Year-end Planning for Employee Benefit Plans

As 2022 comes to an end, the economic event, along with continued COVID-19, has impacted all aspects of business — including employee benefit programs. Now, at year end, we are looking at developments and recommended practices regarding employee benefit plans with an eye toward future potential changes and opportunities.

This webinar recording will discuss actions you can take before year end to help keep the retirement benefits of your employees competitive and safe.

At the end of this session, you will be able to:

- Recognize trends and legislation that may impact employee benefit plans
- Outline recommended practices regarding employee benefit plan compliance
- Identify plan fiduciary considerations

Who should attend

This session is designed for plan sponsors, business owners, HR professionals, finance professionals, and employee benefits managers.

Find additional resources on our event page: https://www.claconnect.com/en/events/2022/year-end-planning-for-employee-benefit-plans

Here is a transcription of this session:

Kelly Davis:

Hello, and welcome to today's webcast, the 2022 Employee Benefit Plan Industry Update. I'm Kelly Davis and I'm a principal in CLA's employee benefit plan practice, and I'm joined today with two of my colleagues, Chip Logan, who is in CLA's wealth advisory practice, as well as Kyle Rose, who also is a principal in CLA's employee benefit practice as well. Couple of disclaimers here, our general disclaimer slide at CLA, and basically just letting you know the content is here for general purposes. If you have additional questions, feel free to reach out to your CLA advisor, your outside advisor, or either one of us on today's webcast.

There's us, and just some general information about CLA to reference back, as you would like. We are a service firm. We do wealth advisory. We do a lot of different types of services. Employee benefit plans is a great practice here at CLA. We do a lot of employee benefit plan audits around the country. We're ranked number one, as the DOL ranks us against our peer firms. So we do quite a bit in that area, as well as employee benefit, tax, and consulting.

Today's objectives, we're going to touch on some trends in legislation. Some things have been going on this year, as well as outlining some practices for employee benefit plan compliance. Those on the webcast today that have gone through the new employee benefit plan audit standard for 2021 on the plans, we're going to revisit that and talk that through. Kyle is going to touch on some things there, as well as looking at some plan fiduciary considerations as well too. So with that being said, I'm going to go ahead and turn it over to my colleague, Kyle.

Kyle Rose:

All right. Thanks, Kelly. Appreciate the introduction. Once again, my name is Kyle Rose and I'm a principal here at CLA, and we have a lot of great content and insights to share with you today. I have the privilege of kicking off this first block, where we'll talk through some past, present, and future legislation as well as some current trends that we've identified in the employee benefit plan space.

First, we'll talk through some required actions. So what does management need to do before the end of this year or in future years? We'll talk through some accounting and auditing matters, specifically as it relates to this past year with the implementation of the new auditing standard with SAS 136. We'll revisit cybersecurity with the DOL regulations or DOL guidance that was put forth in 2021. We'll go over some insights there. We'll talk through SECURE 2.0 and some of the proposed legislation that is currently working through the legislative bodies as well as some other general compliance matters, and we'll also touch on diversity, equity, inclusion, DEI, and its influence on employee benefit plans.

So first up with the required actions. If you have made any policy or plan design changes this past year, please make sure those are formalized and you amend your plan before the end of the plan year. It's important that your actual practices align with what your plan document has stated, so please make sure that everything is reflected and amended accordingly. For those that adopted the CARES Act provisions, which was the coronavirus legislation put forth in March of 2020 that enhanced COVID-related distributions and other relief, for the plans that have adopted the CARES Act provisions, those amendments associated with those provisions were required originally to be made by the end of '22, and those were recently extended to be made before the end of 2025.

And then Cycle 3 plan restatement. The IRS requires that plans be restated every six years. The most recent restatement requirement due date was July 31st of 2022, and this was for defined contribution plans, 401(k) plans, and it covers all legislation through January of 2017. This does not include 403(b) plans. Their latest cycle was due on June 30th of 2020. So if you have not had your plan restated, please make sure that is done as soon as possible.

Moving on to some accounting and auditing matters. I just want to provide some reflection on SAS 136. This was a new auditing standard that was effective for plans with year-ends on or after 12/15/2021. So this impacted the calendar year '21 plans as well as any future fiscal year plans. The purpose behind this auditing standard was to provide additional transparency and clarify some of the reporting requirements on the auditor's report. It eliminated the limited scope terminology and replaced it with essentially referring to the code of 103(a)(3)(C).

It also removed the disclaimer of opinion on the financial statements and allowed for a unique, two-pronged opinion to be issued specifically for 103(a)(3)(C) plans. It also had some additional requirements for auditors and communication on engagement acceptance, risk assessment, making sure the plan Form 5500 was substantially complete, as well as obtaining certain representations for management, as well as requiring certain reportable findings to be communicated with those charged with governance, which we'll go over here a little bit later in the presentation.

One of the other items associated with the new auditing standard, SAS 136, is that it's moved the burden of qualifying for a 103(a)(3)(C) audit onto management in ensuring that the certification is appropriate and able to be relied on. So I just wanted to share some insights associated with the certifications or some issues that sometimes come up in reviewing the certification.

So if you're managing or in governance over a plan, please ensure that your certification is appropriate, as we've noted issues pertaining to certain certifications, and those include not specifically identifying the plan name or not having the certification attached to the investment information, having the certification only speak to the completeness or accuracy of the investment activity and not both, having

it not signed or not signed by a authorized representative of the qualified institutions, or not covering the entire audit period or not covering all the investments that are held by the plan.

This next slide gives you an example of the template, certification language, which basically, in its most boiled-down standing, shows that the qualified institution is certifying that the report that it's offering pursuant to the specific code is complete and accurate. So if the certification that you receive has additional verbiage or additional wording associated with it or caveats, please make sure that you understand specifically what that verbiage is stating and regarding, and make sure that you follow up with your qualified institution to make sure that you understand that the certification is appropriate.

And then I talked about the reportable findings earlier. So this is a new requirement under the auditing standard and essentially identified instances of noncompliance or suspected noncompliance with laws and regulations or with a plan document are now required to be reported specifically to governance, as well if there's any significant findings or internal control deficiencies that are deemed sufficient or significant to report to management.

All right. Moving on to cybersecurity. This continues to remain a hot topic for a lot of our clients and individuals that we speak to. There are a lot of assets and sensitive data that is held within these employee benefit plans, which make them really attractive targets to cybercriminals. Because of that, in 2021, the DOL put out specific guidance related to plan sponsors in order for them to maintain best practices and maintaining their cybersecurity.

And some of those best practices just include making sure you have a plan, making sure you're aware of where all your data is held, who the users of your data are, and making sure that you have appropriate safeguards and steps in place to essentially ensure that the data is secure and that you have policies and procedures in place to deal with any incidents. If you have specific questions on cybersecurity, CLA actually did a specific webinar on cybersecurity back in 2021, and that recording is available on our website if you would like to view it.

All right. Moving on to some of the proposed legislation that's currently working its way in the legislative bodies right now. You may see SECURE Act 2.0 in the news, and it's really a combination of three different proposals, the Securing a Strong Retirement Act, as well as the EARN Act, and the RISE & SHINE Act. So some of these were put forth by Congress and some by the Senate. The legislative bodies are trying to currently reconcile all three. There is a lot of momentum and bipartisan support to push this legislation through before the end of the year, but currently, these bills have not yet been passed into law.

When and if they do pass here in the next few weeks, expect to hear from CLA on more information, but right now, we can only speculate as to what would be in the final legislation. But the common theme with all three of these is making retirement savings plans more accessible to Americans and making sure that their retirement savings is increasing. All three of these contain hundreds of different provisions, but many of them do overlap. So, right now, the process is reconciling all three and moving it forward.

Some of the proposals that are in these three include making automatic enrollment mandatory with a minimum 3% contribution rate, with annual increases up to 10% while still allowing participants to opt out. There's also provisions for increased catch-up contributions for those specifically between the ages of 62 and 64, essentially allowing them to contribute an additional $10,000 per year. Currently, the proposed catch-up limit is 7,500 for 2023.

Another provision is allowing employers to match on student loan repayments as retirement contributions, and this would not require the employee to contribute any personal money into the plan, but simply allowing the employer to match student loan repayments on their behalf. Increasing the required minimum distribution age from 72 to 73 with its stair-stepping in future years, and allowing

403(b) plans to enjoy multiple employer plans. There's also a provision of reducing the number of part-time employees with 500 or more hours to participate in a plan. Currently, the provision is for those employees to work three years and the provision or proposal would reduce that down to two.

And then in line with giving individuals more access to their funds without penalties, there would be a provision to remove withdrawal penalties for individuals experiencing emergencies to withdraw $1,000 per year without penalty and allowing survivors of domestic abuse access to their retirement accounts up to $10,000 without incurring a penalty. So with that, I am going to pass it back to Kelly to go over some more general provisions.

Kelly Davis:

Thank you, Kyle. So I'm going to touch on a few related compliance matters, and one of them is required minimum distributions. Now, there's been some changes through the pandemic and delays and whatnot for access and the requirement to take an RMD. So, as we know, the SECURE Act delayed the required beginning date for individuals to take an RMD until after December 31st, 2019. So we're in that year right now where, as plan sponsors and retirement plan administrators, to make sure those distributions for 2022 are happening before December 31st. For those who attained their required beginning date in 2022, the failure to distribute that creates a tax issue, excise tax issue, for the individual and it's fairly significant.

So make sure you're working on that with your third-party administrators and getting those distributions out as required. Now, there is some transition relief that just came out from the IRS for both qualified plans and IRAs. Both are subject to the RMD rules. And really, it's to the extent that a taxpayer didn't take an RMD in 2021 or 2022 that they were required to have done. There's going to be no consequences to the plan, and the excise tax may not be assessed for failure to distribute, and the taxpayer, if, by chance, they already took an RMD, they may request a refund.

So you may want to dive into that a little bit more with your third-party administrator back up to 0.1 under the SECURE Act and those distributions that should be going out, and also the implications of the relief and how that may impact participants in that particular fashion. Okay. So, student loan debt relief. This has been obviously a big topic on many different genres in the government and whatnot through the pandemic, and some other types of relief I'm going through with debt relief on student loans and employer-provided assistance.

So the American Rescue Plan Act provides relief, additional relief, for student loan debt, and essentially, what it does is it modifies the income tax treatment of student loan debt cancellations to exclude any amount of private or federal student loan debt that are forgiven after December 31st of 2020 and making, essentially, these tax-free through 2025. So prior to the enactment of this particular law, student loan forgiveness was excluded from a recipient's taxable income in only very specific certain situations. There was criteria that needed to be satisfied in order for it to not be a taxable event.

This relief essentially provides some tax forgiveness there through 2025, and then also, it provides some additional relief to the temporary suspension of the student loan payments and employer student loan benefit under the CARES Act as well. Another law... There has been so much laws, I've been going on, through the pandemic and CARES Act with all these different concepts. So the Consolidation Appropriations Act, this is one that was signed into law, and this is where it provided the opportunity for employers to provide loan repayment assistance to their employees up to $5,250 per employee, an employer-provided repayment assistance.

So it's different than the debt relief on the previous slide. It's different from the government-funded relief applying to the Biden administration for student debt relief there. But this is essentially, if an employer wants to provide through an assistance, an educational assistance program, they can do so

and provide this benefit tax-free to an individual. And the interesting thing is that this law, it has been expanded to include that the student debt doesn't necessarily need to be related to the current employee's employment with the employer.

So they could have incurred that student loan with the previous employer or in school prior to joining the company and they're at current date, and if that employer decides they would like to do this type of program, they can certainly exclude or use that loan that was incurred prior to employment to assist that employee if they would like. So in order to be able to do this, there are certain criteria. There is a written program that should be developed. Your HR consulting firm should be able to do that or legal counsel to implement and have a documented educational assistance program that complies with Code Section 127, and this would fall underneath that as well.

And then the last bullet here, in addition to the program requirements, this is something... and the tax-free assistance from the employer, a matter to consider, and this hasn't been addressed. And so, I've been bringing it up when I've been talking with our clients, just their thoughts on providing such a program, as they work through it with either their HR consulting firms or legal counsel, is that if you're... There's no indication at this point in time if an employer is providing tax-free debt relief, but then if someone goes out to the Biden administration and tries to discharge or fully discharge their student loan under that eligibility, would that have an impact to the tax-free employer assistance?

So just something to consider there as you're having some conversations if you have a plan like this. And if you're looking to have a plan like that, that there's also that piece of it where folks could potentially have a portion of their student loan forgiven under the government, the Biden administration, and whether or not that would become a taxable event to the individual in kind of a roundabout way. So, just thought I would touch on that, potential matter to consider.

Another topic is... And I know Chip will be talking about this one as well too, touch on a little bit, but cryptocurrencies as retirement plan investments. The Department of Labor has issued and cautions plan fiduciaries just to have some extreme care in looking at and when they're considering to add a cryptocurrency option into their retirement plan, and the DOL actually did come out with an assistance release to talk through some of the considerations and requirements and their thoughts as far as a fiduciary. You need to act on, obviously, the financial interest of the plan participants and adhere to certain requirements and making sure that the investments are sound.

And cryptocurrency, in the eyes of the Department of Labor, is really kind of... It's tokens. It's coins. It's everything that's out there. They're really hard to value. They're hard to understand. And so, the DOL cautions fiduciaries of putting something into a plan that most people may not necessarily understand and could essentially become a worthless investment, potentially. With the markets, it's a very volatile type of investment, and Chip can add to that. He's kind of on the investment side.

But as part of this notice and the DOL's concerns, they do expect to do investigations and have an investigative-type program that's going to be aimed towards cryptocurrencies that are included in the retirement plan. I'm sure there'll be some reporting on the 5500 that will be added. That would be my guess, for the DOL to flag these types of investments. And the DOL does expect, through this process, that if they do investigate an organization that may be offering such a type of investment, that those plan fiduciaries have some set prudence as to how they determined that this would be a good investment for their plan and have done their due diligence and monitoring it and whatnot.

So it's not that it's not available. It's just that the DOL is just concerned about the type of investment and just the volatility of it, and it's something that most investors don't have a good grip on at this point. One other... I think Kyle may have touched on this one a few slides back to you, but this one's been out there for a while with the SECURE Act, and this is essentially allowing long-term, part-time employees to have the opportunity to be allowed to make 401(k) contributions. And under this particular rule, it's

going to be anyone, employees who work at least 500 hours during each of three consecutive 12-month periods and who are at least aged 21.

So you should be, your employer should be, or your TPA should be tracking the hours starting in January 1 of 2021, because this goes into effect for this group of employees January 1st of 2024, and you need to look back the three years for the hour requirement, the age requirement to make sure that these people are going to be having the opportunity to defer into the plan. It's a mandatory-type change and it's just on the 401(k) deferral side of it. There'll be some vesting components in there as well too. Hopefully, you are working with your TPA or TPAs or tracking these hours for these part-time folks, but something to... If not, definitely have a conversation as to how to identify those folks that may be impacted on January 1st of 2024.

And I'm going to touch on just real quickly on some IRS compliance priorities on employee benefit plans. This is available on the IRS website, but each year, they come up with different types of compliance priorities based on different types of things that they come across, and this is not all-inclusive as far as examinations and the DOL examinations. Those are always a constant, ongoing type of an event outside of their certain priorities, but I just thought it would be good to touch on a couple of these, worker classification, especially with retirement plans the DOL is looking at, and I've had quite a few situations.

I've talked through this with several employers that have been in this situation, where they may have independent contractors but they may not necessarily be independent contractors and they should have been really classified as W-2 employees. I mean, there's some criteria to work through there, but the concern here both on the IRS and the DOL side is that, should they have been in the plan? Should they have not been in the plan? Is there a tax issue with certain types of FICA if you're a 1099 independent contractor versus a W-2? So it does impact different types of things that both the IRS and DOL have concerns there, and can obviously impact your retirement plan if you have folks that should have been in that weren't or vice versa.

The IRS is also looking at small employers and tax-exempt organizations. They're looking at plan investments, whether there's any party-in-interest transactions, if there was any loans from the plan to a CEO or a CFO, party-in-interest. There's a tax event there. General participant loans that are going out to a participant in these small plans. Are they being repaid timely? Are they not? And if there were any probate transactions and also distributions coming out of the plan that are not reported properly on Form 1099-R to the recipient.

IRS is also looking at one-participant 401(k) plans, very similar to the... These are very small plans for generally owners and a spouse, and the IRS is looking at these. These can fall under the radar as far as operational compliance failures because they're not audited, either are the small employer tax-exempt plans either, but they tend to have some of the concerns with excise tax adjustments, operational failures back to the distribution, plan documents generally are extremely outdated with these plans, if they even exist. So they're looking at that.

Again, required minimum distribution, another topic there. They're looking at just making sure those are being complied with and distributed. Here's the tax. It's 50% on the amount, not distributed, so it's a very hefty tax if those distributions don't go out, as they should, given the recent guidance there too, but that's the main gist with the required minimum distributions that they're looking at. And then the IRS does do some general just compliance checks and inquiries. I don't know. I mean, if you...

A lot of plan sponsors, employers receive a checklist or some type of notice from the IRS and just walking through, asking different types of questions related to plan compliance, reporting. This can be both large and small plans. And so, they're just looking for just general information, and it's required to be responded. If you do receive one, it doesn't necessarily mean it's going to result in an examination

from IRS or DOL, but something they're looking for, just general information on your plan. And if you get one, reach out and make sure you respond and evaluate what the inquiry is asking.

Two more. They're also looking for unrelated business income tax on Form 5500. This just generally occurs if there is some type of an investment in the plan, such as real estate or something that's generating income to the trust. There is a tax due on that if it's more of an unrelated business-type transaction or investment within a plan. And so, this is where IRS is looking to make... probably on the 5500 reporting on these types of investments to determine whether or not there should have been a 990-T and a tax filing due on those particular assets.

And then one last point here for our tax-exempt folks, the million-dollar excess compensation that went into effect for plan years or filing years after 12/31/2017. This continues to be an item of concern for the IRS. There's been a lot of employers that did not file as they should each year, if it's required. So, generally, a 21% tax is due on compensation paid to covered employees that exceeds $1 million each year, and it's a payment taxed by the employer to the IRS. If it doesn't apply, it doesn't apply.

But I have seen some inquiry notices coming out from IRS to tax-exempt organizations because they're looking at the W-2s that are being filed under the tax-exempt. They got the EIN number, and so they're cross-referencing that, in my opinion, whether or not the 4720 filing and tax was paid when they see an employee that has been paid over $1 million for a tax year. So just wanted to touch on that one because that one seems to be one that has been flying under the radar for quite a few organizations and seeing some activity with the IRS on sending out notices and things to that effect.

And before I am going to hand it over here to Chip, we added some slides here just on the increases for the cost of living, for employee benefit plans, for deferrals and catch-ups and the annual limit, the compensation limit, as well as the changes for health and welfare plans, and also some changes here for the Affordable Care Act, IRS reporting with respect to the safe-harbor percentages and the penalties have gone up. So this is not intended to be an all-inclusive list, and this list is also available on the IRS website as well too, but that I would just add a couple of just overview on that for your reference.

And then just a couple things here for diversity and inclusion and equity. This is touching on how to bring folks into the plan and offering more of the opportunity to get folks to participate from different age, race, gender groups, and that's kind of looking at a strategy of maybe automatic enrollment, automatic escalation, doing different types of participant groupings, and doing a deeper dive into strategizing around your plan design to include more... as a consideration, include more folks into your plan, and then also some retirement education as well too.

So with that, I'm going to pass it over to... Oh, I got one more slide here. Best practices for year-end. No, Chip isn't going to cover this one. So here, we just summarized in a couple slides just from our opinion, just from our experience in general of payroll records and just looking at definition of compensation. Compensation, that's always a big one, for big plans, small plans, just the pay codes, payroll systems. If you're doing a bonus, if you're not doing a bonus, does the bonus... Is that included in compensation for the retirement plan contributions? Is that included? Fringe benefits as well. Just some general examples. That one's always an issue with a lot of plans. Plan loans, policies.

Big one here is making sure that there's repayments happening timely. RMDs, we kind of covered that. Internal controls, obviously having some segregation of duties. That helps in that particular area. Plan documents, summary plan descriptions, making sure everything is up-to-date and you're operating your plan in accordance with your most current plan provisions and just staying on top of that. That's where things can create some operational issues with the plan, and some compliance.

And there's been so much change, as Kyle had mentioned, with the recent updates for retirement plans and 403(b) plans and the SECURE Act and all these different changes, CARES. There's a lot of moving

parts that may have happened to your plan in a written form that may not necessarily been translated to operation. So just a best practice to take a look at that. And then eligibility with regard to any leasing employees, missing participants, tracking down anyone that may have received a distribution, and there's just stale checks out there that maybe there was some distribution on plan assets and the checks haven't been cashed for quite some time.

And then also contributions, of course, on the deferral side and loan repayments. That's a big DOL one there. They're always looking at that, making sure that participant contributions and loan repayments are remitted timely to the plan, and making sure you have a good fidelity bond compliance with ERISA bonds. And then one last slide here before I turn it over to Chip, and then mergers and acquisition. There's been a lot of activity here. There always is, in my opinion, but certainly over the last year or two through the pandemic, we've just seen, I, a big uptick in M&A activity, and this creates a lot of things that employers both on sides of the transaction, whether you're the seller or the buyer, who's winding down the plan, where is it going, who's taking it over?

And a lot of times, a lot of these issues don't come up in the due diligence process until either at post, the transaction's closed, or two days prior to the close or somewhere, you've got it down to the nth hour, and all of a sudden, all the attorneys are like, "Hey, we need to talk about all these employee benefit plans." And it's not necessarily your retirement plans. It's your welfare plans. It's COBRA. It's whose money is out, the contracts, payouts, ACA reporting, payroll.

Get downloads of all the information, because at some point, if there's an issue, whether it's IRS examination, DOL examination, failure to file your ACA reporting or questions, that information needs to be available somewhere to be able to address a lot of these things, and also through a plan audit, when we're doing an audit of a plan and there's a new TPA or it's going through a merger and acquisition. You still need to look at both sides of the records of the transaction from a plan audit perspective as well too. So this is a big one if you're contemplating a transaction or looking at a transaction, whether it's a small organization, a large organization, tax-exempt, for-profit. These all apply unilaterally across the board. So with that, I will now pass it over to Chip.

Chip Logan:

Thank you, Kelly. I am that elusive Chip. So I appreciate it. Hey, there's a lot of information in this presentation, and what we really wanted to provide was some information, some talking points, but also the information that you could refer back to. And so, Kyle, Kelly, and I are all hoping that out of this presentation, there are three or four or five things that kind of click to you and make sense to look at and address.

Before I get into the slides, Chip Logan. I'm with the advisory side of our retirement plan business. And so, I work exclusively with retirement plan sponsors and the investment committees just to make sure that we have things running well, whether it is compliance, whether it is the investment platform overall, whether it is things like recruiting and retention through the retirement plan itself. And so, that's the role that I've been doing for a number of years here at CLA and absolutely love.

This first slide, I was questioning myself as I was typing it out thinking this just feels wrong, when I work with committees, when I work with plan sponsors, talk about the fact that the markets shouldn't impact how we're managing the plan, but this has been a different year. And so, if you'll indulge me, I'd love to cover just a couple of items. It's a great slide that Vanguard put together. They've got three actually that I'll go through. And this first one looks at the stock market, so it looks at just the stock market returns for the first three quarters of the year going back to 1928.

So it's a histogram giving that snapshot in time so that you can see where we are compared to other years, and you can see that we are way out in the tail of the returns. In this case, at the time, it was

negative 24%. We've had a rebound since then, and so we're at negative 17% as of the close of yesterday. I have no idea what's happening today yet, but that's where we stand right now. Still, it's an outlier. We couple that with the bond market, and this looks at the US bond market in that same period of time, again, for a three-quarter-of-the-year return.

And again, this is the furthest out of any of those years. This also has come back in. We're at negative 11% right now, but I think that the big thing to recognize here is that we've always depended upon the fact that there is a low correlation between stocks and bonds. And so, when we put them together, they act in a way to dampen negatives. Stock market takes a dive, bonds go up. Bonds come down, stocks go up, and we've always had that.

Let me go back. If we look at a 20-year number for correlation, the number is 0.14, with 1% being perfectly correlated. This year, you take a look at one year, it's 0.7. So that's five times the correlation that we had in the past and the impact on a balanced fund. Again, we've had things come back. We're probably around 17% right now instead of the negative 20, but that is horrible. And so, how does that impact, and why are we talking about that? I'm going to be really quick on defined benefits because I know that most organizations don't have defined benefit plans, but if we take a look at defined benefit plans, it is that vested benefit that has to be paid to employees and to the participants of the plan. When we're unfunded, we've got to fund it. Okay?

If we take a look at even a heavily weighted fixed-income bond portfolio, because these tended to be conservative, we're probably still looking at a 14% loss. If we add in the fact that these plans have an expected growth that gets added every year between 2 and 5%, it's easy to take a look at a situation where we've got losses of 18% from the beginning of the year to the end of the year. The impact is putting that 18% back in even before we owe the money for the following year. If we don't put it in and your plan is subject to the PBGC, Pension Benefit Guaranty premiums, those premiums are a function of how much is unfunded. Those get calculated, and this gets wonky and I apologize, but those get calculated based on old interest rates.

So it's based on the interest rate for most plans of December 2021, corporate bond yields, December 2021. That's the metric that gets used to calculate how much the premium is. The lower the bond yield, the higher the premium. We've got a confluence of events of low corporate bond yields in December of 2021 and a drawdown in most portfolios just because of the way that they're constructed. If you have a defined benefit plan, please take the time to talk to your actuary and your advisor if you haven't already, just to make sure you know where you stand going into next year.

If we flip over and take a look and talk about defined contribution plans, again, 404(c), what does it say? It says that if we give diversity in choices and we have a due diligence process to make sure that those are good choices and we give the employees those choices, that it's kind of on them what happens with market swings. And with that, we've got a lot of baby boomers retiring. We've got employees who are experiencing losses. Unfortunately, employee behavioral finance too often drives people to pull money out when they've lost and not get back in in time. And when we see these losses, our risk, obviously, is that unhappy employees are going to look for somebody to blame and litigation could very well be the result of that.

And so, with that, we'll get into some litigation, we'll get into some trends, but the first thing I want to touch on here is just a quick refresher. I know that most of you are very familiar with this slide, but ERISA, it's a process code. It is not a... You have to have the best investment. You can't lose money. And so, if we follow the process, we're going to have a defensible position. That's where we want to be. It's something that we should all be considering at this time because the market swings, again, could easily, and I would submit, has led to litigation.

We want to act solely in the interest of plan participants. I'll bring that up again a little bit later. Obviously, prudent. We want to follow plan documents. We want to make sure that the expenses are appropriate for the services and value that we're getting. We want to have, in terms of the process, governance around it. We want to have some meetings, the investment policy statement, the IPS, and make sure that we're documenting what we're doing.

Looking at recent litigation, we've got more than 30 excessive fee cases in 2022, so that's continued. And as these cases come through, they start coming down in size. And so, where it used to be just billion-dollar plans, it is coming down. I'm not going to suggest that it has come down where you have a lot under 50 million. Most of them are still north of 100 million, but we do have a lot of cases. The Supreme Court came back with a ruling on Hughes versus Northwestern University earlier this year.

One of the interesting things I took away from that was a really specific line in there that I've got copied that it's not just providing good options for the employees to choose from, but it's also removing imprudent ones. So that's something that... I don't think there has been the level of clarity before. It's something I think we should keep in mind. That might be on the uptick as well.

In terms of target-date funds, and I'll get into the weeds a little bit here on additional slides, but in terms of target-date funds, we've seen eight recent cases. Here's something that we probably could have figured out and should have projected. If we took a look at the roaring teens, four or five, six years ago, all of the litigation in and around target-date funds was in and around excessive fees. All right? Participants coming back and saying, "Look, you put it in an active manager. I could have done just as well with a passive manager, and so I'm going to sue."

That's not what we're seeing in some of these new target-date funds. We're seeing excessive risk. In the teens, in that period of time that we just got through, we had markets going crazy. It was a fun time to be in an investment advisory role because everything was going up. All right? With that, what did the companies managing target-date funds do? What they actually did was they were pressing down on the fees and they were increasing some of the risk. In other words, the glide path was going up in risk. Now we're seeing the recent cases around target-date funds being around excessive risk. And so, that's a new metric.

In 2013, again, a lot of you might be very familiar with this and I won't read through the whole thing, but the DOL did give us guidance and said, "Look, when you're looking at target-date funds, make sure you have a process, make sure you're taking a look at things like the glide path, consider whether you want it to be an active or passive target-date fund, and make sure you got a process for communicating that to employees as well."

There was a study done that showed that more than a third of plan sponsors said that the way they came about came to their target-date fund with their advisor recommended it. That doesn't fit into a fiduciary process, needless to say. And so, I'd encourage all of you to make sure that you've got even updated analysis that your target-date fund is doing what you want it to do and is appropriate for your employees. There's some good options out there now.

Managed account litigation. This is not too far off in some ways of the discussions around target-date funds. The DOL came out with the different types of investments that were appropriate for a qualified default investment alternative, a QDIA. All right? A balanced fund was what everyone started working with, and then we got to managed accounts and target dates being a kind of managed... Excuse me. Allocation models, and target dates being a kind of allocation models.

Managed accounts is that next level. What's going on right now is, the payroll companies are feeding information that they need to the record keepers. The record keepers are saying, "Look, we know more than a participant's age. We actually know how much they make, what percent they're saving, how

much is in their account. And if the person is going online and adding in and aggregating information on our site, we know even more information about them. And so, we can have a customized... We can use this data and we can create more of a custom allocation for that individual."

The personalization is great, and that's a wonderful thing. It also actually increases employee's deferral rates and makes it so that when we go through market swings like we have this year, they're less likely to pull money out. All that stuff is really, really good. Gosse versus Dover is the first managed account litigation that I've been familiar or I've seen. That came out just in August, so we have no idea what's going to happen with it, but one of the pieces was, it addressed excessive fees in managed accounts.

Callan did a study last year that said that 71% of plan sponsors were not benchmarking the outcomes. All right? A managed account is something that is frequently just an opt-in situation, and so the employee is making that choice to go with it. It doesn't mean that it takes away our fiduciary responsibility to make sure that those are appropriate fees, and the industry really doesn't have a good framework right now for taking a look at how to benchmark the managed accounts. And so, it's something to consider. I'd make sure that in taking a look at managed accounts, you're doing a good, solid review and taking a look at these things.

A couple of other just really quick things on the managed accounts. Take a look at the disclosures to make sure that you're comfortable with the way the record keeper is disclosing them. Sometimes, it can be fairly fine print, fairly deep end. You might want to overlay with additional communication about the fees. Okay? It can decrease record-keeping costs. So think about this. There's a whole bunch of us, but all of us are fiduciaries of the plan and we're in a committee and we have a record keeper come to us and say, "If we add in the managed accounts, we will decrease your record-keeping fees." Okay? That feels great, but that's a little bit of an offset that they're capturing more revenue from the managed accounts, and so they're decreasing their record-keeping fees.

I'd be cautious of that. Working solely for the benefit of participants, you got to be careful to make sure that you understand how services are being paid and that it's fair across. Okay? There are also some 401(k) advisors who will make more money if the participant goes into the managed accounts, another item that I would just be aware of and make sure that I'm reviewing. I'm going to really quickly just go through a couple of trends and then open it up for questions.

We do have record keepers doing great stuff with technology, pulling in HSAs, pulling in student debt assistance, things like that, some huge value. We've got a lot of plans out there that you might have been with a record keeper for a number of years. If you haven't looked into payroll integration, 180 or 360, so payroll and your record keeper are talking to each other, huge benefit in getting rid of problems and making sure problems don't happen. Last year at this session, I know we talked a little bit about pooled employer plans, PEPs. That's really brought about more of an interest in an administrative fiduciary, a 3(16) fiduciary, and that continues to grow.

It can be a great way to offload plan administration to a company that just does plan administration. Okay? Behavioral finance continues to be something that, as an industry, we focus on. ESG, we talked a little bit about last year. Interesting. It's slowed. The adoption of ESG has slowed. It's not that it's backtracked. There's still more and more of it, but the pace has slowed dramatically, and participants aren't using it quite as much as they used to.

One last item. Just like the managed account, there are some target-date series out there that have gotten creative, and in using the target-date series, it can decrease your records-keeping costs. In some cases, those target-date funds have a whole lot of the general account of the insurance company that's providing it, meaning that that general account is where they're pulling in the profit and they're decreasing the record-keeping fees because of it. In some cases, I've seen as much as 48%, the account

balance for somebody at retirement being in the insurance company's general account bucket. Okay? I'd make sure in the target-date analysis that you're reviewing that as well.

That's a whole lot. I appreciate it. I think we're going to go to Q&A. Kelly and Kyle, I can take on... There were two questions that I saw. One, "How many people do you need to... How many people in a company will require you to have a 401(k)?" Okay? There is still no requirement for that at a federal or state level. You do have state programs that are offering options if you don't adopt a 401(k). The other question was, "A minimum number of people to have auto-enrollment." It could be that certain record keepers have that as a number, but as a rule, record keepers love auto-enrollment. And so, to a large degree, I haven't seen companies, record keepers put a minimum on that.

Kelly Davis:

Mm-hmm.

Chip Logan:

Kelly, do you have...

Kelly Davis:

Yup, and I think... Yes, and I think too, with the types of 401(k) plans that are out there, it kind of just depends on... There's quite a few different options available. The IRS has small plan type, whether it's a SEP or a SEP-IRA. There is different types of programs available for smaller employers. It just kind of depends on what you're looking for, for their... Just some options to entertain.

There is a question here. Chip, I'm going to throw this one to you. "Can you touch a little bit on..." And I know this one comes up quite frequently, speaking of our friends in the small business community. What could they do with respect to fees if they don't have assets that are large enough to have good investment options that help with lower fees versus higher fees? I don't know if you can speak to that point.

Chip Logan:

Yeah. Absolutely, I'll speak to it. A couple of things. The investment fees themselves should be the same investment fees as a large organization. Work with a registered investment advisor to make sure that the share class in the plan is as low as it can be. There are other fees. If you've got a small plan, I will typically recommend to look to see if, as an organization, you can pick up some of the fees, so it's not as much of a drag on the participant's growth of their funds. If you're the business owner, on the growth of your funds as well.

Sometimes, the difference of picking up a couple thousand dollars a year in expense can make a dramatic difference in what the fees are. And so, there are still some great record keepers that work in that smaller space. And so, take a look around. Feel free to give us a shout. We work with that type of plan as well and we're happy to help if we can. Kelly, I'm realizing I didn't mention anything on crypto.

Honestly, with crypto, my experience is that plan sponsors will come to me and say, "Hey, can we put crypto in that?" And I'll say, "Look, our view on crypto is, as a behavioral finance thing, it's got the volatility that's got a lot of risk for employees doing the wrong things over and over again, that we usually encourage employees to look at their 401(k) or 403(b) as their core retirement, and if they want to invest crypto assets on the outside, that's okay."

The response I usually get from plan sponsors is, "Thank you," because they weren't really interested in it. It was one of their participants and they just wanted a good answer to be able to deflect. It's possible.

We can do it. It's just not... To Kelly's point, it is, the volatility can lead to really bad behavior and a lot of losses for participants.

Kelly Davis:

Thank you on that. Another one here, if you want to, or Kyle, "The best way for our payroll and record-keeping vendors, providers to communicate." Any thoughts there?

Chip Logan:

Kyle, do you want to...

Kyle Rose:

So I think that-

Chip Logan:

Go ahead.

Kyle Rose:

Yeah. I think that depends on the functionality of the systems. So sometimes they are bundled products and sometimes they're unbundled. So it's really a matter of, one, finding out the functionality of those systems to determine how they can communicate. So it's asking the right questions and seeing where that path will lead as far as how the data can be transferred and how those systems can communicate.

And I had one other point to kind of reiterize for the cybersecurity and internal controls. We really recommend for the user profiles that are set up on TPA websites as well as the payroll websites to be reviewed on an annual basis to ensure that those that have the ability to access either the TPA or payroll websites, make sure that they are the appropriate individuals and if you've had turnover in staff or advisors or any other outside individuals to ensure that the user profiles have been updated accordingly.

Chip Logan:

One other thought, Kyle, appreciate it, dead on, in terms of having the discussion and having the different vendors discuss what's the right answer. Do know that there are also tech companies out there that will essentially create the technology so that payroll and the record keeper do talk to each other. So if you've got two that are saying, "We don't play nicely in the stand," ask and find out if there is a way to have an integration technology that will do that. Sometimes, that costs as little as 75, 80 bucks per month.

Kelly Davis:

Mm-hmm. Yeah, I agree. And I have one last question here before we wrap up, because this one has come up quite a bit, but whether or not we're going to do a separate cybersecurity webinar. CLA did do a webinar. Kyle, was that back in 2021?

Kyle Rose:

It was 2021. Correct. Yup.

Kelly Davis:

Yup. And that's a really great... Cybersecurity can touch on quite different things, whether it's on the employee benefit plan space or the investment space or a lot of different types of things around cybersecurity from an organization perspective, but we do have that link available. It's on our website, but we can certainly... To those that are interested in looking at that, feel free to reach out and we can certainly send you the link.

Kyle Rose:

All right. Well, I wanted to say thank you again for all those attending our webinar today. An email will be sent out which includes a link to this event, which has the slides, as well as our annual white paper with our year-end comments associated with this content. So once again, thanks again, and have a great day, everyone.