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Ask Kidder.®

Consulting Offices:
Omaha, Nebraska
Albuquerque, New Mexico
Rochester, Minnesota

Regional Consulting and Administrative Office:
Tucson, Arizona

"Deposit Your Deferrals Timely or Pay Sanctions Upon Audit"

This title is an actual message from a local IRS auditor during a recent random exam. A similar message was also provided to a benefits attorney in the Atlanta region. The attorney explained that the IRS imposed a $25,000 sanction for a minor error, which would have historically been negotiated down to $5,000 – $10,000. The size of this penalty is alarming considering the plan had only 60 participants. This provides a warning that we should heed: **do not leave anything in your plan open for IRS or Department of Labor (DOL) scrutiny.**

When Should Deposits Occur to Avoid Additional IRS/DOL Scrutiny?
In our April *Ask Kidder* newsletter, we mentioned the relief provided under the proposed rules for small plans. The article explained the steps needed to avoid extra DOL scrutiny. Following this advice also protects you in an IRS audit. This article can be found at **www.askkidder.com/newsletters**. Here is a reminder:

Does your plan have less than 100 participants at the beginning of the Plan Year?

- If yes, **deposit all employee contributions within seven business days after being withheld.**
- If no, deposit all employee contributions even sooner – as soon as possible after being withheld.
- Reminder: employee contributions are considered withheld as of the paycheck date.

What Authority Allows the IRS to Apply a Sanction?
Employee contributions have been traditionally viewed as the territory of the DOL. However, the IRS has authority over the written language of your plan document. The IRS requires plan documents to state that **employee contributions must be deposited timely**. Thus, the IRS views late deposits as an operational error. Congress grants to the IRS the authority to impose sanctions upon employers whose retirement plans are found to have operational errors.

You are a Potential Target for Sanctions if:

- You deposit a full month's worth of deferral withholdings on or after the end of the month "to make things easy" even though your payroll is not monthly.
- You deposit amounts later than seven days after the amounts are withheld from employee paychecks.
- You wait until the 15th business day of the following month to deposit employee contributions (this makes you an easy target for the IRS and/or the DOL).

Who is responsible for watching deposit deadlines?
Ultimately, the IRS and DOL place the burden entirely on the plan sponsor, i.e. the Employer. Your payroll provider or CPA may be able to assist. Kidder does not have the ability to monitor the lag time between your withholding date and your actual deposit date. To protect yourself from audit sanctions, take the following steps:

- Review your payroll withholding procedures
- Talk to your payroll provider
- Discuss this with your CPA
- Make sure your deposits are made timely

How was the Local IRS Audit Resolved?
The local IRS auditor could not find any other problems other than late deposits. Because of this and due to the relatively small amount involved, Kidder was able to convince the agent to allow self-correction without sanctions. However, we do not expect to be this successful with every audit. If you have any questions about this topic and its effect on your plan, please contact your KBC Consultant or Primary Administrator.

Fee Disclosure Is Here - DOL Proposed Regs saves $94 per participant over 10 years!

The Department of Labor (DOL) has issued proposed fee disclosure regulations for plan years **beginning on or after January 1, 2009.** This 103 page proposal is designed to establish uniform, basic disclosures for plan participants. The intent is to provide critical investment-related information for making informed decisions by using a format that encourages a comparative review of the plan's investment returns and related fees.

The regulations require participant disclosure to be provided on or before plan entry and annually thereafter. The disclosure includes:

Non-Investment Related Fees

- This includes plan administrative expenses such as legal, accounting, and recordkeeping charges that apply to individual accounts
- The disclosure must state how these costs are allocated: pro-rata or per capita.
- The actual dollar amount charged to the individual account for the preceding quarter must be disclosed.
- A brief explanation of each charge must be included.

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NOTICE- Any tax advice expressed in this communication (including any attachments) is not intended to be used, and cannot be used, for the purpose of avoiding penalties imposed on the taxpayer by any government taxing authority or agency. If any such tax advice is made available to any person or party other than the party to whom the advice was originally directed, then such advice is to be considered as being delivered to support the promotion or marketing of the transaction or matter discussed or referenced. Each taxpayer should seek specific tax advice based on the taxpayer's circumstances from an independent tax advisor.

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Investment Related Fees

- Investment related fees can be provided in a chart format which may also display investment returns.
- The disclosure must provide the name of the fund, its website, its average annual returns for 1, 5, 10 years, its benchmark returns, and a fund management explanation (passive or active).
- Fee and expense charts must include the type of fund and provide detailed expense information.

The DOL estimates that this new disclosure program will reduce qualified plan fees by $6.1 billion (present value) over the period 2009 to 2018 for 65 million affected participants. That is a total of $94 per participant over ten years.

Conflicts of Interest, Compensation, and Fiduciary Status — Proposed Regs Under 408(b)(2)

The Department of Labor (DOL) has issued proposed regulations under ERISA Section 408(b)(2) requiring qualified plan service providers to obtain written agreements which disclose all direct and indirect compensation and each potential confiict of interest. Failure to comply with these regulations will result in a Prohibited Transaction (PT). This proposed regulation is **expected to be effective January 1, 2009**.

Under ERISA, almost every party (plan sponsor, trustee, fiduciary, vendor, CPA, investment provider or platform, financial professional) working with a qualified plan has a potential conflict with the plan. In essence, under ERISA everyone is guilty unless they have an exemption. To allow parties to work with a qualified plan and be compensated for services, ERISA provides Prohibited Transaction Exemptions (PTE). Each service provider has to fit within one of the PTEs to be considered innocent and allowed to work with the plan.

Proposed 408(b)(2) provides clarification and states that written agreements are required and they must be “reasonable”. If the disclosures as described above are not made, it is not reasonable and the result is a prohibited transaction. This means the service provider must restore the amount involved which is generally the compensation to the plan. In addition, a 15% excise tax applies.

The service providers covered by 408(b)(2) includes any service provider who:

- Is a fiduciary under ERISA or the Investment Advisors Act of 1940;
- Provides banking, consulting, custodial, insurance, investment advisory, investment management, recordkeeping, securities or other investment brokerage, or third party administration services;
- Receives indirect compensation and provides accounting, actuarial, appraisal, auditing, legal, or valuation services.

Expect a number of new documents and service agreements being generated to outline compensation, confiicts of interest, and fiduciary status in order to achieve 408(b)(2) compliance. Overall, these disclosures will help plan fiduciaries make informed decisions and will help them fulfill their fiduciary requirements.

Reminder – 403(b) Plan Document Requirement and Compliance

In our April issue, we discussed the new requirement for all 403(b) plans to have a written plan in place **by January 1, 2009**. This article can be found at **www.askkidder.com/newsletters**. As a response to the final 403(b) regulations, many 501(c)(3) organizations and school districts are reviewing their entire plan model. In addition to resolving the plan document issue, many are reducing the number of investment providers due to administration and compliance issues, such as:

- Eligibility monitoring
- Hardship withdrawals
- Participant loans
- Section 402(g) deferral limits
- Section 415 contribution limits
- Form 5500 filing
- Audit requirements (for larger plans)

There is also a trend to move closer to a 401(k) service model by offering only one investment platform supported by a Third Party Administrator. This simplifies the process, reduces liability, and provides for better controls.

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