How to be a Hero to Your Retirement Plan Clients

By Charles M. Lax

Over the next 18 months, you have a chance to be a real hero to your retirement plan clients. No matter how actively you are involved with the administration, you have a chance to make recommendations that can enhance the retirement plans that your clients maintain.Approximately 10 years ago, the Internal Revenue Service implemented a new procedure which generally requires preapproved retirement plans (prototype and volume submitter plans) to be restated every six years. Plan document sponsors were required to update their plan documents and submit them to the Internal Revenue Service by April 2, 2012. Over the next two years, those plans were reviewed and, in most cases, the plan document sponsor was authorized to begin the restatement process as of May 1, 2014. That process will continue for two years through April 30, 2016.

Now, how do you become a hero? Many plan document sponsors will do little more than send their client a restated document, which merely incorporates all of the same provisions and features that have been used in the past. *Unfortunately, the world has changed!*

While that plan and those features may have fit the client's needs 10, 20 or even 30 years ago, they may not make sense today. That being said, now is the time for you and your client to look critically at the plan's features to see if there are any modifications and improvements that could be made. In many cases, you are the one best suited to help your client with this process.

Recently, some of my clients have said that their plan had become too expensive to operate and they have decided to "shut it down." In those instances, I have suggested there are ways in which they can ease administrative burdens, reduce administrative costs and even reduce costs or contributions for nonessential or nonkey employees.

In other instances, I have heard from clients approaching their own retirement date, who indicate they are in a position to "shelter" large portions of their income, as long as the costs remain reasonable for the administration of the plan and contributions for their staff of employees. This can be done through a variety of methods, either within the context of their existing plan or by adding a new, more appropriate plan.

Finally, there are a group of my clients whose businesses have changed dramatically since their retirement programs were implemented. In those cases, they are less concerned about personal tax shelter and instead want to provide their employees with a meaningful retirement benefit at a reasonable cost.

Here are a few suggestions that may work in one or more of the three situations I have just described:

1. Add a 401(k) Feature to a Profit Sharing Plan. If the client still does not sponsor a 401(k) plan, it is not too late. 401(k) plans provide the best “bang for the buck” to help plan participants accumulate meaningful retirement benefits.
2. Adopt a Solo-k Plan. If the client is self-employed and wants a low cost plan that provides a high level of shelter, a “Solo-k” plan can shelter up to 60% of their self employed earnings at a level of $50,000 and up to 40% of self employed earnings at a level of $100,000 with relatively small administrative costs.
3. Add a Safe Harbor Feature to a 401(k) Plan. For those clients who maintain a 401(k) plan and are having difficulty passing ADP testing (requiring the return of deferrals to the owners and other highly compensated employees), a safe harbor 401(k) plan should be considered. Generally, safe harbor plans require sponsors to commit either a minimum 3% fully vested employer contribution or an approximately equivalent matching contribution.

   In instances where the clients are hesitant to even make that commitment, a “wait and see safe harbor plan” may be preferable. This type of plan allows an employer to make the decision on adopting a safe harbor feature as late as the 11th month of the plan year.
4. Add Roth Features to a 401(k) Plan. Including a “Roth feature” in a 401(k) plan is not new. Many clients, however, were hesitant to include Roth features because of various uncertainties. Those uncertainties have now subsided. At a minimum, younger employees with lengthy horizons on retirement and older employees with estate plan considerations have all seen the great potential of savings with a Roth vehicle. In order to facilitate

this, adding Roth features where they have not been available, as well as allowing for Roth 401(k) rollovers and “in plan Roth conversions” will facilitate the use of Roth accounts for those employees.

5. Add a Cross-Tested Allocation Feature. For many years now, the Internal Revenue Service has allowed “cross-tested” allocation methodologies within discretionary contributions plans. Through the cross-testing feature, different levels of contributions can be targeted for different groups of plan participants. Typically, this has been used as a vehicle to leverage smaller contributions for staff employees into much larger contributions for the owners and other key employees. To the extent a client has not yet added this feature to a plan, it should be considered. Even those clients who have already used this approach should now be aware of the additional flexibility that is now available. This is done by placing every employee in their own allocation group and targeting different levels of contributions for specific employees.
6. Reduce Plan Expenses Borne by the Plan Sponsor. Historically, many of our plan clients have borne the administrative costs of maintaining their retirement plan. In recent years, however, a trend has developed whereby employers are passing along many of the administrative costs to plan participants. In some cases, it is limited to the costs directly attributable to the services that the employees utilize. This may mean charging a participant’s account with the cost of plan loans, qualified domestic relations orders, hardship distributions and other distributions. In other instances, administrative costs such as accounting, legal, investment and other fees are charged to the accounts of plan participants.
7. Use Forfeitures to Pay Plan Expenses. A further method by which plan administrative expenses can be reduced is for the plan to utilize forfeitures created by terminating employees to be used to pay plan expenses rather than increasing contributions or benefits for plan participants.
8. Increase “Cash Out” Limits. Approximately ten years ago, “cash out” limits were reduced. This is a feature that allows a plan to cause the distribution of small balances to plan participants, even if they are not requested. While a cash out limit as high as $5,000 could be adopted, many employers were hesitant because of various administrative responsibilities. Instead a $1,000 cash out limit was selected. Unfortunately, this lower cash out limit has led to the accumulation of small account balances in many plans. Obviously, there are costs and responsibilities by continuing to hold those small accounts. Recently, many of our clients have revisited the cash out limit and have increased it to $5,000, easing administrative burdens.

9. Determine Other “Pain Points.” In reviewing the plan’s operation with some clients, the best approach is to merely ask about “pain points.” One client adopted a plan provision many years ago which provided that a terminating participant with more than a $15,000 account balance could not receive their benefit until the earlier of their death or normal retirement date. Since that time, they have lived with many “unhappy former employees” who have gone to extraordinary ends to cause a distribution. While the client believed that this type of provision was in the best interest of their employees and former employees, eventually they recognized that it “just wasn’t worth it.” Instead they have now adopted a provision that indicates that any employee who terminates with more than a vested account balance of $15,000 must merely wait two years to receive their distribution. By doing this, they have protected employees against a knee jerk reaction of terminating employment “to buy a new boat, etc.,” while providing a reasonable distribution policy for other more responsible former employees.
10. Add a Cash Balance Pension Plan. In recent years, many of our clients have either replaced existing defined contribution plans or added to an existing defined contribution plan a type of defined benefit plan known as a cash balance pension plan. This is a hybrid plan that has features of both a profit sharing plan and a traditional defined benefit plan. Most importantly, it has provided them with a vehicle that will allow large contributions and accumulations for business owners and other key employees as they approach retirement at a reasonable cost. While demographics matter, in many cases these plans can be adopted with relatively small costs for non-essential employees. An additional feature of this type of plan is the fact that it provides far greater flexibility in the funding requirements than traditional defined benefit plans have in the past.

If this article strikes a chord with you and you would like to discuss it or have any further questions, please feel free to call upon any of the members of our Benefits Group: Chuck Lax, Mark Wise, and Bill Sigler at 248.354.4030.