THE EMPLOYEE BENEFIT
Forum
current issues in retirement benefit planning

qualified PLANS LLC

Designated Roth 401(k) Accounts

SITUATION: Several of our employees have asked us to add designated Roth accounts to our 401(k) plan. We want to remain competitive to attract and retain qualified employees but are unsure whether we should add this feature.

QUESTION: Do many other 401(k) plans offer designated Roth accounts?

ANSWER: According to the Plan Sponsor Council of America's (PSCA) *55th Annual Survey of Profit Sharing and 401(k) Plans*, an increasing percentage of 401(k) plans are offering their participants the option to make after-tax designated Roth contributions. In 2011 (the most recent data available), 43.4% of the 401(k) plans surveyed offered designated Roth accounts. That's an increase of almost five percentage points from 2010, when 38.7% offered this feature.

DISCUSSION: In addition to helping your company recruit and retain qualified employees, adding a designated Roth account option may increase plan contributions. By offering Roth contributions, you can provide all employees — including higher paid employees and owner-employees who may not be able to contribute to a Roth IRA due to the tax law's income restrictions — more flexibility in how they can save for retirement. Note: Your 401(k) plan must continue to offer traditional pretax contributions as well.

Offering Roth contributions may also encourage a greater number of younger and lower paid employees, who would pay little tax on their contributions now, to participate in your plan. Higher participation makes it easier for your plan to satisfy the annual nondiscrimination tests. Designated Roth account contributions are counted with other contributions when testing the plan.

For employees: Earnings on after-tax designated Roth contributions can grow tax free, and both contributions and earnings can be distributed tax free after five tax years have elapsed since the first designated Roth contribution and the participant is age 59½ or older. After five tax years, distributions made on account of the plan participant's death or disability are also tax free. In 2013, plan participants can contribute up to \$17,500 (\$23,000 if age 50 or older) to a designated Roth account versus \$5,500/\$6,500 to a Roth IRA.

CONSIDERATIONS: Adding a Roth 401(k) option is relatively simple, but be aware that some additional administration and expense will be involved.

IRS Stops Letter Forwarding

In the past, many retirement plan sponsors have relied on the IRS to help them reach former employees who still participate in their plans and plan beneficiaries for whom the sponsors no longer have a current address. But as of August 31, 2012, the IRS has stopped forwarding letters for plan sponsors and administrators. The IRS's reason: Since the letter-forwarding program began in 1994, numerous alternative missing person locator resources, such as Internet search tools, have become available to plan sponsors and administrators.

What options, besides the Internet, do you have to locate missing participants and beneficiaries? The Social Security Administration (SSA) offers a letter-forwarding program for locating persons who are due "a sizeable amount of money" (and in certain other circumstances). The SSA charges a $35 nonrefundable fee per forwarded letter. It cannot guarantee delivery. The U.S. Department of Labor also recommends using certified mail, checking the records of related plans, if available, checking with a designated plan beneficiary, and using a commercial locator service or credit reporting agency.

Using Your Match More Effectively

Are you looking for ways to get the most results from your employer matching contribution money? Recent research from the National Bureau of Economic Research (NBER) provides some ways you may be able to more effectively leverage matching contributions into increased employee contributions.

It's the Threshold, Not the Percentage

One NBER study[1] suggests that raising the threshold for employer matching contributions can do more to encourage employees to increase contributions than raising the match rate. For example, instead of a 50% match on the first 6% of compensation, you might match 25% and raise the threshold to the first 12% of compensation. Because many employees try to contribute enough to receive their employer's full matching contribution, you may be able to increase employee contributions at no extra cost to your company.

Cue Participants into Contributing More

A second NBER study[2] tested contribution "cues" that plan sponsors might use in their plan communications, such as "you could increase your contribution rate by 1% [3%, 10%, or 20%] and get more of the match money for which you're eligible." The study concluded that higher numerical cues (such as the 10% and 20% used in the study) tend to increase contributions, while lower ones can actually decrease contribution rates.

You may want to review your communication materials to make sure they aren't inadvertently encouraging low contribution rates and consider adding messages to encourage higher contributions to regular employee communications, such as statements.

[1] *Matching Contributions and Savings Outcomes: A Behavioral Economics Perspective*, Brigitte C. Madrian, National Bureau of Economic Research, July 2012

[2] *Small Cues Change Savings Choices*, James J. Choi, Emily Haisley, Jennifer Kurkoski, Cade Massey, National Bureau of Economic Research, February 2012

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A DOL Audit — Are You Ready?

The U.S. Department of Labor (DOL) plans to substantially increase the number of ERISA compliance audits it conducts each year. If your plan were selected for an audit, would you be ready? Below we answer questions you and other plan sponsors might have about preparing for a DOL audit.

How does the DOL select a retirement plan for an audit? Unlike the random audits conducted by the IRS, DOL audits are generally conducted for a reason. If you receive a notice from the DOL's Employee Benefits Security Administration (EBSA) that your plan has been selected for audit, the DOL is likely looking for something specific, although some audits are random. For example, the DOL may be acting on complaints from plan participants or in reference to something on your Form 5500.

What will we need to show the auditor? Generally, the EBSA notice will list documents it wants you to have available at the audit. This list may include:

- The plan document and amendments
- IRS Form 5500 for the period being audited
- The summary plan description
- Distribution forms provided to participants
- The fidelity bond for the plan
- A list of the plan's investments
- The plan's investment policy
- Minutes of meetings of the trustee or investment committee showing how investment decisions are made
- Information about the plan's policies with respect to the voting of proxies

If there's anything on the list that is unclear to you, call and ask for clarification.

What else should we do to prepare? You should review all the requested documents, gather supporting evidence, and organize plan records. This groundwork will prepare you to answer the EBSA's questions. Also, make the plan's legal advisor and independent auditors aware of the audit and have them review the requested documents before meeting with the DOL. You may want your advisor and auditor to attend the audit (or be available to answer questions).

What areas might the DOL target in an audit? Some of the things an audit may focus on are:

- Timeliness of deposits of participant deferrals
- Employee compensation and eligibility for participation
- Distributions
- Payment of plan-related expenses
- Funding policy
- Investment process
- Prohibited transactions
- Accuracy of financial data reported on Form 5500
- Bonding
- Reporting and disclosure (including the new participant fee disclosures)

What happens if the audit uncovers an apparent violation? The EBSA will issue a voluntary compliance request letter. The letter informs the employer of the results of the investigation, cites pension law provisions that the DOL considers to have been violated, and asks for correction of the violation(s) through full compliance. Depending on the violation, correction may include restoring losses of plan assets and lost investment earnings.

Are there steps we could take now to be ready for a possible audit? Yes, regularly review the plan documents the DOL might request, along with plan investments and your investment policy, to make sure they comply with pension law (ERISA) and the tax law. In addition, you may want to periodically conduct — or have a benefits professional conduct — self-audits.

RECENT DEVELOPMENTS
In Benefit Plans

2013 Cost-of-Living Adjustments. The IRS has released the annual cost-of-living adjustments for various retirement plan limitations. Most of the limitations have increased for 2013 — with the exceptions of catch-up contribution amounts and compensation determining key and highly compensated employees.

Also, the Social Security Administration announced a $3,600 increase in the Social Security taxable wage base effective January 1, 2013. This change affects plans that consider Social Security in determining benefits or contributions.

	2013	2012
Defined contribution plan dollar limit on annual additions	$51,000	$50,000
Defined benefit plan limit on annual benefits	$205,000	$200,000
Maximum compensation used to determine benefits or contributions	$255,000	$250,000
401(k), SARSEP, 403(b), and 457 plan deferrals/catch-up	$17,500/$5,500	$17,000/$5,500
SIMPLE deferrals/catch-up	$12,000/$2,500	$11,500/$2,500
Compensation defining highly compensated employee	$115,000	$115,000
Compensation defining key employee (officer)	$165,000	$165,000
Social Security taxable wage base	$113,700	$110,100

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