Employee Benefit Trends
Why Now is a Good Time to Re-evaluate Plan Design

When is the last time you and your governance group took a fresh look at your employee benefit plan? If it was more than a year ago—or worse, if you can’t really remember—then now is a good time to re-evaluate your plan design in light of changes in your employee base and broad shifts in workforce dynamics.

Two trends to keep an especially close eye on are the growing number of younger employees entering the workforce and the shortening average employee tenures. These trends are forcing some plan sponsors to change key components of plan design so their plans better serve participants’ needs.

Work Tenures are Shortening
The days of employees working for one or two employers for their entire career are a thing of the past. According to the Bureau of Labor Statistics (BLS), the average employee tenure has fallen to just 4.2 years.

However, 401(k) vesting schedules to receive employer matches generally haven’t been adjusted to reflect these shorter average tenures. As a result, many short-tenured employees are missing out on receiving the full value of their employers’ 401(k) matches.

In fact, shorter tenures correlate to a potential decline in retirement readiness, according to a report recently released by the Employee Benefits Research Institute (EBRI). This is because shorter tenures may reduce the percentage of employees who are eligible for or contributing to a retirement plan.

Also, short-tenured employees who don’t receive the full employer match become disenchanted with retirement saving. This can discourage them from participating in or maxing out contributions to a retirement plan when they join a new employer.

Re-examine Vesting Schedules
One solution to this problem is to change your plan’s vesting schedule so that short-tenured employees receive more of their promised employer match when they leave your company.

For example, many employers use a six-year graded vesting schedule in which employees gradually work their way up to 100 percent vesting over a six-year period. Using this schedule, an employee who leaves after three years would only be vested at 40 percent. If the total amount of the employer match at departure is $1,000, the employee could only take $400.

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Some employers would like to offer their workers a retirement plan, but they’re discouraged by high administrative costs and cumbersome compliance requirements. This is especially true for small businesses that don’t have the financial and administrative resources of larger firms.

As a result, about 38 million private-sector U.S. employees don’t have a retirement plan through their employer, according to the Department of Labor (DOL).

To overcome these challenges, some small businesses have partnered to form multiple employer plans, or MEPs. This is an ERISA-protected, 401(k)-type retirement plan in which multiple small employers share a core plan administrator, lowering the costs and administrative duties for each participating employer.

Obstacles to Widespread MEP Adoption
Unfortunately, there’s a rule that has made it hard for many small businesses to offer MEPs to their employees. Employers participating in an MEP must have some kind of connection, like a common profession or membership in an industry trade association. MEPs are common in the medical profession for this reason.

Last fall, President Trump signed an executive order (EO)—the Executive Order on Strengthening Retirement Security in America—to loosen the requirements for businesses that want to participate in MEPs. More specifically, this EO would allow unrelated businesses to partner so they can offer an MEP to their workers.

In response, the DOL published a proposed rule that would make it easier for small employers in different industries to offer MEPs. This rule would allow groups of employers in a geographic region or a specific industry nationwide to offer MEPs and association retirement plans (ARPs).

Sole proprietors and their families would also be allowed to join these plans, “which give employers a simple and less-burdensome way to offer valuable retirement benefits to their employees,” stated Labor Secretary Alexander Acosta.

An important distinction with MEPs and ARPs is that employers are not viewed as sponsoring their own plans under ERISA. Instead, the plan is treated as a single employee benefit plan.

SECURE Act Would Allow Open MEPs
More recently, a retirement plan reform bill making its way through Congress—the SECURE Act—includes a similar provision that would allow “open MEPs.”

This provision would also make tax credits available to businesses that offer MEPs to their employees. And it would exempt employers from penalties if other MEP members violate fiduciary rules. This potential problem, referred to as the “one bad apple” liability risk, has previously kept some small businesses from participating in MEPs.

Not a Silver Bullet
While there is excitement in the retirement plan community about how these changes could enable more Americans to participate in a plan, there’s also some caution that MEPs aren’t a silver bullet.

For example, while a single Form 5500 filing and plan audit are performed at the MEP level, participating employers still retain some level of fiduciary liability. This includes selecting the MEP and monitoring the lead employer’s activities.

Also, it may be necessary to limit the fund menu and investment choices when designing the plan to streamline processes and keep costs affordable for small businesses.

We will keep you updated in future issues on the progress of the proposed DOL rule and pending legislation affecting MEPs.

Please contact our office if you have questions about multiple employer plans and association retirement plans.
Modernizing Your Benefits Plan
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With a three-year cliff vesting schedule, employees are zero percent vested until they have worked for an employer for three years, at which time they become 100 percent vested. Using this vesting schedule, the same employee would be able to take the entire $1,000 match when leaving the company.

Some companies are eliminating vesting schedules altogether and making employees 100 percent vested in employer matches immediately. According to a survey recently conducted by the Plan Sponsor Council of America, more than one-third of plan sponsors offer immediate vesting of employers’ 401(k) matching contributions.

Consider the Safe Harbor Option
Another option is to adopt a safe harbor 401(k) plan. With this plan design, you are required to contribute a minimum amount to participants’ accounts, and participants are fully vested in these matching contributions immediately.

Of course, there’s a cost to relaxing vesting schedules. When employees forfeit unvested funds, employers can use this money to help reduce plan costs or even increase matching contributions to employees who remain. Also, many businesses view vesting schedules as an employee retention tool, because some employees will remain with their employer long enough to be fully vested.

But some retirement experts question whether vesting schedules actually lower employee turnover. They point out that many employees (especially younger millennials) are going to jump ship to another job if it offers higher pay, more advancement opportunities, or a better work environment—even if this means forfeiting some of their employer match.

Re-examine Waiting Periods
Another aspect of plan design to re-examine is the length of the waiting period for new employees to become eligible to participate in your retirement plan. Traditionally, many sponsors required employees to wait for up to six months or one year until they were eligible.

Some employers are eliminating waiting periods in an effort to attract the best and brightest employees in a tight labor market. A key factor here is the stability of your workforce.

If you employ a large number of low-level, minimum-wage workers who don’t tend to stick around for very long—such as is common at many restaurants and retail stores—you might be better off retaining a waiting period for eligibility. Otherwise, you could end up with a lot of small-balance retirement accounts left behind by former employees.

Look at Auto-Enrollment and Auto-Escalation
Auto-enrollment and auto-escalation are two more aspects of plan design that you should re-examine. Participation levels in plans that automatically enroll new employees and then force them to opt out of they don’t want to participate are significantly higher than plans that don’t feature auto-enrollment.

You can take auto-enrollment a step further by adding auto-escalation to your plan design. With this feature, the percentage of pay that participants contribute to their retirement account is automatically increased each year—usually by one percentage point up to a maximum deferral rate of 10 percent. Research has indicated that employees are less likely to increase their deferral amounts if they’re auto-enrolled in a plan, so adding both auto-enrollment and auto-escalation to your plan design could be smart.

According to the Defined Contribution Institutional Investment Association (DCIIA), almost one-third of employees participating in plans with auto-escalation contribute more than 10 percent of pay to their retirement plan. However, just one-fifth of employees participating in plans without auto-escalation contribute this much.

Make Your Plan More Attractive
Plan to meet soon with your governance group and third-party administrator to re-evaluate your employee benefit plan to determine whether you should make changes to the plan design. Doing so could make your plan (and your business) more attractive to potential job candidates and more beneficial to existing employees.
Avoid Prohibited Transactions When Making Participant Deferrals

As an employee benefit plan sponsor, you must remit participants’ deferrals to the plan trust in a timely manner. This is defined by the Department of Labor (DOL) as being “the earliest date that is reasonably possible to segregate the contributions from the employer’s general assets, but no later than the 15th business day of the following month.”

Note, however, that the “earliest date” is specific to each plan sponsor. So if a sponsor typically remits contributions the same day of the deferral or the next day, this is considered “timely” for this plan.

If you fail to remit deferrals in a timely manner, you can make corrections using the IRS Employee Plans Compliance Resolution System (EPCRS). Keep in mind, however, that this failure can result not only in a correctable operational mistake, but it can also lead to a prohibited transaction that can’t be corrected under the EPCRS.

A prohibited transaction is a transaction between an employee benefit plan and a disqualified person, which the employer becomes once deferral deposits aren’t made in a timely manner. In this scenario, the plan sponsor must pay an excise tax of 15 percent of the amount of lost earnings on the deferrals that weren’t remitted on time.

Worse yet, if the operational mistake isn’t corrected, an additional excise tax of 100 percent of the amount may be assessed.

To correct late deferral deposits using EPCRS, you must determine which deposits were late and calculate any lost earnings. Next, you must deposit missed elective deferrals and lost earnings into the plan trust. You may also be required to review your deferral procedures and correct any deficiencies that led to the untimely deposits.

Note that if your plan has fewer than 100 participants, you can take advantage of a safe harbor rule. Here, you’ll have seven business days after receipt or withholding of participants’ deferrals to make remittances.