CHAPTER 7

Recovering Retirements and Making Sense of Employer-Provided Retirement Benefits in a Changing World

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Synopsis

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§ 7.01 INTRODUCTION

The COVID-19 pandemic, which most fully revealed itself in the U.S. in mid-March, brought organizations around the globe to a halt. As government orders were issued in the U.S. to close businesses and shelter in place, many employers who had not previously permitted telecommuting had to transition to remote working arrangements overnight. Many employers also had to deploy furloughs, layoffs and separations from employment to stay afloat, while others re-configured their businesses, requiring employees to provide new services or make new products. As a result, many members of the U.S. workforce faced, and continue to face, an uncertain future regarding their jobs. Yet, even before the pandemic, the employer-employee relationship and the meaning of a "workplace" was already evolving in the "gig" (or "sharing" or "on-demand") economy. Further, shifting worker models caused by advances in automation, and the impact of artificial intelligence on the future-of-work, was garnering attention and fostering debate regarding the availability of future jobs and the skills that would be required in order to obtain them. This confluence of events and technological advancements follow an already growing debate regarding the availability of a social safety net for U.S. workers, the security of retirements, and access to affordable health care.

As employers execute their Return-to-Work plans and re-open their businesses, they will have numerous compliance issues related to their employer-sponsored benefits programs to ensure that the changes they made as a result of the laws and guidance that were issued during the height of the pandemic are accurately reflected in plan operations and documentation. Plan sponsors will re-group and determine how their programs can be enhanced or re-designed in response to the near-term workforce changes. In addition, they must consider the long-term view in an ever-changed world and endeavor to make sense of the manner in which employer-sponsored benefits are provided to truly attract, motivate and retain talent. This article seeks to identify key considerations for the long-view with regard to defined contribution retirement plans and the related programs which will enable employees to more effectively save for their retirement years.

§ 7.02 RETIREMENT SAVINGS BENEFITS

It is often said that the demise of the employer-provided pension plan and the rise of participant-directed savings plans has compromised the retirement security of workers, as exemplified by the debates regarding participant savings rates, education regarding investments and fee transparency, and the U.S. Department of Labor's ("DOL's") fiduciary rule regarding investment advice. In early 2020, U.S. retirement plan sponsors were digesting the Setting Every Community Up for Retirement Enhancement Act of 2019 (the

"SECURE Act"),[1] which included important guidance on lifetime income options for retirement plans, as well as rules for allowing certain part-time employees to contribute to plans, which exemplified movement back toward a means of providing more access to employer-provided retirement savings programs and a predictable form of retirement income. By the end of March, 2020, however, efforts to secure retirements were further hindered by a pandemic, ensuing market volatility and need for disaster relief as set forth by the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act").[2]

Plan sponsors should not lose sight of the SECURE Act's long-view approach for retirement savings. In addition, plan sponsors should revisit their retirement plan features in light of the CARES Act and evaluate plan amendments that would best align with a long-view philosophy. Moreover, plan sponsors should consider the types of supplementary programs that can be offered to enhance a retirement savings program and enable participants to recover from recent economic losses.

This long-term planning analysis should include consideration of the following:

[1] Lifetime Income Distribution Options

Section 204 of the SECURE Act provides plan sponsors and fiduciaries with a safe harbor for the selection of an insurer for a guaranteed lifetime income distribution option for defined contribution plans under Section 401(a) of the Internal Revenue Code (the "Code"). The SECURE Act specifies measures that a plan fiduciary may take in selecting an insurer in order to fulfill its prudence requirements vis à vis assessing the insurer's ability to satisfy its obligations under the contract. While the new guidance is not definitive in that it neither establishes minimum requirements nor provides the exclusive means for satisfying requirements, it identifies prudent measures that include: engaging in an objective, thorough search for potential insurers, evaluating the financial capacity of the insurers and the costs of the contract, and concluding that at the time of the selection the insurer is financially capable of meeting its obligations and that the costs are reasonable. This diligence will require determining that the insurer: is licensed; at the time of selection (and for each of the preceding seven years) operated under a certificate of authority from its state Insurance Commissioner that was not revoked or suspended; has filed audited financial statements and undergoes requisite exams, maintains applicable reserves, and is not operating under an order of supervision, rehabilitation or liquidation. These new guidelines can serve to encourage inclusion of lifetime income investment options in plan investment line-ups and these options should be explored with retirement plan investment advisors.

Regardless of whether a lifetime income distribution option is available under the plan, Section 203 of the SECURE Act requires plan sponsors to include in at least one participant benefit statement issued during any 12-month period a lifetime income

[1] Setting Every Community Up for Retirement Enhancement Act of 2019, as Division O of the Further Consolidated Appropriations Act, 2020 (P.L. 116-94).

[2] Coronavirus Aid, Relief, and Economic Security (CARES) Act of 2020 (P.L 116-136).

disclosure. This requirement will apply for participant statements furnished more than one year after the last applicable guidance (including interim final regulations, model disclosures or assumptions) issued by the Department of Labor. This disclosure will be required regardless of whether the employer's plan includes a lifetime income or annuity distribution option.

The purpose of the disclosure will be to set forth the lifetime income stream equivalent of the participant's total account balance under the plan (i.e., to provide an estimate of what the participant could receive from the plan if their benefits were paid in the form of a qualified joint and survivor annuity (assuming a spouse of equal age to that of the participant) or single life annuity). Requirements for model disclosures will include (a) a statement that the lifetime income stream is only an illustration, (b) an explanation that actual payments pursuant to a lifetime income stream purchased with the account balance will depend on numerous factors, and (c) an explanation of the assumptions used in the illustration. When guidance is issued, plan sponsors and fiduciaries will need to determine if these disclosures necessitate additional communications to plan participants, especially if an annuity is not actually an option for a plan distribution.[3] Thus, it remains to be seen whether this disclosure obligation will become a factor which leads to the actual availability of lifetime income distribution options, which should be considered in any long-term plan design analysis.

[2] Portability of Lifetime Income Options

Section 109 of the SECURE Act also provides plan sponsors with the ability to adopt certain portability design features related to lifetime income investment options. In the event that a lifetime income investment ceases to be an option under a qualified defined contribution plan, a 403(b) plan or governmental 457(b) plan, the SECURE Act allows the plan to permit certain qualified distributions to another employer retirement plan or individual retirement account, or may allow distributions of a lifetime income investment in the form of a qualified plan distribution annuity contract, if made on or after the date that is 90 days before the date on which such lifetime income investment is no longer authorized to be held as an investment option under the plan. This portability window may be further modified or explained in regulations.

Prior to the SECURE Act, participants in defined contribution plans could request an in-service plan distribution only in limited circumstances if the plan so allowed—thereby preventing a participant from avoiding surrender charges or fees with regard to these options, or preserving the otherwise discontinued investment through a distribu-

[3] On August 18, 2020, the Department of Labor's Employee Benefits Security Administration announced that it would publish an interim final rule regarding the disclosures, which, once published, is subject to a 60 day comment period regarding the methodologies, requirements, and model language before publication of a final rule.

tion or rollover. This flexibility should not only allow participants invested in such de-selected options to avoid certain surrender charges and fees and maintain their lifetime income investment, but should also assist plan fiduciaries responsible for deciding whether to remove or replace lifetime income options.

[3] Part-time Employees

Effective for plan years beginning after December 31, 2020, Section 112 of the SECURE Act requires 401(k) plan sponsors to allow part-time employees who work at least 500 hours per year for at least three consecutive 12-month periods, and are at least 21 years old by the end of the last 12-month period, to participate in a 401(k) plan and make deferrals. For purposes of counting the 500 hours per year, hours of service during 12-month periods beginning before January 1, 2021 will not be taken into account. As a result, it will not be necessary to permit any employees to make deferrals under this provision before 2024. Under these rules, these part-time employees may be excluded from nondiscrimination, coverage and top-heavy testing, and plan sponsors are not required to provide employer non-elective or matching contributions to these part-time employees.

That being said, plan sponsors should take into consideration providing such employer contributions to these part-time employees, and whether the plan should be amended to allow participation for all part-time employees, even if they do not meet the three-consecutive year threshold or other eligibility requirements. This would allow access to retirement savings vehicles to a broader range of workers. It also remains to be seen whether future iterations of State-sponsored payroll IRA savings programs will have requirements for employers to enroll employees that are not otherwise eligible for their employer-sponsored retirement savings programs (as opposed to being based on whether the employer sponsors a plan at all), which may motivate employers to provide all part-time and other categories of common law employees with eligibility for their own plans.

[4] Employer Contributions

During the pandemic crisis, many plan sponsors amended their plans to suspend matching contributions and other employer contributions to the extent permitted by the parameters of their plan documents and applicable law (*i.e.*, within the confines of their pre-approved plans, or as feasible given any safe-harbor designs, especially if many participating employers adopted the plan). As organizations return-to-work, the resumption of the employer contribution features of the plans should be addressed so that plan amendments can be made and participant communications regarding the changes timely provided. For plan sponsors that did not previously provide an employer matching contribution or a discretionary contribution, consideration should be given to implementing these features, which will also serve to improve employee morale as they work to re-build the organization.

[5] Plan Distributions and Loans

Section 2202 of the CARES Act permits Section 401(k) plans, Section 403(b) plans, and governmental Section 457(b) plans to be amended to allow qualified individuals to request certain distributions. Qualified individuals are defined in IRS Notice 2020-50[4] to include those who are diagnosed with the SARS CoV-2 virus or the COVID-19 disease, whose spouse or tax dependent is diagnosed with COVID-19, or who experience adverse financial consequences due to certain COVID-19-related events including quarantine, furlough, or layoff, having hours reduced, or unable to work due to lack of child care. The distributions include:

(a) Coronavirus-related plan distributions up to $100,000 in the aggregate (determined on a controlled-group basis by the employer maintaining the plan, not including any individual retirement account distributions) on or after January 1, 2020 and before December 31, 2020 ("COVID-19 Distribution"). In addition, COVID-19 Distributions can be included in income ratably over a three- year period, and are not subject to (i) the additional 10 percent tax under Section 72(t) of the Internal Revenue Code (the "Code"), (ii) 20 percent mandatory withholding, or (iii) the Code Section 402(f) notice requirement. These distributions can be recontributed to an eligible retirement plan within 3 years from the date of the distribution in a direct rollover if the plan accepts eligible rollover contributions; and

(b) Plan loans up to the lesser of $100,000 or 100 percent of their vested account balance, during a 180-day period beginning on March 27, 2020 (the date of the CARES Act enactment) to no later than September 22, 2020. While the prohibited-transaction exemption for plan loans requires that plans cannot use more than 50 percent of the present value of a participant's vested accrued benefit to secure all outstanding plan loans made to the participant to ensure adequate security, later DOL guidance under the CARES Act provided that this rule would not be enforced for these loans (as had previously been announced with respect to prior Hurricane Katrina distributions).[5]

In addition, qualified individuals with an existing plan loan were permitted to suspend for one year any loan repayments due between March 27, 2020 and December 31, 2020. The loan would be appropriately adjusted to reflect the delay and any interest accruing

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[4] IRS Notice, 2020-50, 2020 IRB LEXIS 261.

[5] *See* EBSA Disaster Relief Notice 2020-01, https://www.dol.gov/agencies/ebsa/employers-and-advisers/plan-administration-and-compliance/disaster-relief/ebsa-disaster-relief-notice-2020-01 and IRS Notice 2020-50, note 4 above.

for such delay, and the period of delay would be disregarded in determining the 5-year period and the term of the loan. This was further complicated by IRS Notice 2020-23,[6] which allowed for the suspension of loan payments for any individual with a plan loan for payments due April 1, 2020 through July 15, 2020.

While these provisions were important to assist applicable plan participants navigate the immediate impact of the pandemic, it is important for plan sponsors to reflect on and analyze their plan participant demographics and their actions for future planning. It is important to determine the extent of the participant requests for COVID-19 distributions and loans, and the effects of the withdrawals on account balances, as well as whether there have been a series of similar distributions from past disasters as similar rules were enacted for past hurricanes and wildfires. This information can shape future plan design discussions. It will also be important to amend plans to ensure that the plan has the requisite rollover provisions allowing participants to repay CARES Act coronavirus-related distributions to the plan.

The analysis may also serve to inform whether plan amendments are need to limit the number of future loans that can be taken from the plan, as well as whether the plan will permit similar distributions for any future disasters that may arise within a certain period of time. Loan policies may also benefit from amended provisions to allow participants time to re-pay loans following a separation from service rather than being subject to an immediately due and payable provision. The cumulative effect of disaster withdrawals and loans, combined with market volatility, and suspension of employer contributions, can set participants' retirement savings back significantly, and plan sponsors can take action to alleviate those effects.

[6] Other Features

Plan sponsors should carefully consider avoiding plan amendments for optional plan features which will further dilute retirement savings, especially at a time when retirement savings have been adversely impacted by market volatility and disaster distributions. For example, Section 113 of the SECURE Act adds an in-service withdrawal option for "qualified birth or adoption distributions" from eligible retirement plans and IRAs described in Code Section 402(c)(8)(B) (other than a defined benefit plan). This withdrawal provision permits an employee to take qualified birth or adoption distributions up to a total amount of $5,000 from the defined contribution plans in the employer's controlled group. An employee who receives a qualified birth or adoption distribution may repay that distribution by making one or more contributions to a plan in which the employee participates, up to the amount of the distribution (subject to applicable plan provisions). While this may be a desired feature by participants, plan sponsors must weigh the pros and cons of features that may serve to

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[6] IRS Notice, 2020-23, 2020-18 I.R.B. 742.

further dilute vulnerable retirement savings. Employers can provide assistance through other programs to cover the cost of adoption and certain expenses related to the birth of a child. Plan participant demographics, savings rates and statistics regarding recent distributions and loans may serve to inform whether a particular plan should permit additional types of in-service distributions.

Plan sponsors should focus on retirement savings plan features that promote savings, such as automatic enrollment and auto escalation which can provide employees with the assistance they need to enroll and continue their participation in a retirement savings plan. As stated above, providing employer matching contributions and/or profit-sharing contributions, and limiting the number of plan loans that can be taken at one time, can provide an additional boost to employees' savings. When these features are combined with retirement and investment educational tools and/or access to advice, employees can become further engaged and understand better the importance of retirement savings and the effects of their plan distributions and loans on their future.

[7] Unrelated and Small Employers

The SECURE Act includes provisions that unrelated and/or smaller employers may find of interest in order to establish retirement savings programs for their employees. For example, commencing in 2021, Section 101 of the SECURE Act provides that unrelated employers may more easily participate in the same multiple employer plan (MEP) which may assist in reducing plan management costs. Also, under Section 104 of the SECURE Act, there is now a new tax credit of up to $500 per year (for up to three years) for small employers' (100 or fewer employees) start- up costs to establish new 401(k) plans and SIMPLE IRA plans that include automatic enrollment, or to convert to an automatic enrollment design. This is in addition to the other credit available for such small employer plan start-up costs (up to $5,000 for up to three years) to make it more affordable for small businesses to set up retirement plans.

[8] Supplementary Programs to Boost Retirement Savings

Plan sponsors should also consider additional programs that can enhance a retirement savings offering and enable participants to recover from recent economic losses. Efforts in that regard would make such programs more effective and assist participants in maximizing their retirement savings.

[a] Education Campaigns

Plan fiduciaries should consider enhancing their required plan communications with additional retirement education materials for the participants, which are often available from plan service providers. In some cases, education on even the most basic financial literacy concepts is needed. Programs can address the benefits of participating in a retirement savings plan, explain the features of the plan, educate on asset allocation and diversification, and explain the long-term impact of in-service distributions and loans. These programs are often delivered through on-demand webinars, website materials and tools, or in some cases via live consultants. Plan fiduciaries should develop an education program in accordance with the permissible parameters available under applicable regulations (e.g., Labor Regulation Section 2510.3-21),[7] which requires prudent selection and monitoring of the programs.

[b] Investment Advice

Plan fiduciaries may also consider offering plan participants access to investment advice, which extends beyond education. Investment advisors render participants advice for a fee, make investment recommendations, and may have discretion or control over the investments made in the participant's account (e.g., managed account models). Under an eligible investment advice arrangement under ERISA, a fiduciary adviser may receive a level-fee which does not vary depending on the investment options selected, or an objective, unbiased computer-model approach may be used. Plan fiduciaries should evaluate these programs under Labor Regulation Section 2550.408(g)-1[8] and applicable guidance. Plan fiduciaries must prudently select and monitor any investment advice program.

§ 7.03 FINANCIAL WELLNESS PROGRAMS

Employer-sponsored financial wellness programs are also gaining traction. Employers recognize that while employees need competitive compensation and benefits, it is becoming apparent that they also need the tools to understand how to manage their money and save for retirement, health care, and overall financial needs. In turn, employers that can assist their employees with competitive wages and benefits as well as mechanisms to understand their finances and reduce their financial stress will increase productivity in the workplace and their bottom line, reduce turnover and absenteeism, reduce health care costs and disability claims, increase retirement plan participation and actual retirements, and improve overall employee wellness.

There is wide latitude in designing a financial wellness program and some employers connect their program with their health and welfare offerings, making a business case that offering these programs directly ties to improving the overall health of the employees as they reduce their stress to manage their lives better. Access to financial planning and estate planning tools and services can provide education regarding the importance of having a will or financial planning concepts. For employers that wish to provide further assistance, they can provide access to financial planners and group legal services plans as voluntary benefits.

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[7] 29 C.F.R. Section 2510.3-21.

[8] 29 C.F.R. Section 2550.408(g)-1.

§ 7.04 UPSKILLING THE WORKFORCE AND EDUCATIONAL DEBT

Another reason why employees fail to save for retirement is student-loan debt. Many employees carry educational debt for years, even decades, and many others may find that they need to re-skill or upskill to continue in their careers, taking on more educational expenses. Employers can assist their employees by offering tax qualified educational assistance programs in accordance with applicable tax code rules,[9] consider offering taxable student loan repayments, and explore ways to make special contributions to 401k plans (mindful of nondiscrimination and coverage testing issues) to assist those employees with student loan debt (and related legislation should be monitored).

General student loan debt repayment programs, (e.g., $100 per month toward the principal balance of a student loan), are currently taxable and includible in wages under law. There have been legislative proposals to exclude from gross income the amounts paid by an employer under student loan repayment assistance programs, (*see e.g.,* the Student Loan Employment Benefits Act of 2016 (to exclude up to $5,000 per year from income) and the Student Loan Repayment Assistance Act of 2015 (to exclude up to $6,000 from income)). Section 2206 of the CARES Act allows employers to make tax-free payments toward their employees' student loans for a limited time (through December 31, 2020) by amending Section 127 of the Code, which already permitted educational-assistance programs for tuition, fees and books. The student loan payments by the employer must be under an educational-assistance program complying with the tax code requirements. There have also been legislative proposals to increase the amount of tax-free tuition assistance, which to date have not moved forward (*see e.g.,* the Upward Mobility Enhancement Act of 2017 (to exclude up to $11,500 of tuition assistance per calendar year)).

Under Code Section 132, working condition fringe benefits, which are property or services to an employee that an employee could otherwise have deducted from income, are not included in gross income. These may include educational costs that maintain or improve required skills or are a condition to maintain a particular job as defined under Code Section 162 and regulations thereunder. Expenses to meet minimum educational requirements of the individual's current business or as part of a program to qualify the individual for a new business would not qualify. Employers that can provide educational benefits that meet these tax code requirements may be able to provide such benefits on a tax-free basis.

Employers should carefully consider working condition fringe benefits as they introduce automation and artificial intelligence into the workplace. As it becomes increasingly more important for certain employees to re-skill and re-tool to work alongside machines, employer provision of the requisite education to perform these new jobs may qualify as a working condition fringe benefit.

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[9] IRC § 127.

Certainly, employees will find programs related to student loan repayment or educational assistance attractive and beneficial. Employers interested in offering these types of benefits should consider the available approaches under current law, communicate programs in a meaningful way, and monitor ongoing developments as new methods emerge in this trending area. These programs will alleviate overall financial stress and enable employees to save for retirement.

§ 7.05 CONCLUDING THOUGHTS

It will not be easy to recover from the economic impact of the COVID-19 pandemic, and the recovery will impact the future-of-work, including what it means to be an employee, which was already evolving. As the workplace changes, the role of the employer-provided system of benefits, on the retirement and health care front, will continue to be challenged and compromised. Employers that can find ways to maximize their retirement savings program offerings for the broadest possible scope of their workers will assist in the preservation of this system. Employers will also need to monitor legislation affecting employee benefits and applicable compliance requirements. The tasks as highlighted in this article should be analogously undertaken with respect to analyses of all employer-sponsored benefit programs. As legislation evolves, employers may conclude that it is more desirable to establish, or expand coverage under, an employer-sponsored plan. The future of this crucial system will require thoughtful, long-range planning.