Employee Retirement and Deferred Compensation Plans

&

Fiduciary Responsibilities of Retirement Plan Administrators

Presented by:
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What is a Retirement Plan?

Contributions In

Money Invested

Distributions Out
How to Differentiate Between Retirement Plan Types

Is the Plan...
- Defined Contribution or
- Defined Benefit

And, is it...
- Qualified or
- Non-Qualified
Defined Contribution Plan

Plan defines contribution amount

Benefit amount determined by:
1. Contributions made
2. Investment earnings
Defined Benefit Plan

Contributions In

Money Invested

Distributions Out

Plan defines benefit

Contribution amount determined by:
1. Benefit amount
2. Duration of benefit (mortality)
3. Investment earnings
“Qualified” Plans Enjoy Special Tax Benefits

- Participants are not currently taxed on contributions
  - For-profit employers can deduct the contributions

- Investment earnings are tax-deferred

- Benefits taxed at distribution

- Benefit distributions can be rolled over to another qualified plan or IRA
Qualified Vs. Non-Qualified Plans

Qualified

Required to cover a broad group of employees

Non-Qualified

Must limit coverage to select group of management
Qualified VS. Non-Qualified Plans

Qualified

Subject to Many Rules & Regulations

Non-Qualified

Subject to Few Rules
Qualified VS. Non-Qualified Plans

**Qualified**

- Must be funded
  - In a trust
  - Out of reach of both the employer and the employer’s creditors

**Non-Qualified**

- Cannot be “formally” funded
  - Unsecured promise to pay
  - Asset segregation allowed (Rabbi Trust)
  - Subject to claims of employer’s creditors
Specific Types of Plans

- **Qualified**
  - Defined Benefit
  - Defined Contribution
    - Money Purchase
    - Profit Sharing
    - 401(k)
    - 403(b)

- **Non-Qualified**
  - 457(b)
  - 457(f)
Overview: Nonqualified Plans

• **457(b)**
  – Full and immediate vesting allowed
  – Not “income” taxable until withdrawn
  – Employer & Employee contributions permitted
  – Employer contributions may be discretionary
  – Contributions not coordinated with other plans (more later)

• **457(f)**
  – Taxed when vested “regardless” of distribution schedule
  – Employees could contribute (but why would they?)
  – Employer contributions may be discretionary
  – Contributions not coordinated with other plans (more later)
The Face Off: 457(b) VS. 457(f)

<table>
<thead>
<tr>
<th>Plan</th>
<th>Who Can Establish?</th>
<th>Maximum Eligibility Requirements</th>
</tr>
</thead>
</table>
| 457(b)| - Governmental Employers  
      |   - Public Utility Companies  
      |   - Elementary & Secondary Schools  
      |   - Public Universities & Colleges  
      |   - City, County & State Hospitals  
      |   - Certain Non-Governmental Tax-Exempt Employers | - Governmental - None  
      |                                                      | - Tax-Exempt – Select group of management or Highly Compensated Employees (HCEs)  
      |                                                      |   • excluding church related group |
| 457(f)| - Same as 457(b)  
      |   - Usually used by tax-exempt employers  
      |   - Rarely by governmental employers | - Select group of management or key HCEs |
### The Face Off: 457(b) VS. 457(f)

<table>
<thead>
<tr>
<th>Plan</th>
<th>Contribution Limits Employer</th>
<th>Contribution Limits Individual</th>
</tr>
</thead>
<tbody>
<tr>
<td>457(b)</td>
<td>▪ Employer contributions offset employee deferral limits</td>
<td>▪ Employer &amp; employee contributions combined cannot exceed the lessor of 100% of compensation or $17,500 in 2013 (prior to any potential catch-up options)</td>
</tr>
<tr>
<td>457(f)</td>
<td>▪ No limit</td>
<td>▪ No limit</td>
</tr>
</tbody>
</table>
## The Face Off: 457(b) VS. 457(f)

<table>
<thead>
<tr>
<th>Plan</th>
<th>Catch-Up Contributions Age 50+</th>
<th>Roth Contributions</th>
</tr>
</thead>
</table>
| 457(b) | - Governmental - $5,500  
  - **Tax-Exempt – Not Available**  
  - Both Govt & T/E  
    - Additional catch-up provision available within 3 years of NRA equal to lessor of:  
      - (1) 2x normal limit  
      - (2) Normal limit minus unused amounts from prior years | - Yes*              |
| 457(f) | - Not Applicable  | - No                |

* This is a design option the plan may or may not permit
# The Face Off: 457(b) VS. 457(f)

<table>
<thead>
<tr>
<th>Plan</th>
<th>When Must the Plan Be Established</th>
<th>Who Directs Investments</th>
</tr>
</thead>
<tbody>
<tr>
<td>457(b)</td>
<td>- The plan may be established anytime during the calendar year</td>
<td>- Participant</td>
</tr>
<tr>
<td>457(f)</td>
<td>- The plan may be established anytime during the calendar year</td>
<td>- Employer/Trustee directed</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Plan may permit participant direction</td>
</tr>
</tbody>
</table>
### The Face Off: 457(b) VS. 457(f)

<table>
<thead>
<tr>
<th>Plan</th>
<th>Are Loans Available</th>
<th>Vesting</th>
</tr>
</thead>
<tbody>
<tr>
<td>457(b)</td>
<td>- Governmental – Yes</td>
<td>- Employee salary deferrals</td>
</tr>
<tr>
<td></td>
<td>- Tax-Exempt – No</td>
<td>- full and immediate</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Employer contributions may vest over time according to plan terms</td>
</tr>
<tr>
<td>457(f)</td>
<td>- No</td>
<td>- “Any” vesting schedule</td>
</tr>
</tbody>
</table>
# The Face Off: 457(b) VS. 457(f)

<table>
<thead>
<tr>
<th>Plan</th>
<th>*Distributions: Up to 70 ½</th>
<th>*Distributions: After - 70 ½</th>
</tr>
</thead>
<tbody>
<tr>
<td>457(b)</td>
<td>- Severance from employment</td>
<td></td>
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<tr>
<td></td>
<td>- Death or Disability</td>
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<td></td>
<td>- Unforeseeable emergency**</td>
<td></td>
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<td></td>
<td>- Small inactive accounts**</td>
<td></td>
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<tr>
<td></td>
<td>- Plan termination</td>
<td></td>
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<td></td>
<td>- QDROs</td>
<td></td>
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<tr>
<td></td>
<td>▪ Required Minimum Distribution</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• by April 1st of calendar year in which participant becomes 70 ½</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• OR calendar year in which they retire if later</td>
<td></td>
</tr>
<tr>
<td>457(f)</td>
<td>▪ Distributions must be made on any monies that become vested.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>▪ No Required Minimum Distribution</td>
<td></td>
</tr>
</tbody>
</table>

* No tax penalty on any distribution  **If stated in the plan language
The Face Off: 457(b) VS. 457(f)

<table>
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<tr>
<th>Plan</th>
<th>How Are Distributions Taxed?</th>
<th>Eligible Rollovers</th>
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<tr>
<td>457(b)</td>
<td>▪ Traditional Account – as Ordinary Income</td>
<td>▪ Governmental Employees upon triggering event:</td>
</tr>
<tr>
<td></td>
<td>▪ Roth Account – Tax-Free</td>
<td>• Plan termination</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Death</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Separation from service</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Disability</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Over Age 59 ½</td>
</tr>
<tr>
<td></td>
<td></td>
<td>▪ <strong>Tax-Exempt - No</strong></td>
</tr>
<tr>
<td>457(f)</td>
<td>▪ Ordinary Income</td>
<td>▪ Not permitted</td>
</tr>
</tbody>
</table>

**Plan How Are Distributions Taxed?**

- **Traditional Account – as Ordinary Income**
- **Roth Account – Tax-Free**

**Eligible Rollovers**

- Governmental Employees upon triggering event:
  - Plan termination
  - Death
  - Separation from service
  - Disability
  - Over Age 59 ½
  - **Tax-Exempt - No**

- Not permitted
The Face Off: 457(b) VS. 457(f)

<table>
<thead>
<tr>
<th>Plan</th>
<th>Portability: Rollovers Among Plans</th>
<th>Advantages</th>
</tr>
</thead>
</table>
| 457(b) | ▪ Applies to Governmental 457s only:  
▪ Qualified Plan*  
▪ 403(b) Plan  
▪ 457(b) Governmental Plan  
▪ SEP/IRA  
▪ IRA(except a SIMPLE IRA)  
▪ Roth IRA** | ▪ If an employer offers a 403(b) or 401(k) plan in addition to a 457(b), an employee can defer the maximum to both plans  
▪ Employers may restrict participation to select key employees or management |
| 457(f) | ▪ Not Allowed | ▪ Employers may restrict participation to select key employees or management |

*Except to a SIMPLE 401(k)
**The pre-tax amount of a rollover is taxable in the year in which the rollover occurs.
# The Face Off: 457(b) VS. 457(f)

<table>
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<tr>
<th>Plan</th>
<th>Impact of Legislation</th>
<th>IRS Form 5500 Filing</th>
</tr>
</thead>
</table>
| 457(b) | - EGTRRA increased contribution limits and repealed coordination with qualified plan contributions  
                 - PPA made higher limits permanent  
                 - IRC 409(a) exempts 457(b) | - One-time, one page notice of plan adoption is filed with DOL to document “Top-Hat” exemption from ERISA |
| 457(f) | - Full IRC 409(a) compliance as of 1/1/09.  
                 - Serious consequences for non-compliance!! | - Same as above with exception for public institutions |
“457(f) plans are a mixed bag”

<table>
<thead>
<tr>
<th>The Good News</th>
<th>The Bad News</th>
</tr>
</thead>
<tbody>
<tr>
<td>...better than 457(b)</td>
<td>...worse than 457(b)</td>
</tr>
<tr>
<td>▪ No limit on amount of deferral</td>
<td>▪ Amounts are subject to taxation as soon as they are no longer subject to a “substantial risk of forfeiture”</td>
</tr>
<tr>
<td>▪ No restrictions on when amounts may be distributed</td>
<td></td>
</tr>
</tbody>
</table>

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“Substantial risk of forfeiture”

- Section 457 says it means that the right to compensation is conditioned on “future performance of substantial services”
  - More commonly referred to as “vesting”
  - Usually a very easy concept to apply:
    - The individual vests after performing certain years of service
      - (plan inception or actual contribution options)
    - The individual vests at given age
      - (Golden Handcuffs concept)
    - Vesting can also occurs upon death, disability, plan termination or change of control

**Vesting has nothing to do with the financial security of the plan**
Best Practices for ERISA Fiduciaries

Comment: Consider adopting ERISA Fiduciary Best Practices whether your plan is ERISA governed or exempt

- If ERISA governed, understand:
  - Who are the fiduciaries?
  - The primary duties of an ERISA fiduciary
  - The liabilities associated with being a Fiduciary
  - Structured plan governance
  - Current trends in the Non-Profit Sector
Best Practices for ERISA Fiduciaries

- **Who Are The Fiduciaries?**
  - Are they Named Fiduciaries or Functional Fiduciaries?
    - DOL set to promulgate a new definition of ERISA fiduciary status in late 2013/early 2014
  - Examples of Named and Functional Fiduciaries
    - Plan Sponsor
    - Plan Administrator (ERISA 3(16))
      - Not to be confused with the Plan’s TPA, Recordkeeper or Directed Trustee
    - Plan Advisor (ERISA 3(21))
    - Plan Investment Manager (ERISA 3(38))
    - Anyone who has discretionary authority over plan or plan assets
      - (e.g. Administrative/Investment Oversight Committee, Board of Directors/Trustees)
Best Practices for ERISA Fiduciaries

• Primary Duties of an ERISA Fiduciary
  • Act solely in participants’ best interests
  • Carry out duties prudently
  • Follow the plan documents
  • Pay only reasonable plan expenses
  • Diversify plan investments
Best Practices for ERISA Fiduciaries

• Understand The Liabilities Associated With Being A Fiduciary
  • Direct
  • Contractual
  • Functional
  • Associated (i.e. “Co-Fiduciary”)
  • Personal
Best Practices for ERISA Fiduciaries

• **Structured Plan Governance**
  
  • Create an formalized Retirement Plan Oversight Committee (RPOC)
  • Determine the initial need for and on-going role of outside advisors
  • Provide committee members with fiduciary training
  • Adopt a “detailed” Investment Policy Statement (IPS) and RPOC Charter
  • Determine preferred tools, formats and frequency for consistent Plan and investment oversight and review
  • Calendar regular RPOC meetings
  • Document, Document, Document
  • Communicate, Communicate, Communicate
Best Practices for ERISA Fiduciaries

- **Current Trends in the Non-Profit Sector**
  - Comprehensive benchmarking of fees, investment performance, participant utilization and projected retirement readiness
  - Auto-Features
  - ER contribution optimization
  - Scalable advice and guidance tools
  - QDIA scrutiny

- **PLATFORM CONSOLIDATION**
Thank you for your time

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