



FIDUCIARY PERSPECTIVE

For Plan Fiduciaries by Plan Fiduciaries

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Precept Advisory Group

BB&T

precepttps@preceptgroup.com

800-344-1430

130 Theory

Suite 200

Irvine, CA 92617

www.preceptadvisory.com

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Stocks dipped in the run-up to the presidential election and then rebounded. The economy chugged along and interest rates remained low.

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The rules governing plan sponsors and other fiduciaries are about to change. As an employer offering a qualified retirement plan, you need to fully understand what is expected of you going forward.

Q1 Plan Sponsor's Quarterly Calendar

To ease administration of your 401(k) plan, we have assembled a short guide to your responsibilities and reminders for the quarter.

The quarter ended with a strong post-election rally.

Fourth Quarter 2016 Market Recap

(For the quarter ended December 31, 2016.)

A trendless summer stock trading pattern was broken up by the volatility that accompanied the fall election cycle. That in turn was ended by a post-election market rally in major equity benchmarks. When the dust settled on New Year's Eve, major indexes had regained all they had lost in the volatility, and then some. The bond market stayed strong, and consumer confidence was high. And early indications suggested that auto sales were on pace for a near-record year.

Through 12/31/16*	Quarter	1-Year	3-Year Annualized	5-Year Annualized	Closing Value
S&P 500	3.25%	9.5%	6.6%	12.2%	2,238.83
Dow Jones Industrials	7.94%	13.4%	6.0%	10.1%	19,762.60
NASDAQ Composite	1.34%	7.5%	8.8%	15.6%	5,383.12

Source: DST Systems, Inc. The S&P 500, Dow Jones Industrials, and NASDAQ Composite are unmanaged indexes. It is not possible to invest directly in an index. Past performance is no guarantee of future results. Not responsible for any errors or omissions.

*Price only. Does not include dividends.

Economy Watch Final results on the third quarter were released as the fourth quarter drew to a close. Government figures suggested that the economy was the strongest since mid-2014, growing at an annual rate of 3.5%.

Fed News One year on from its first rate hike since the financial crisis, the Federal Reserve's market regulators moved to nudge rates a little higher in December. They boosted their short-term interest rate target range 25 basis points to 0.50%-0.75%.

Bond Market Update Bond yields remained low in comparison to historical norms, even as they rebounded slightly from the unprecedented lows hit in the wake of the Brexit vote last summer. The benchmark 10-year Treasury bond yield started the quarter at 1.63% and ended it at 2.55%.

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For those participants who are not currently making after-tax contributions, advisors may want to encourage them to do so, if their employer plan allows.

The IRS Clarifies Rules on Rollovers of Retirement Plan Monies

After years of ambiguity around what is and is not allowed regarding the disbursement of after-tax contributions to an employer-sponsored retirement plan, the IRS ruled in September of 2014 that plan participants can roll those dollars into a Roth IRA tax free.

IRS Notice 2014-54, Guidance on Allocation of After-Tax Amounts to Rollovers, "provides rules for allocating pretax and after-tax amounts among disbursements that are made to multiple destinations from a qualified plan."¹ Importantly, the Notice states that all disbursements from a retirement plan made at the same time will be treated as a single distribution even if they are sent to multiple new accounts. Prior to this ruling, the IRS treated distributions from a retirement plan that were rolled over to multiple new accounts as separate distributions, each requiring that a proportional share of pretax and after-tax monies be disbursed.²

A Simplified Process

Now individuals holding both pretax and after-tax amounts in their plan can transfer -- through direct, trustee-to-trustee rollovers -- the pretax portion of the distribution (including earnings on after-tax amounts) to a traditional IRA and the after-tax portion of the distribution to a Roth IRA. In the past, this could only be accomplished through indirect 60-day rollovers, not through simplified direct rollovers.²

More Clarification, Please

As with many IRS rulings, Notice 2014-54 raised many questions with taxpayers. In response, the IRS recently issued some answers to those commonly asked.

Q: If I have both pretax and after-tax monies in my retirement account, can I roll over just the after-tax monies to a Roth IRA, leaving all of the pretax monies intact?

A: No, the new rule does not change the requirement that each distribution from a plan -- including partial distributions -- must include a "proportional share" of the pretax and after-tax amounts.

Example: If your account balance is \$100,000 and consists of \$80,000 in pretax amounts and \$20,000 in after-tax amounts, and you request a distribution of \$50,000, your distribution would consist of \$40,000 of pretax amounts and \$10,000 of after-tax amounts.²

In order to roll over all of your after-tax contributions to a Roth IRA, you could take a full distribution (all pretax and after-tax amounts), roll over all the pretax amounts directly to a traditional IRA or another eligible retirement plan, and roll over all the after-tax amounts directly to a Roth IRA.

Q: Can I roll over my after-tax contributions to a Roth IRA and the earnings on my after-tax contributions to a traditional IRA?

Yes, since earnings on after-tax contributions are considered pretax monies, after-tax contributions can be rolled over to a Roth IRA while the earnings on those contributions can be directed to a separate traditional IRA and avoid being taxed until they are distributed.

Plan Sponsors: A New Opportunity

The new guidelines present an opportunity for plan sponsors to reach out to participants to determine which individuals have after-tax money in their plans and explain the new rules -- and the new opportunity -- to them. Further, for those participants who are not currently making after-tax contributions, advisors may want to encourage them to do so, if their employer plan allows.

With the current annual pretax contribution limit of \$18,000 -- or \$24,000 for individuals age 50 or older -- high-earning employees who are not making after-tax contributions are missing out on the chance to sock away significantly more (the annual total contribution cap on defined contribution plans is \$53,000 in 2015) while benefitting from tax-deferred investment growth.

¹The Internal Revenue Service, Notice 2014-54, Guidance on Allocation of After-Tax Amounts to Rollovers, September 18, 2014.

²The Internal Revenue Service, *Employee Plans News*, December 23, 2014.

Engaging Employees Through Targeted Plan Communications

Your workforce may include a number of employees who aren't taking full advantage of your retirement plan and are at risk of not having enough savings to retire comfortably. How can you engage employees and encourage them to use their retirement plan effectively? Tailoring employee communications and education can help. Below, are answers to questions you may have about targeted communications.

Why do targeted communications encourage greater engagement? Different groups of employees often have different retirement planning needs. When a retirement plan communication is tailored toward a specific group, that message is more relevant. For example, younger employees may be more interested in a message about the importance of getting an early start on saving and the power of compounding than older employees who are getting close to retirement age.

How should employees be segmented? It really depends on the demographics of your workforce. Grouping employees by life stages is a relatively common approach. But other criteria, such as income or educational level, also may be useful.

In addition to demographics, you may want to look at retirement plan participant behavior. For example, messages can be targeted toward employees who don't participate in the plan, employees who don't contribute enough to receive the full employer matching contribution, employees who don't increase their contributions over time, or employees who take frequent loans from the plan.

Should retirement planning messages be gender specific? Women have a longer average life expectancy than men do. They are also more likely to have stopped working at some point during their careers due to the demands of their families. Workshops, articles, and other communications that discuss issues like these may encourage female employees to make sure they're taking action to have sufficient income during retirement.

Should plan communications target specific cultures? If a workplace has a significant non-English-speaking population, providing bilingual plan communications and presentations that are also sensitive to specific cultural differences could help boost plan participation and contributions.

What strategies may be effective when communicating with younger employees? Younger employees need information on the importance of joining their retirement plan and contributing as much as possible. In this case, communications might focus on how the plan works and on the advantages of pretax contributions, tax-deferred compounding, starting early, and contributing regularly. In addition to tailoring the message, also consider how employees will receive the information. Younger employees may be interested in learning about financial issues through social media, for example.

Which topics will resonate with older employees? Participants who plan to retire in the next five years need information on transitioning from accumulating assets to spending those assets in retirement. Older workers generally are interested in information on shifting their account's asset allocation into investments that are more conservative.¹ Older employees also should understand their plan's distribution options and the need for a withdrawal strategy that helps guard against depleting savings too quickly. The impact inflation may have on their expenses and investments is another topic of interest.

Engaged employees who have received retirement planning information that is relevant to them are more likely to see the value of your retirement plan and to feel empowered to make the most of the important benefit you are providing.

¹Asset allocation does not assure a profit or protect against a loss.

A plan fiduciary must follow the plan documents (unless they're inconsistent with ERISA) and act solely in the interests of the plan participants and their beneficiaries and for the exclusive purpose of providing benefits to them.

Plan Fiduciary -- Roles and Responsibilities

Many activities involved in operating a qualified retirement plan may make the person or entity performing those activities a plan fiduciary. As a plan sponsor, it's important for you and other fiduciaries of your plan to fully understand your responsibilities and the consequences of not fulfilling them.

Who is a fiduciary? New regulations impacting retirement savers and the financial professionals who serve the retirement industry were introduced by the U.S. Department of Labor (DOL) in April 2016. The so-called "conflict of interest" rules are intended to require that all who provide retirement investment advice to employer-sponsored plans and IRAs abide by a "fiduciary" standard -- putting their clients' best interest before their own profits.

With limited exceptions, under ERISA, a fiduciary includes anyone who: exercises any discretionary authority or discretionary control over the management of the plan; exercises any authority or control with respect to management or disposition of the plan's assets; or has any discretionary authority or discretionary responsibility over the administration of the plan.

In addition to plan sponsors and/or plan administrators, under the DOL's final "conflict of interest" rule, "a person is a fiduciary if the person receives compensation for providing advice with the understanding it is based on the particular needs of the person being advised or that it is directed to a specific plan sponsor, plan participant, or IRA owner. Such decisions can include, but are not limited to, what assets to purchase or sell and whether to roll over from an employment-based plan to an IRA." In this capacity, a fiduciary could be a broker, registered investment adviser, or other type of adviser.

What are a fiduciary's duties? A plan fiduciary must follow the plan documents (unless they're inconsistent with ERISA) and act solely in the interests of the plan participants and their beneficiaries and for the exclusive purpose of providing benefits to them. In addition, a plan fiduciary must act with the care, skill, and diligence that a prudent person would exercise under similar circumstances. Fiduciaries must also make sure the plan's investments are diversified (unless it's clearly prudent not to do so under the circumstances) and ensure that plan expenses are reasonable.

Does the pension law prohibit any specific actions? Yes. ERISA prohibits certain types of transactions between a plan and specified related parties (called "parties in interest"). As employer/plan sponsor/fiduciary, you are considered a party in interest to the plan. Other parties in interest include employees of the plan, any other fiduciaries (such as the plan's administrator, officer, trustee, or custodian), the plan's counsel, plan service providers, a direct or indirect owner of 50% or more of the sponsoring company, and relatives (as defined under ERISA) of 50%-plus owners.

What transactions are prohibited? Examples of prohibited transactions between the plan and a party in interest include selling, exchanging, or leasing property; lending money or extending credit; and furnishing goods, services, or facilities. The law contains exceptions that protect the plan in conducting necessary transactions that would otherwise be prohibited and for many dealings with financial institutions that are essential for the plan's ongoing operations. For example, a plan can hire a service provider as long as the services are necessary to operate the plan and the contract or arrangement with the provider and the compensation paid for the services are reasonable. And plans may offer loans to participants as long as certain requirements are met.

Are there any other prohibitions? Fiduciaries also are prohibited from self-dealing. Various restrictions prevent a fiduciary from deriving personal gain from actions that involve the plan. Because of the complexity of the prohibited transaction rules, you should consult your plan's ERISA attorney for advice before engaging in transactions involving plan assets.

What happens if a plan sponsor breaches its fiduciary duty? Fiduciaries that breach their responsibilities may be personally liable to restore the plan to the condition it was in prior to the breach, including restoring any monetary losses and returning any profits made through the use of plan assets. A fiduciary also may be subject to excise taxes for violating the prohibited transaction rules. For more on the roles and responsibilities of plan fiduciaries, visit the [U.S. Department of Labor's website](https://www.dol.gov/eisapage.cfm).

Q1 Plan Sponsor's Quarterly Calendar

Consult your plan's counsel or tax advisor regarding these and other items that may apply to your plan.

JANUARY:

- Send payroll and employee census data to the plan's recordkeeper for plan-year-end compliance testing (calendar year plans).
- Audit fourth quarter payroll and plan deposit dates to ensure compliance with the Department of Labor's rules regarding timely deposit of participant contributions and loan repayments.
- Verify that employees who became eligible for the plan between October 1 and December 31 received and returned an enrollment form. Follow up for forms that were not returned.

FEBRUARY:

- Update the plan's ERISA fidelity bond coverage to reflect the plan's assets as of December 31 (calendar year plans). Remember that if the plan holds employer stock, bond coverage is higher than for non-stock plans.
- Issue a reminder memo or e-mail to all employees to encourage them to review and update, if necessary, their beneficiary designations for all benefit plans by which they are covered.
- Review and revise the roster of all plan fiduciaries and confirm each individual's responsibilities and duties to the plan in writing. Ensure that each fiduciary understands his or her obligations to the plan.

MARCH:

- Begin planning for the timely completion and submission of the plan's Form 5500 and, if required, a plan audit. (Calendar year plans) Consider, if appropriate, the Department of Labor's small plan audit waiver requirements.
- Review all outstanding participant plan loans to determine if there are any delinquent payments. Also, confirm that each loan's repayment period and the amount borrowed comply with legal limits.
- Check bulletin boards and display racks to make sure that posters and other plan materials are conspicuously posted and readily available to employees, and that information is complete and current.