Public Sector Retirement News & Views | Q2 2018

TAX CUTS AND JOBS ACT

What it Means for Retirement Savings Plans & Loans

While defined contribution (DC) plans experienced minimal changes resulting from The Tax Cuts and Jobs Act of 2017, one important change was authorized. The change pertains to plan loans, the new law allows for a longer payback period if certain conditions are met.

Employees are typically required to repay the full outstanding balance of a loan if they terminate employment or if the plan is terminated. If the employee is unable to repay the loan, the unpaid balance is treated as a distribution and is reported to the IRS on Form 1099-R. The employee can avoid the immediate income tax consequences by rolling over all or part of the loan's outstanding balance to an IRA or eligible retirement plan by the due date (including extensions) for filing the Federal income tax return for the year in which the loan is treated as a distribution. This rollover is reported on Form 5498. Under previous law, such loans were required to be repaid within 60 days.

We recommend that if your plan allows loans, you should check your plan document to determine whether repayment language needs to be updated.

An Opportunity for Contribution Increases?

When the new tax rates were implemented in payroll systems, many employees enjoyed an increase in their take-home pay. Most increases were small, so perhaps not extremely noticeable to employees. Employees could easily increase their retirement contributions by this small amount! Small changes can make a very big difference over time.

WASHINGTON UPDATE

The Tax Cuts and Jobs Act produced minimal changes to defined contribution (DC) plans (see Loans article above), yet many issues related to DC plans were under discussion. Issues such as Rothification, plan consolidation, elimination of the 10 percent excise tax penalty and others were dodged; however, these issues may be reintroduced at any time in future tax- or pension-related legislation. NFP will continue to monitor evolving issues and proposals and will keep you informed about how DC plans may be affected and any actions plan sponsors should be taking.

FEE EQUALIZATION AND FEE LEVELIZATION

Fees in defined contribution (DC) plans can be one of the most complicated things for a plan sponsor to understand. Historically, fees have not been fully and simply disclosed, but the industry is changing towards greater and more understandable disclosure.

Simply put, there are two basic types of fees: administrative and investment-related. The investment-related fees are deducted from earnings on participant accounts and will vary from one investment to the next. These fees are paid to the firms that are making decisions about how the various funds are invested in the market. Participants will pay different investment-related fees, as the fees are based on where the participant chooses to invest their assets.

Administrative fees are also deducted from participant accounts. If the plan has not implemented a fee equalization (also known as fee levelization), administrative fees will also vary from one investment to the next. Administrative fees are designed to pay for administrative-related activities associated with recordkeeping participant accounts. Such activities can include marketing, statements, education, processing contributions and withdrawals, issuing required tax forms and meetings with local representatives.

Fee equalization addresses the equity of the administrative fees being charged to participants. Unlike the duties associated with investment management, duties associated with administering participant accounts do not change depending on where a participant has directed his or her investments. Arguments can easily be made that administrative fees should be the same for all participants because they have the same recordkeeping requirements. Regardless of investment selection, account value, contribution level – the administrative duties are equal for all participants, so the administrative fees should also be equal.

NFP recommends to all our clients that a fee equalization structure be implemented in your plans, so participants are sharing equally in the cost of administering this important benefit.

UPDATE: FIFTH CIRCUIT VACATES THE FIDUCIARY RULE

On March 15, 2018, the U.S. Court of Appeals for the Fifth Circuit (the Court) nixed the Department of Labor's (DOL's) Fiduciary Rule (the Rule) in a 2-1 decision in U.S. Chamber of Commerce v. DOL, 5th Circ., No. 17-10238.

Background

As background, the Rule amended ERISA's definition of fiduciary by considering a larger subset of communications to be investment advice that renders the person providing that advice a fiduciary. Since the Rule was finalized in April 2016, several industry leaders have come out in opposition to it. Additionally, one of Pres. Trump's first actions in office was to issue a presidential memorandum directing the DOL to review the Rule and its impact on American investors. The president's directive led to a delay of the effective date of the Rule (to June 9, 2017) and a delay of the majority of the Best Interest Contract Exemption (BICE) provisions (to July 1, 2019).

U.S. Chamber of Commerce v. DOL

There have been various challenges to the Rule in federal courts across the country; however, the plaintiffs in U.S. Chamber of Commerce v. DOL were the first to file suit. Among other claims, their suit alleged that the Rule's amended definition of fiduciary was inconsistent with the definition that was intended under ERISA and that the DOL went beyond their authority in promulgating the rule.

The court essentially agreed with the plaintiffs (overturning the Federal District Court decision), holding that the DOL exceeded its regulatory authority by implementing the Rule. The majority specifically claimed that Congress would have written ERISA's definition of fiduciary differently had they intended to make a more expansive scope of financial practitioners fiduciaries (especially those advising with regard to IRAs).

As such, they found the DOL's new definition of fiduciary to be unreasonable and found the BICE to be the DOL's attempt at creating additional private rights of action where ERISA and Congress hadn't already done so. The court reversed the prior judgment of the district court and vacated the Fiduciary Rule "in toto" — meaning the entire rule, not just a portion, is vacated.

What does the ruling mean for plan sponsors and participants?

The court's ruling would vacate the rule for the whole nation. However, the ruling also represents a split in the circuits, as the U.S. Court of Appeals for the Tenth Circuit ruled in favor of the Rule earlier this week (in Mkt. Synergy Grp., Inc. v. U.S. Dep't of Labor). The fifth circuit's mandate is due by May 7, 2018, and their opinion will become final at that time unless an effective challenge is filed.

Furthermore, although the court vacated the Rule in its entirety, there are still procedural limitations that give time for additional action by the DOL. The DOL has the following choices. They could:

- Appeal the case to the Fifth Circuit for an en banc hearing (which would be in front of the full Fifth Circuit) and even appeal the case all the way to the U.S. Supreme Court.
- Do nothing and let the rule become vacated after the appropriate procedural stays have been exhausted.
- Attempt to amend the rule in a way that addresses the Fifth Circuit's concerns and salvages a portion of the Rule.

It's hard to know how they'll proceed. On one hand, the Trump administration seems opposed to the Rule as written (as evidenced by their attempts to review it and delay it). On the other hand, many in the industry have already begun to comply with the rule and accepts its standards. Only time will tell how the DOL chooses to proceed.

As always, NFP will continue to keep you abreast of any changes to the Rule.

NFP GOVERNMENTAL RETIREMENT PLAN EXPERTISE

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