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Benefits in Brief
SUMMER 2021

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How to Handle the SECURE Act's Part-Time Employee Mandate

The Setting Every Community Up for Retirement Enhancement (SECURE) Act that was signed into law in late 2019 includes several provisions designed to expand retirement plan coverage. One of these provisions requires employers to let certain part-time employees participate in the company's 401(k) plan starting in 2024.

Part-time employees' eligibility to participate in their employer's 401(k) will be based on the number of hours they worked during the three years preceding 2024. This means employers that offer 401(k) plans must begin tracking employees' hours worked starting this year to determine their eligibility to participate.

What the Act Requires

According to the legislation, part-time employees who work between 500 and 999 hours per year for the three consecutive years preceding 2024 must be allowed to make elective deferrals into their employer's 401(k) plan starting in 2024. The rule does not apply to 403(b) and 457(b) plans, which have different elective deferral requirements.

Note that the rule only applies to elective deferrals. The rules regarding employee eligibility to receive employer matching contributions are unchanged—plan sponsors can still impose a service requirement for receiving employer matches that excludes many part-time workers. Plans can also impose age requirements for 401(k) plan eligibility.

If an employer makes a non-vested contribution to a part-time employee's 401(k) account, a unique vesting standard will apply. Under this standard, the part-time employee must be credited with one year of service if he or she works at least 500 hours during a 12-month period.

To Track Part-Timers' Hours…or to Not?

This new rule could present challenges for plan sponsors when it comes to tracking the number of hours that part-time employees worked. While this function may be outsourced to a plan recordkeeper, there are still inherent data issues in this type of tracking. Failure to plan ahead could result in operational compliance errors.

There are alternatives to counting the number of hours part-time employees worked. The simplest is to allow all of your part-time employees to participate in the 401(k) plan, regardless of how many hours they work over the next three years. The cost to your business would likely be negligible because you wouldn't have to make matching contributions and there probably wouldn't be a rush of part-timers signing up, which would help keep average account balances and recordkeeping costs down.

You could also use equivalencies to credit the hours worked. In other words, part-time employees would be credited with a set number of hours for each period worked, such as 10 hours per day or 45 hours per week. The SECURE Act doesn't directly address equivalencies, but experts believe this is a viable strategy.

Plan Your Strategy Now

Regardless of which strategy you choose, you should plan now to comply with the SECURE Act's part-time employee mandate. Failure to do so could cost your business thousands of dollars if you have to reimburse eligible part-time employees for missed contributions and lost earnings.

What to Know About Choosing ESG Funds as QDIAs

On January 12, a final Department of Labor (DOL) rule went into effect that amends the regulations that govern how fiduciaries select retirement plan investments under ERISA. The DOL made some important changes to the Final Rule from the proposed rule that was first issued a year ago. In particular, the Final Rule eliminated specific references to environmental, social, and governance (ESG) or ESG-themed funds. The DOL acknowledged the fluid definition of ESG factors and concluded that "the lack of a precise or generally accepted definition of 'ESG,' either collectively or separately as 'E, S, and G,' made ESG terminology not appropriate as a regulatory standard."

Eliminating ESG Terminology

The Final Rule does retain the proposed rule's prohibition of the use of ESG funds as a qualified default investment alternatives (QDIA), but it does so without using ESG terminology. Instead, it refers to "pecuniary and non-pecuniary factors" when defining relevant fiduciary investment duties. Specifically, the rule states that a fund cannot be used as a QDIA "if its investment objectives or goals or principal investment strategies include, consider, or indicate the use of one or more non-pecuniary factors." The DOL believes that if a fund's objectives include non-pecuniary goals, the fund should not be the default investment alternative—even if the fund was selected based on objective risk-return criteria.

According to the DOL, this prohibition is intended to help ensure that participants' financial interests remain paramount by removing non-pecuniary considerations if their retirement savings are being automatically invested through a QDIA.

Determining the Use of Pecuniary Factors

The question, of course, is how plan sponsors can determine whether a fund's objectives, goals, or strategies use non-pecuniary factors. According to the DOL, you can determine this by reviewing a fund's prospectus.

But this determination may still be open to interpretation and subjectivity. If it references the fund's objectives or strategies to ESG goals or screening criteria—such as excluding investments in companies that produce or distribute alcohol or tobacco—you will have to determine whether goals or criteria are based on pecuniary or non-pecuniary factors.

The DOL has stated that if no non-pecuniary factors are reflected in a fund's objectives or principal strategies, it can be selected as a QDIA. This makes it critical to review a fund's objectives and principal strategies as communicated in the prospectus before deciding whether to select it as a QDIA.

Note: If the fund is a fund of funds, you'll need to review the prospectuses of all underlying funds as well.

Minimize Your Risk

At this early stage, it's still unclear whether ESG factors affect an investment's risk or return. The DOL has acknowledged that ESG factors could be considered pecuniary in certain circumstances; however, it has cautioned plan sponsors against assuming that ESG funds may be selected as QDIAs based on pecuniary factors.

In short, if you choose a fund whose objectives or strategies involve ESG goals or screening as your plan's QDIA, there is a risk that the fund is not a permissible QDIA under the DOL Final Rule. You have until April 30, 2022 to ensure your plan complies with the Final Rule's QDIA selection requirements.

What is a "Pecuniary Factor"?

The DOL's Final Rule amending the regulations for fiduciaries' retirement plan investment selection refers to "pecuniary and non-pecuniary factors" that plan sponsors should consider when selecting funds as a QDIA.

The rule defines a pecuniary factor as "a factor that a fiduciary prudently determines is expected to have material effect on the risk and/or return of an investment based on appropriate investment horizons consistent with the plan's investment objectives and the funding policy." Any factor that is not pecuniary would presumably be considered non-pecuniary.

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SECURE Act 2.0 Seeks to Boost Retirement Savings

Last October, the House of Representatives introduced legislation titled *Securing a Strong Retirement Act of 2020*. Commonly referred to as the SECURE Act 2.0, this legislation contains provisions designed to increase retirement saving opportunities, as well as ease plan administrative burdens for employers. Here are a few of the main provisions of the legislation:

Auto-enrollment in 401(k), 403(b), and SIMPLE plans would be mandatory.

Studies have shown that auto-enrollment increases plan participation rates because many employees do not opt out of the plan after they're automatically enrolled. Currently, 69 percent of retirement plans feature auto-enrollment.

All new plans except those offered by businesses with 10 or fewer employees and those in business fewer than three years would be required to automatically enroll new employees at a minimum salary deferral rate of 3 percent. Plans would also require a 1 percent auto-escalation of compensation per year up to a maximum of 10 percent.

The rules for taking required minimum distributions (RMDs) from retirement plans would be relaxed.

The age for taking RMDs from traditional IRAs would be raised from 72 to 75. Also, individuals with IRA and employer retirement plan (not counting defined benefit plans) balances of less than $100,000 wouldn't have to take RMDs.

The catch-up retirement plan contribution limit would be raised.

Once they reach age 60, 401(k) and 403(b) plan participants could contribute an additional $10,000 over and above the normal annual plan limits, with annual cost-of-living adjustments.

Employer de minimus financial incentives for plan participation would be allowed.

Currently, a matching contribution is the only financial incentive that employers can offer employees to participate in a retirement plan. The legislation would allow employers to offer other financial rewards such as gift cards to incent employees to participate.

The Saver's Credit would be amended.

The current tiered structure for this credit would be replaced with a flat 50 percent credit for the amount of IRA and salary deferral contributions made by eligible individuals, while the maximum credit would be increased from $1,000 to $1,500 per person.

A new employer tax credit would be added.

Businesses with fewer than 100 employees that establish a new retirement plan would receive a tax credit of up to $1,000 per employee to offset employer contributions. The credit would be phased out over five years.

On the plan administration side, the legislation would also relax certain retirement plan disclosure requirements, expand the IRS Employee Plans Compliance Resolution System (EPCRS), and change the requirements for recouping accidental overpayments made to retirees. Conforming plan amendments could be made by the end of 2022.

Are You Regularly Reviewing Plan Service Providers?

One of your most important responsibilities as a retirement plan sponsor is selecting competent service providers that charge reasonable fees.

But you must also periodically review and monitor your plan service providers' performance and fees.

Here are three areas to examine as you perform a plan service provider review:

1. Reporting Quality

The AICPA's *Audit and Accounting Guide* encourages employee benefit plan sponsors to critique service providers' monthly and annual reports for their timeliness, accuracy, and completeness.

Also analyze whether the reports contain the information needed to monitor plan activity and ensure regulatory compliance.

2. Processes, Procedures, and Controls

Your fiduciary duty requires you to analyze the quality and effectiveness of your service providers' processes, procedures, and controls that produce the plan's accounting information. This includes obtaining a SOC 1, Type II report from each service provider annually, if available.

This report will include a detailed description of the service provider's system and controls governing the plan's financial statements. You should also be aware of the complementary controls you need to have in place to allow service organizations to perform their duties.

3. Performance Relative to Agreed-Upon Standards

Are providers' services and cost consistent with what you agreed upon? For example, are the fees they're charging the same as the fees in your agreement?

Check whether plan participants have logged comments or complaints about service providers and whether complaints have been resolved.

The DOL requires plan sponsors to establish a formal review process at reasonable intervals throughout the year to decide whether to retain or replace service providers.

Ideally, this process should include onsite visits from your corporate finance or HR department.