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On November 16, 2007, a variety of regulatory agencies, including the Employee Benefit Security Administration/Department of Labor (EBSA/DOL), the Internal Revenue Service (IRS) and the Pension Benefit Guaranty Corporation (PBGC), published revisions to the Form 5500 Annual Return/Report for Employee Benefit Plans for 2009 in the Federal Register.

These new regulations mean beginning in 2009, employee benefit plans sponsored by not-for-profits with 403(b) plans will be subject to the same reporting and audit requirements as *Employee Retirement Income Security Act* (ERISA) plans. Smaller plans (defined as those with 100 or fewer participants) are generally exempt from the audit requirement.

With these changes, plan sponsors face a variety of challenges. Those include establishing plan accounting records and proper controls, identifying all participant accounts to be included in plan assets, determining beginning account balances and other financial information for the plan's financial statements. Be aware under the structure of many outside administrators, it is fairly common for 403(b) plans to have participant records that are difficult to "roll up" into plan-level records.

These new regulations have led to numerous inquiries and questions by not-for-profit organizations. Here are some of the most frequently asked questions and their answers:

Q Why have governmental agencies increased regulations on these entities at a time when so many other issues are facing our country?

A These changes have actually been in process for a considerable amount

of time. Reports of fraudulent activity and other violations have been an issue the DOL has been concerned about for a number of years. During a recent inspection by the DOL, the agency found violations in 78 percent of 403(b) plans reviewed. The DOL provides oversight to the nation's retirement plan system and its leaders feel these changes are warranted to protect plan participants.

Q Are there additional requirements beyond the new Form 5500 and audit requirements for 403(b) plans?

A Yes. There must be a written plan that meets the requirements of the final regulations. As part of these plans, organizations must:

- ◆ Identify vendors approved to receive future contributions
- ◆ Allocate responsibility for administrative tasks with approved vendors
- ◆ Notify nonapproved vendors
- ◆ Make sure the plan is available for all eligible employees
- ◆ Determine if the plan is subject to ERISA

Plan sponsors should have written service agreements with each approved vendor. There also are certain exceptions to the universal availability requirements.

Q Even though our organization has more than 100 employees, only about half of them are contributing to the plan. Since that number is well below the threshold established by the DOL, we should not have to go through the audit, right?

A Wrong (probably). The DOL definition of participant in the plan is not necessarily what most people would define as a participant. A participant for DOL purposes is any employee who is

eligible for the plan (whether they choose to contribute to the plan or not). It also includes any former participant who has left employment with the plan sponsor and has left funds in the plan. The determination date for whether the plan is considered a small plan (most likely no audit requirement) or a large plan (definitive audit requirement) is the first day of the plan year. Certain small plans that use "non-qualifying assets" or do not respond to participant requests for plan information may still have an audit requirement. The DOL anticipates approximately 7,000 403(b) plans will be considered large, while another 9,000 plans will be counted as small for 2009.

Q What is this 80/120 rule that affects whether we have an audit requirement?

A When ERISA was first rolled out in 1974, private industry raised major concerns about the 100-participant threshold. The primary concern was over plans that would always hover at around 100 participants and the confusion caused by a participant count that would fluctuate to just above and then to just below the threshold. In response, the DOL devised the 80/120 rule, which states if you are a plan that is growing then you may go all the way up to 120 participants before the audit requirement applies. Essentially, you file as you filed in the prior year, *i.e.*, a small plan. For the audit requirement to then stop, it would require the plan to drop below 100 participants. Given the limited reporting requirements of these plans, it is unclear at this point how the 80/120 rule would apply to the 403(b) plans. Initial indications suggest it would be applied to these plans, but we are still awaiting final word on that assessment.

Q Can we just terminate the plan and not have to worry about these new requirements?

A This is not a viable option for most plan sponsors. The DOL requires the complete distribution of assets within a reasonable amount of time and, given this is already 2009, the requirements would still be in effect for this year.

Q Are any 403(b) plans exempt from these new requirements?

A Yes. In general, church plans and governmental plans continue to be exempt from the new reporting requirements.

Q Are there any plan provisions that would create an exemption from these new standards?

A Yes. Certain plans that only provide for salary reduction contributions, *i.e.*, employee contributions, would be exempt from the new standards provided they meet the “safe harbor” rules as provided by the DOL.

Q When are the Form 5500s and audits required to be completed? Are there any unusual reporting requirements given 2008 is the first reporting period?

A The Form 5500 tax return is due seven months after the plan’s year end and can be automatically extended another two and a half months. For example, the first plan period to have an audit requirement will most likely be December 31, 2009. The tax return and audit would initially be due on July 31, 2010, and could be automatically extended to October 15, 2010. While the audit requirement is for the 2009 plan year, the opening *Statement of Net Assets Available for Benefits* will have to be compiled (at a minimum). This will require plan sponsors to pull together the required information, *i.e.*, investments, contributions receivable, cash, administrative fees payable, as of December 31, 2008, for a calendar year-end plan.

Q Our 403(b) plan uses numerous service providers. Will the new regulations force us to consolidate these vendors?

A We anticipate these new regulations will generally result in the consolidation of service providers for these plans. An expected impact of these new regulations is to have third-party administrator (TPA) relationships similar to the 401(k) plans. To a certain extent, the DOL believes the more outside vendors are involved in a plan (particularly one with lax oversight), the more opportunity there is for fraudulent activity.

Q We have never been very involved in this 403(b) plan. We have essentially hired (a firm) to handle all of the administration for us and all we really do is send the TPA the contributions. Is this going to be a problem?

A Yes. The DOL has been critical of plan sponsors of 403(b) plans because of the lack of plan oversight. The agency believes this lack of oversight is the primary reason behind the extremely high violation rate mentioned above. Plan sponsors should work on establishing individuals internally and externally who have responsibility for the plan as well as establishing proper internal controls. Applicable control procedures would include proper segregation of duties for remittance of employee and employer contributions, review of distribution requests, interim review of plan investment activity and allocation reports and review of outside administrator internal control reports, just to name a few. Significant gaps in the internal control structure will be communicated to plan management at the end of the audit engagement in a formal letter.

Q We have heard the DOL delayed certain new provisions originally effective January 1, 2009. Is there any chance it will defer the audit and Form 5500 requirements as well?

A On December 11, 2008, the IRS did defer the need for a written plan document for public schools, colleges and universities and other tax-exempt organizations until December 31, 2009, under certain provisions. This announcement was made by the IRS at the American Institute of Certified Public Accountants (AICPA) Mid-Year Conference on employee benefit plans in Washington D.C. During a question-and-answer session, an attendee asked the DOL this exact question. The DOL indicated there is no consideration currently being given to deferring these new standards. The bottom line is this: plan sponsors need to have their new provisions in place in 2009 in case the DOL does not defer these new standards.

Obviously there is much to consider with these new regulations. Please contact your BKD advisor to assist you with these issues.

Q This is a lot of information on a topic for which we do not have much experience. Where should we start?

A Get the right people on your team. BKD audits hundreds of employee benefit plans. We can assist by examining your current plan setup, performing testing of processes and performing the plan audit, if required. Another important piece of this puzzle is making sure you have a strong relationship with your plan’s third-party administrator. BKD can help you assess the best options for your plan. ♦♦

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