet. The main advantages of using a private search company are speed and minimal cost. Often a search takes only a few minutes using the Internet. Many of our clients have reported great success in using a service called APSCREEN (www.apscreen.com/locates.htm).

3. **Forfeiture.** Some plan documents (including the plan document used by REPTech) include a provision that permits a plan to forfeit a lost participant's account if the account balance is less than \$5,000. Generally, the provision requires the plan to send a registered letter with return receipt to the participant. If the letter is returned to the plan, the plan waits for a period of time (e.g., 6 months) and then forfeits the account. The forfeiture approach is a very effective and efficient method for dealing with lost participants. If



the lost participant is later located, the plan provides for a restoration of his/her account. The restoration first comes from current year forfeitures. If the forfeitures are insufficient, the employer must make an additional contribution to the plan. However, once the DOL default rollover provision discussed below goes into effect, the plan only may use the forfeiture/restoration approach for accounts that do not exceed \$1,000.

4. **PBGC.** For defined benefit plans subject to PBGC insurance, the PBGC permits the plans to transfer the benefits of lost participants to the PBGC. Unfortunately, this approach is not available to defined contribution plans, such as 401(k) and profit sharing plans.

A Look to the Future

Default Rollover. One of the more promising methods for resolving the lost participants' accounts is the default rollover. The IRS has ruled that a plan may provide for a default direct rollover of a participant's account to an IRA if the account is distributable and the participant does not affirmatively elect to make a direct rollover or to receive a cash payment. The default rollover option is available for participant accounts not exceeding \$5,000, and for larger accounts where the participant has attained the later of age 62 or the plan's normal retirement age. Since most lost participants' accounts are less than \$5,000, the default rollover should be a valuable tool in distributing the lost participant's accounts. Unfortunately, the default rollover is not widely used at present because of the concerns of the financial institutions regarding (1) the responsibility for the investment of the rollover, and (2) the legality of establishing an IRA without the participant's signature.

As part of the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"), Congress enacted a provision requiring a plan to roll over the accounts of participants that exceed \$1,000 (but do not exceed \$5,000) and are distributable if the participant does not elect to roll over the account directly or to receive the distribution. The new provision, however, is not effective until DOL guidance is finalized. EGTRRA requires the DOL to issue this guidance by June 7, 2004. The guidance is intended to relieve legal and fiduciary concerns of the financial institutions. Specifically, the guidance will provide safe harbors for the investment of the default rollover. Although the new default rollover provision will not solve the lost participant problem for the smallest of the lost accounts (up to \$1,000), many employers are hoping the DOL guidance will provide sufficient comfort to the financial institutions so that they will also accept small default rollovers.

Escheat or Unclaimed Property Laws

Some employers, after making several

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RETAINING EMPLOYEE BENEFIT PLAN RECORDS

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- including demographic data regarding plan participants and information regarding actuarial assumptions;
3. Payroll records that document the employees covered by the plan;
 4. Board resolutions, minutes of board and committee meetings, service provider contracts, invoices from service providers, and other records that document the identity of plan fiduciaries, service providers, and compensation received by providers;
 5. If any plan benefits are insured, copies of insurance contracts, premium invoices, and claims paid; and
 6. Copies of discrimination, contribution limit, and top-heavy test results, and records of all actions taken to rectify test failures.

Substantiation of Participant Benefits

Every employer must maintain records sufficient to determine benefits due, or which may become due, to employees. Proposed DOL regulations issued in 1980 provide that individual benefit records must be retained "as long as a possibility exists that they might be relevant to a determination of the benefit entitlements of a participant or beneficiary." Although the DOL is-

sued a notice in 1993 that suggested it was prepared to consider reasonable time limits on record retention, to date it has not issued any follow-up guidance. As a result, employers should assume that records regarding plan benefits must be maintained indefinitely. The types of records that should be maintained under this requirement include:

1. Census data regarding employees, including birth date, hire date, plan participation date, hours of service during plan years of participation, compensation during relevant plan

years, and class of employment (e.g., collectively bargained, salaried, etc.);

2. Documents, including plan documents, plan amendments, trust agreements, summary plan descriptions, summaries of material modifications, notices to participants;
3. Contribution records, such as salary reduction agreements, payroll records, transmittal records, and deposit records;
4. Records regarding distributions from the plan, such as completed distribution elections, copies of distribution forms packages, check copies, applications for loans, and in-service withdrawals;
5. Copies of qualified domestic relations orders, beneficiary designations, and investment election forms; and
6. Copies of all communications with participants regarding their eligibility for the amount of their benefits, including records regarding any appeals made by participants.

Having assisted many clients with IRS and DOL audits, we have seen requests for most, if not all, of the items noted above. So even though the task of keeping and storing retirement records may seem onerous, it is advantageous to the plan sponsor in the long run.



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employer's deposits to determine whether the deposits were, in fact, made in accordance with the regulations. The auditor then must disclose on the audit report his/her determination in accordance with generally accepted auditing standards. If the auditor's opinion does not agree with the response on line 4a, the employer either must change its response or anticipate a DOL investigation. Of course, small plans that qualify for the audit waiver under line 4k do not have to be concerned with the plan auditor review, but the employer still must respond accurately.

Beginning with the 2003 returns, the DOL no longer requires an employer to report late deposits of participant contributions as prohibited transactions on the Form 5500. However, the employer should still correct the prohibited transaction, pay the excise tax via Form 5330, and footnote the Schedule H or I to indicate to the DOL that the correction has taken place.



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RESOLVING THE LOST PARTICIPANT PROBLEM

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attempts to locate participants, simply take advantage of state escheat or unclaimed property laws and transfer the lost participants' accounts to the state. Unfortunately, the DOL has ruled that ERISA preempts state escheat laws. Therefore, employers should not send lost participants' accounts to the state if the plan is subject to ERISA.

Terminating Plans

For a plan that does not address the lost participant problem until the plan terminates, the plan may find its options limited. For example, if the plan has distributed the accounts of all the participants with the exception of the lost

participants, the plan may find it impractical to use the forfeiture method. The plan may need to rely on one of the other approaches. In many circumstances, plan termination can make some participants' accounts distributable, and therefore eligible for one of the lost participant approaches. A profit sharing plan that is not subject to the joint and survivor annuity requirements can force out accounts that exceed \$5,000 upon plan termination. If the plan is subject to the joint and survivor annuity requirements, the plan should be able to purchase an annuity to allow the plan to terminate.

Conclusion

A plan with lost participants should take steps to eliminate

these accounts to minimize administrative complexity and cost and to reduce fiduciary exposure to liability. For example, a plan that provides for participant direction of investment will not have ERISA §404(c) protection with respect to lost participants because such participants do not provide any investment direction. Accordingly, the plan should develop an investment strategy for such accounts until they are distributed or forfeited. At present, the above options comprise a menu that the employer should review in determining how to rid the plan of lost participant accounts or at least to reduce the number of these accounts. Any option taken should be consistent with the plan language (if any) addressing lost participants.

Help us Move To The Electronic Age



QUESTIONS?

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