InFRE® Retirement Plan Administrator Series

Fundamentals of Operations

Part 2

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Workshop Overview

All individuals with responsibilities for a retirement program, especially those with a fiduciary role, should have a basic understanding of the operation of defined benefit (DB) and defined contribution (DC) plans.

This workshop provides an overview of the operational requirements of retirement plans and is specifically designed for individuals involved with public sector retirement plans.

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Course Agenda

- Plan Administration
- Role of an Administrator
- Contracting Service Providers
- Administering Distributions
- Plan Amendments, Special Events, Post Retirement, and Designated Roth Accounts
- Nonqualified Deferred Compensation Plans
- Monitoring and Evaluation

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Today's Webinar Agenda

- Text Book Chapters
  3. Contracting Service Providers
  4. Administering Distributions

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Chapter 3

Contracting Service Providers

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Definition of Outsourcing

- Transferring work to contract providers
- Competitive process generally used to select contract providers
- In-house staff or consultants may be used in the procurement process
- Public sector commonly outsources all or most functions of supplemental defined contribution plans

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Determining What is Outsourced

- Administrative functions, products and services can all be outsourced
- Initial analysis should consider
  - What can be handled more efficiently with contract providers?
  - Are there cost benefits to outsourcing?
  - Can services or products be improved?

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Timing of Outsourcing

- Establishing a timeline is critical
- Timeline should include sufficient time for contingencies
- Target date should not be set in stone
  - Flexibility is needed to address unexpected
- Any blackout periods during a transition (DC plans) should follow best practice guidance

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Outsourcing Costs

- Cost is a critical factor in outsourcing decisions
- Cost-benefit analysis can help determine best approach for the plan and its participants
  - Can the outsourced services or products add value not currently experienced?
  - Can current costs be reduced without eliminating value?

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Procurement Process

- Public sector employer typically has a formal process that must be followed
- Request for Proposal (RFP) provides:
  - Consistent basis to gather information from potential contractors
  - Manageable method of comparison
  - Documentation of due diligence process

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Request for Information (RFI)

- Condensed version of an RFP
- Typically solicits general information about products or services
- Generally used:
  - For narrowing field of providers
  - When functions to be outsourced are minimal
  - To help develop more in-depth RFP document

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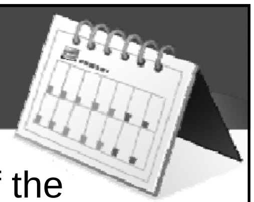
Objectives and Timeline



- Plan objectives are the foundation of the outsourcing project
- Input from various parties should be considered in objectives
- Industry trends should also be examined
- Tentative timetable for the RFP process should begin to be developed

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Identify Potential Bidders

- Resources include
  - Current contractors used by the employer
  - Trade publications
  - National organizations
  - Peer employers
- When list is developed, a solicitation letter should be sent to determine vendor interest

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The RFP Should Include…

- Detailed definition of all services/products being sought
- All relevant information about the plan and its participants
- Any enhancements or changes that are desired
- Format for submitting proposals, including special instructions for proposed cost

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Distribution and Bidder's Conference

- Before distributing RFP to vendor list, document should be edited for clarity and thoroughness
- RFP can be distributed electronically or posted to employer Web site with instructions for submission
- Vendor questions are often answered at a bidder's conference

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Proposal Evaluation

- Initial review determines if minimum and mandatory requirements have been met
- Evaluation criteria covers
  - Cost
  - Expertise and experience
  - Quality of service and/or product

- Cost generally considered after proposal questionnaire has been evaluated and scored

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Selecting Finalists

- Top two to four proposals may be identified as finalists based on RFP score
- Onsite visits of the finalists headquarters may be advisable at this point
- Reference checks are also conducted to further evaluate providers and identify any potential issues that need to be explored

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Best and Final Offers

- Finalists have one last opportunity to review their proposal and cost
- Employers may have certain leverage to negotiate better terms and conditions
- Cost should be evaluated in an apples-to-apples comparison
- Maintaining documentation is critical

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Decision to Award Contract

- Present findings from RFP process to decision makers
  - May include finalist presentations
- Contracting decision must be based on the best interest of participants / beneficiaries
- Contract negotiations begin immediately
- Performance guarantees identified

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Timetable and Contract

- Initial timeline adjusted based on needs of plan and selected provider
  - Detail needs to be added to identify each step
  - Responsible party and target date established
- Letter of agreement may be needed if contract not immediately executed
- Proposal and any best & final offers should be incorporated into agreement

3/3-20

Implementation

- On-going meetings between provider and employer staff are critical
- Frequent reports on status updates a necessity
- Performance standards incorporated into contract should begin to be monitored
- Performance guarantees should be based on both qualitative and quantitative measurements

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Exit Strategy

- Termination clause and exit strategy is essential in the contract negotiations
- Contract should address the termination process at
  - Contract end date
  - Termination for cause
  - Termination for convenience

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Contract Development

- Plan administrator will be intricately involved in contract development
- Communications with all involved parties is critical to ensure all understand terms
- Performance guarantees and penalties for failure to meet standards must be spelled out in detail
- Frequency and process for performance reviews should be identified

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Vendor Management

- Relationship between employer/provider
  - Communication
  - Trust
  - Competence
- Monitoring is one of the most important roles of the plan administrator
- Ensuring vendor provides accurate and timely information is critical to monitoring process

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Chapter 4

Administering Distributions

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Distributable Events

- Separation of service (i.e., normal or early retirement, termination, resignation)
- Death
- Disability
- Loans
- Hardship

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Rules Vary By Plan Type

- DB plans – generally provide lifetime benefit payments
- DC plans – generally offer several types of options ranging from lump sum amounts (full or partial) to lifetime annuities

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Defined Benefit Plans

- ***Qualified pre-retirement survivor annuity (QPSA)*** - benefits paid to the surviving spouse if a married participant with a vested benefit dies before benefit payments begin
- ***Qualified joint and survivor annuity (QJSA) -*** benefit that is paid out in series of equal, periodic payments over the participant's lifetime, with payments at death continuing to the surviving spouse

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Normal Retirement Age

- The age that a participant can receive a benefit from the DB plan without an actuarial reduction
- IRS regulation sets rules for earliest NRA
  - Below age 55 years is presumed unreasonable unless it is justified by facts and circumstances
  - Between 55 and 62 years is deemed reasonable if the employer makes a good faith determination
  - At least 62 years (or age 50 for plans covering qualified public safety employees) is presumed to comply

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Normal Retirement Distributions

From qualified plans and IRAs

- Periodic (annuity) payments
- Discretionary installment payments
- Irregular distributions
- A lump-sum distribution

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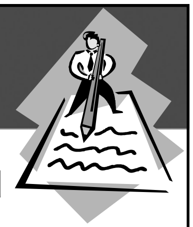
Notification of Rights



- Provided to participants between 30 and 90 days prior to distribution
- Notice must include:
  - Federal tax obligations
  - Rollover rights
- IRS provides model notice at www.irs.gov

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Periodic Payments

- Distributions that are paid at regular intervals over a specified period of time
- Amount of payment will be affected by
  - Age of annuitant
  - Number of lives covered by the benefit (single or joint life)
  - Survivor benefit guarantee period or benefit ratio
  - Mortality assumptions

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Types of Annuities

- Straight single-life annuity
- Life annuity with guaranteed payments
- Conventional joint and survivor annuity
- Joint and survivor (first death reduction) annuity
- Joint and survivor annuity with "pop-up" feature

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Non-Periodic Payments

- Withdrawals of irregular amounts at irregular times
  - Lump-sum and partial lump-sum distributions
  - Installment payments calculated to meet RMD requirements
- Lump sum distributions are the payment of the entire benefit within a single tax year

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Distributions Before NRA

- Distributions from DB plans may be prohibited until a designated early retirement age
- Distributions from a DC plan generally are more flexible and can occur at any age after termination of service
- Certain distributions prior to age 59½ may be subject to early withdrawal tax penalty

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Distributions at Termination

- Before early or normal retirement age, the following may occur
  - Forfeit benefits if employee has not vested in the benefit plan; employee contributions are always 100% vested
  - Receive lump sum benefits that may be eligible to be rolled into another tax favored account
  - Leave benefits in employer plan until early or normal retirement age is reached, or RMD rules apply

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Taxing Distributions

- Distributions are taxed as ordinary income after deducting participant's cost basis
- Cost basis includes
  - After tax contributions
  - Repayment of loans that were treated as deemed distributions
  - Any other contributions previously taxed to the participant

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Tax Withholding

- Mandatory 20% withholding normally applies to taxable distributions that are eligible to be rolled into another tax favored plan
- Exceptions include
  - RMDs, which are required to begin at age 70
  - Installments over 10 years or life annuities
  - Return of excess deferrals and contributions
  - Deemed distributions for defaulted plan loans
  - Taxable distributions of less than $200

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Early Distribution Tax Penalty

- A 10% penalty applies to most distributions before age 59½ from retirement plans and IRAs
- Exceptions to the penalty include:
  - **Distributions from eligible governmental 457(b) plans**
  - **Early distributions from qualified plans made to public safety employees over age 50**
  - **In case of participant's death, disability or QDRO**
  - **Distributions that are made in substantially equal payments over participant or joint lifetime**

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Required Minimum Distributions

- Apply to all qualified plans, 403(b) and 457(b) plans and IRAs
- RMD rules require payments to begin by the required begin date
  - For employer plans: later of April 1 following the year participant attains age 70½ or retires
  - For IRAs: April 1 following the year participant attains age 70½

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Application of RMD Rules

- Different types of accounts cannot be aggregated to meet RMD rules
- Failing to comply
  - Subject participant to substantial tax penalties
  - Jeopardize the plan's tax qualification status
- Due diligence must be taken to locate participants and beneficiaries eligible to receive a benefit to comply with RMD rules

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Application of RMD Rules

- Uniform lifetime table is used to calculate the RMD and is based on a joint life expectancy
- RMD rules also apply to beneficiary distributions
  - If beneficiary designated, based on life expectancy of beneficiary
  - If no beneficiary is designated, may be based on participant's life expectancy at time of death or five years

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Rollovers

- Assets are transferred from an employer plan to another eligible employer plan or traditional IRA
- Preserves tax-deferred status of assets
- Delays payment of income taxes
- Avoids early distribution penalties
- Special rules apply to rollovers into 457 plans http://www.irs.gov/pub/irs-tege/rollover_chart.pdf

3/4-23

Rollovers

- A direct rollover is:
- An indirect rollover is

Rollovers

- A direct rollover is:
  - Assets transferred directly from one eligible plan to another
  - Plan must permit direct rollovers out; not required to accept rollovers into the plan
- An indirect rollover is:
  - Distribution is made to participant who can then transfer to another tax-favored plan within 60 days
  - Subject to 20% tax withholding

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Eligible Rollover Distributions

- Taxable portion of distribution from retirement accounts
- Distributions not eligible for rollover:
  - Payments for more than 10 years or lifetime
  - RMDs
  - Hardship distributions and loans
  - Distributions to correct excess contributions
- Distributions to spouse and non-spouse beneficiaries may be eligible for rollover

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In-Service Distributions

- Financial hardship withdrawals
- Loans
- De minimis distributions of small, inactive account balances
- Distributions upon attainment of age 59½ for certain DC plans and age 62 for DB plans

3/4-28

Hardship Distributions 401(k), 403(b) Plans

- Plans are not required to make available
- Can only be released for immediate and heavy financial need
- If taken, elective deferrals and after-tax contributions are prohibited for six months
- IRS provides safe harbor guidelines for identifying financial need
- Subject to taxation and early distribution penalty, if applicable

3/4-31

Financial Emergency Withdrawals 457(b) Governmental Plans

- More restrictive than hardship distributions
- 457 IRC Regulations provide specific examples of situations that meet requirements
- Documentation must demonstrate the financial need
- Only the amount necessary to satisfy emergency need, plus applicable taxes, can be released

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Loans

- Plans are not required to allow loans
- To avoid taxation, loans must be limited to certain maximums and repaid within specified time frame
  - If not structured properly, loan becomes a deemed distribution.
- Deemed distribution subjects loan amount to immediate taxation and 10% early distribution penalty, if applicable

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De Minimis Distributions

- Qualified Plans
  - Involuntary cash-outs of small ($5,000 or less) accounts of terminated employees
  - Accounts greater than $1,000 must be rolled into an IRA or other retirement account

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De Minimis Distributions

- Section 457 Governmental Plans
  - Cash-outs of accounts under $5,000 with no new deferral activity for two years or more (termination not required)
  - Can be made as involuntary cash-out or at the employee direction
  - Subject to same rollover rules as above for accounts greater than $1,000

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Qualified Domestic Relations Order

- QDRO gives alternate payee a right to a portion of participant's benefit
- Plan administrator must determine if a domestic relations order is qualified.
- Procedures for determining qualification and how benefits will be paid must be written in plan.
- Alternate payee has same distribution options as participant.
- Spouse/former spouse may roll over distribution under a QDRO.
- Alternate payee is liable for taxes on distribution.

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Next Webinar

December

- Administration Issues: Plan Amendments & Special Events
- Nonqualified Deferred Compensation Plans
- Plan Monitoring and Evaluation

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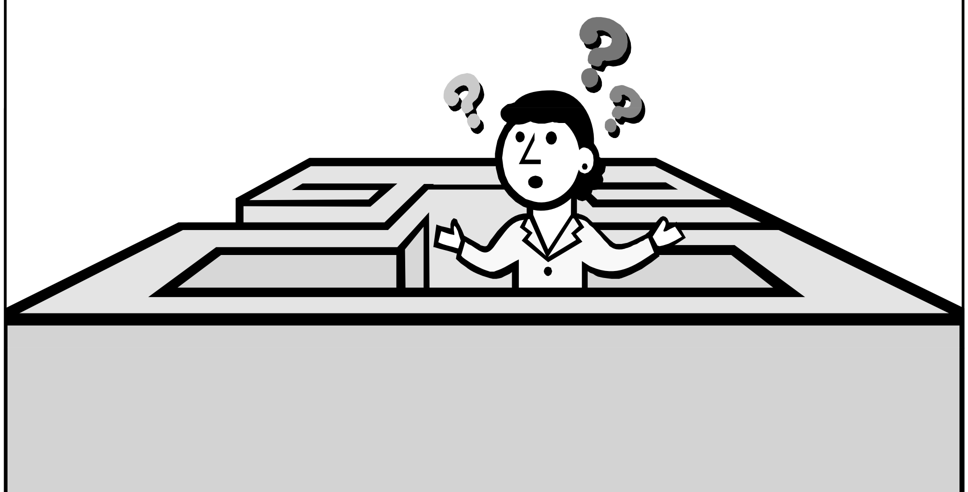
Any Questions?



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