



Fiduciary Best Practices: Process, Process, Process

I recently gave a presentation entitled "Retirement Plans: Insight on Fiduciary Responsibility" to the local chapter of the International Society of Employee Benefits Specialist (ISCEBS). Those who know me know that a technical presentation can "take all of the fun" out of the material – and it did. While not a "fun" topic, it was a meaty presentation on the fundamentals of fiduciary responsibilities. ERISA clearly defines fiduciary responsibilities in 404(c) and 404(a), which provide the back bone for fiduciary process and relief.

As a fiduciary, you should consider a prudent process and documentation your best defense. As long as you routinely follow a sound investment monitoring and review process of analyzing investments, and your decisions follow the results of this process (also documented in your Investment Policy Statement), it is the process that not only helps ensure sound investment options for participants, but also help limit adverse fiduciary liability consequences as a result of those actions.

If you or your fiduciaries would like the full presentation – or additional insight on fiduciary fitness, please ask.

401(k) Plan Loan Reminders

401(k) plans may allow participants to borrow from their accounts, but the plan document must specifically provide for such loans. Plan loans are allowed by law, but they are not required. In fact, many successful plans do not offer any participant loans. There are a few limitations or restrictions on the use for loans, including that plan loans must be reasonably available to all participants, but for the most part sponsors can be somewhat creative in how they design their loan policies. For instance, employers may restrict loans for specific reasons, limit the number of loans outstanding at one time, or require a minimum amount (typically \$1,000). If your 401(k) plan allows for participant loans, remember to strictly adhere to the terms of your plan document or loan policy.

Generally, unless the plan document is more restrictive, a participant is allowed to borrow up to 50% of their vested account balance to a maximum of \$50,000. If the participant had a plan loan in the last 12 month period, they will be limited to 50% of their vested account balance, or \$50,000, minus the outstanding loan balance in the preceding 12-month period, whichever is less.

Typically, loan payments are deducted from the participant's payroll checks. A loan must be paid back over five years unless the plan document allows for the repayments to be extended for the purchase of a home. If the participant is married, some plans require that the employee's spouse consent to the loan.

While interest rates vary by plan, we typically see the loan rate set as "prime rate" plus one or two percent. The current "prime rate" can be readily found in business publications. Many vendors place the responsibility directly on the plan sponsor to establish and reset this rate as warranted. If you are unsure, we encourage you to check with your vendor to see if you, as the plan sponsor, should be manually setting the participant loan rate and how to do so.

When processing a loan request, make sure the participant is clear when indicating which of their investments should be liquidated to fund the loan. In addition, make sure you understand if your vendor has a default investment to fund the loan, if not indicated on the loan paperwork. A loan cannot be rolled over to an IRA.

Remember, if the participant terminates employment and is unable to repay the loan, then it is considered defaulted and be deemed a distribution. In other words, the unpaid loan will result in income for that tax year.



That amount will then be subject to federal and state income taxes as well as a 10% early withdrawal penalty if the participant is younger than age 59 ½. Typically plans allow for a 30-90 day grace period after termination of employment requiring full repayment of a loan. Take time to make sure you understand your plan document's and your vendor's grace periods. Loan defaults, if not handled correctly, can be considered a prohibited transaction.

Compliance Reminder: 5500

Due Monday, August 2, 2010 (or file extension for October 15)

Communication Corner: Borrowing Against Your 401(k)

Available in English and Spanish!

This month's sample participant communication memo outlines a few important (and costly) drawbacks of borrowing money against your retirement savings. You may consider having this on-hand when a participant requests loan paperwork. I suggest adding the telephone and web-address of your vendor too.

Email Jill.Shea@shea-retirement.com for copy that you can print and distribute to employees.

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Empowering Best Outcomes for Plans, Sponsors and Participants

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