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FYI® In-Depth
For Your Information®

US

Volume 41 | Issue 89 | November 6, 2018

2019 Planning for Governmental Retirement Plan Operations

The calendar provided in this *FYI In-Depth* will help sponsors of governmental retirement plans that are exempt from many ERISA requirements set up a schedule of activities to address as the year progresses so that you meet important deadlines for qualified public-sector plans. As you evaluate the various tasks, you can confirm suitable deadlines with your vendors for their completion. As you make your plans, there are a number of key issues for you to consider as we head into 2019.

Review of Plan Administration

In addition to verifying that routine tasks are monitored in accordance with plan terms and administrative policies — such as making required minimum distributions — administrators must be on the alert for some not-so-common tasks. Here are some key areas to watch:

Remind participants of any opportunity to name beneficiaries. Many plan administrators have had to sort out competing claims for death benefits because of unclear or missing beneficiary designations. These disputes can sometimes result in costly litigation. Most plans make a participant's spouse the default beneficiary. If the plan offers a choice, and a participant wants plan benefits diverted to someone else, such as children, parents or a favorite charity, a properly executed beneficiary designation is key. Make a point of reminding plan participants to update their beneficiary designations and let them know if they must use specific plan forms to make their designation.

> The IRS provided a **memo** to its employee plan examiners on the steps plan sponsors must take – including sponsors of governmental plans – to avoid IRS sanctions for failing to make required minimum distributions to missing participants. Specifically, the memo requires a plan sponsor to: (1) search plan and related plan information as well as public records for alternative contact information, (2) use a commercial locator service, credit reporting agency, or Internet search tool, and (3) send a letter by certified mail or make phone calls.

Identify lost participants with vested benefits. Returned plan notices, statements or distribution checks should be researched timely to identify lost participants. The sooner the search is started, the more likely you'll be able to locate a terminated participant whose address has changed. Funds covering any check that remains outstanding for longer than the plan's stale check period should be redeployed to the trust or, depending on the amount, rolled into an IRA. Adjustments may be needed to address any income tax that had been withheld.

The fact that fewer notices to participants are mandated for governmental retirement plans than for private-sector plans may lead governmental plans to be somewhat passive in maintaining ongoing communications with participants who have terminated with vested benefits. If your plan does not regularly reach out to these participants, we encourage you to begin sending them reminders of their entitlement to benefits and the processes for claiming them. Failure by participants to begin receiving benefits before attaining certain ages can result in a number of adverse outcomes, including tax penalties for affected participants and negative publicity for retirement systems that effectively allow participants to inadvertently forego receipt of benefits they have earned.

Update the "Special Tax Notice" for eligible rollover distributions. In September, the IRS issued Notice 2018-74 to update its Safe Harbor Explanations for eligible rollover distributions to take into account certain legislative changes and other recent guidance. (See our September 19, 2018 *For Your Information.*) The explanations, also known as the "Special Tax Notice Regarding Plan Payments" or the "Section 402(f) Notice," generally must be provided to a recipient of an eligible rollover distribution between 30 and 180 days before an eligible rollover distribution is issued. If you haven't done so already, make sure these notice updates are addressed in a timely manner and incorporated into distribution materials issued to recipients by the plan and its service providers.

Address foreign asset reporting obligations. In an effort to address tax evasion, money laundering, and terrorist financing concerns, compliance requirements mandate reporting of assets held by foreign financial institutions (including retirement plans) and benefit distributions to certain individuals. Plan fiduciaries will want to assess compliance with these requirements, particularly the Foreign Account Tax Compliance Act (FATCA), the Report of Foreign Bank and Financial Accounts (FBAR), and regulations issued by Treasury's Office of Foreign Assets Control (OFAC). Our June 12, 2014 *For Your Information* outlines these requirements; our April 4, 2017 *For Your Information* provides an update on filing timing.

Review and analyze insurance coverage. Insurance can be purchased to protect fiduciaries and the plan against liability or losses occurring due to a plan fiduciary's act or omission. Fiduciaries can be personally liable for losses incurred by a plan due to their breach; insurance can cover some of those losses.

It is important to analyze the policy's major defined terms to understand exactly what risks it covers. Furthermore, understanding when these policies are triggered is crucial to understanding whether the plan and its trustees and staff will be adequately protected. An annual review of these policies may illuminate the requirement to report certain events to the insurer within a specific time frame to collect on a claim.

> **Comment.** Many policies cover the penalties imposed by the IRS under a Voluntary Correction Program but require timely notification to the insurer.

Plan Amendments, Filings and Documentation

Do your plan's governing documents correctly describe the plan provisions as intended, and are any summaries provided to plan participants and administrative procedures in sync with the official documents? Now that IRS has limited its determination letter program, an annual self-check should be considered.

> **Key Point:** Many governmental employers find that adding specificity to their documents improves the clarity of plan terms and consistency of administration. This helps to eliminate the need for case-by-case determinations for unusual situations and helps to mitigate litigation risk.

Evaluate the need for plan amendments — and deadlines. IRS procedures call for executing discretionary amendments by the end of the plan year and provide extended amendment periods for modifications necessary to address changes in legal requirements. Governmental plans are also allowed an extended period for adoption through 90 days after the last day of the third regular legislative session beginning after the amendment's effective date in which the governing body with authority to amend the plan can consider the amendment under the laws and procedures applicable to the governing body's deliberations.

If you missed any deadlines for making required amendments, consider IRS' Voluntary Correction Program (VCP). IRS announces the VCP fees and associated rules each January in its annual Revenue Procedure for written determinations. Beginning in 2018, discounted VCP fees are no longer available to sponsors who voluntarily correct plan document failures within one year after the applicable deadline, which was the case for earlier years. Although VCP filings can be costly, the alternative of self-correction without filing is not permitted in this circumstance.

> **Changes in compensation definitions.** The Tax Cuts & Jobs Act changed the tax treatment of certain fringe benefits such as moving expenses for non-military personnel and bike commuting expenses for 2018. These changes may affect whether these items count as plan compensation for purposes of determining contributions and benefits. Also, changes may need to be made in data collection and payroll practices.
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> **Normal retirement age.** IRS has proposed regulations on normal retirement age (NRA) specific to governmental plans that would allow for an NRA based on years of service — both instead of, and in conjunction with, age. The proposed rules also set forth safe harbors on NRA that are available only to governmental plans. They address many of the concerns governmental plan sponsors expressed in response to the 2007 NRA regulations. While governmental employers should review their plan terms in light of the proposal, it is expected that most would be able to maintain their current NRA definitions under these rules. Details are provided in our February 16, 2016 *For Your Information.*
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> **Cash balance and other hybrid plans.** Although governmental plans are exempt from the Code sections amended by the Pension Protection Act of 2006 to address age discrimination for private plans, comparable changes made to ADEA may need to be considered. For example, a DROP account could be considered a form of cash balance account. The interest crediting rate under the plan may not be the only issue that requires attention. Many plans need to adjust other provisions, such as lookback periods, early and late retirement factors, and plan termination rules.

Assemble and maintain documentation of transactions with participants. Proper administration of plans as they are currently written is key — but don't toss old documents. Be sure to create and maintain records of participant data, such as proof of benefit distributions, benefit elections, and beneficiary designations, which may be priceless when participants who terminated from service decades ago question whether or not payment had been made. There's a reason ERISA includes document retention obligations for plans — being exempt from those requirements doesn't mean there isn't value in voluntarily adopting them.

Service Providers Need to Know

Have you provided your actuary, consultant, TPA, etc. with copies of current signed documents? Your service providers need up-to-date information about you and your plans to be able to spot issues and assure quality service. Make sure to keep them in the loop!

Communicating with Your Actuary

2019 offers an opportunity to discuss rational funding expectations. Proposed revisions to Actuarial Standards of Practice will discourage the use of amortization rules that defer elimination of a plan's unfunded liability to an excessive degree. If adopted as proposed, the revised standards will provide a strong incentive to revisit funding policies if such a review has not already been undertaken.

Consider mortality and other assumptions. Without a doubt, your plan population is living longer and the cost of defined benefit plans will generally increase over time as a result. At some point, these mortality improvements will be reflected in updated mortality tables used by your actuary to estimate plan costs. It may be worth considering whether a revision of annuitant mortality assumptions is now in order. Plan trustees may wish to address this matter in advance of the next regularly scheduled experience study; at minimum, it would be advisable to know the likely impact of adopting a modernized mortality assumption. New mortality tables developed specifically for public retirement systems will soon be released in final form by the Society of Actuaries, so the examination of this assumption will be particularly timely in 2019.

Plan trustees and their actuaries will also want to consider changes in other assumptions, which may counterbalance the impact of mortality improvements. In response to longer life expectancy and the longer period for making retirement savings stretch, many employees are planning to continue working beyond the plan's "normal" retirement date. Aligning plan retirement assumptions with this new paradigm can reduce plan liabilities, particularly for retiree medical plans and pension plans with suspension of benefits provisions and generous early retirement subsidies. On the other hand, it can also boost liabilities for a plan that provides generous actuarial increases to those electing late retirement.

Governmental plans face a fundamentally different set of choices for de-risking, but by making appropriate choices in plan design, funding policy and investment policy, a public-sector retirement system can greatly reduce volatility in funding requirements and GASB reporting outcomes.

Defined Contribution Plan Design Changes

If you share the concern that your employees may not have sufficient funds to last through retirement, the timing may be right to consider new provisions such as auto-enrollment or auto-escalation to boost participant savings rates. You may also consider adding annuities to your retirement plans now that the IRS has made it easier to do so. The IRS issued final regulations on qualifying longevity annuity contracts which, if properly structured, enable a participant to start payments at an advanced age — as late as 85 — and exclude the value of the annuity from required minimum distribution calculations. Our July 10, 2014 *For Your Information* explains the option.

And if your workforce includes a significant number of individuals struggling to pay off student loans, a new approach to defined contribution plan contributions that is gaining interest in the private sector would match student loan repayments with nonelective contributions to the plan for those participants who are losing out on matching contributions because they cannot afford to make deferrals. The idea has attracted a great deal of attention on the heels of the release of a private letter ruling — hopes are high that IRS will soon release guidance that will offer reliance more broadly. Our August 30, 2018 *For Your Information* explains how this works.

In Closing

Planning with trusted advisors to identify tasks and set compliance goals for the coming year is an important first step for assuring smooth operations during 2019. In addition to the key items noted above, plan sponsors may want to perform an annual “checkup” (i.e., a review of operational practices and fiduciary responsibilities) to address plan expenses, design considerations, and investments. Plan sponsors may elect to conduct their own self-audit or contract with an independent party. Regardless of who performs the audit, identifying problems and initiating corrections in advance of any official agency audit is the preferred course of action.

Calendar of Significant Governmental Retirement Plan Compliance Tasks[1]

Action Item	Due Date
January	
Form 1099-R to participants (or write letter for 30-day extension)	January 31, 2019
Form 945 to IRS (to report income withheld on distributions)	January 31, 2019
February	
Form 945 (alternative date if withholding deposits timely made)	February 11, 2019
Form 1099-R to IRS (if paper; or file Form 8809 for 30-day extension)	February 28, 2019
March	
Report U.S. source income of foreign persons: Form 1042-S to participants and IRS (or file Form 8809 for 30-day extension for 1042-S filing with IRS; write letter to request 30-day extension for providing 1042-S to participants); Form 1042 to IRS (or file Form 7004 for 6-month extension)	March 15, 2019
April	
Required minimum distributions for first time qualifying participants	April 1, 2019
Form 1099-R to IRS (if electronic; or file Form 8809 for 30-day extension)	April 1, 2019
Distribution of all excess 2018 deferrals (e.g., $18,500 plus $6,000 catch-up)	April 15, 2019
Form 990-T unrelated business income tax return (or Form 8868 to request filing extension). This tax is sometimes triggered if the plan earns income from certain plan investments (for example, limited partnership interests)	April 15, 2019
December	
Required minimum distributions	December 31, 2019
Last day to adopt discretionary plan amendments for 2018 (unless legislative session rule applies)	December 31, 2019

[1] Assumes calendar plan and sponsor tax year. Does not account for short plan years, or new plans. Weekend rule generally applies to filing deadlines and certain other acts under tax rules.

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