When Your Retirement Plan Document Becomes a Pain in the _____.

By Ary Rosenbaum, Esq.

As a retirement plan sponsor, you may forget that a retirement plan isn't just a tax deferred savings vehicle. A retirement plan. It is a legal entity supported by a legal document called a plan document. Issues with the plan document can create a host of compliance issues that threaten the tax exempt status of the Plan. The problem is that most times, plan sponsors aren't aware of any plan document issues. So this article should serve as a guide as to when a plan document can have issues that need to be corrected to avoid harm to the Plan.

The Plan hasn't been updated to current law.

My favorite law professor at law school, Bernie Corr, summed it up best as to one of the reasons why they keep on updating the bankruptcy code; it's a way to make bankruptcy lawyers some money. Changes in the Internal Revenue Code changes the rules on how retirement plans must operate, so the Internal Revenue Service (IRS) does throw ERISA attorneys a bone by requiring all qualified retirement plans to restate their plan document every 5-6 years and also making tack-on ancillary amendments every year or so to comply with current law. Plan documents must be up to date, so failing to restate or amend the Plan by the deadline can disqualify the entire Plan. The way to avoid being disqualified is for plan sponsors to have their Plan handled by a competent third party administration (TPA) firm and/or ERISA attorney. The IRS does allow Plan sponsors that have failed to timely amend their plans to correct it through their voluntary compliance program with a low penalty based on the number of participants in the Plan.

The Plan has been drafted by someone who doesn't know what they are doing.

There are a number of professionals that can draft a retirement plan. There are ERISA attorneys who can draft it, but most are too pricey. There are ERISA attorneys and paralegals at TPAs who can handle the task (I did it for 9 years). There are also accredited pension professionals (especially those certified by ASPPA) at TPA firms that have the background to do it. Then there are those that just shouldn't be drafting plan documents since they understand very little about the rules governing them. These types of incompetents may include ERISA attorneys, paralegals, and accredited pension professionals, or those with very limited retirement plan background. Unless you know exactly who drafted the plan document, you can't be so sure that they had the experience and knowledge to do it correctly. A retirement plan is a legal entity and a plan documents is a legal document with legal consequences. While there is nothing wrong with paying nothing for a plan document instead of an ERISA attorney who can charge $10,000 (I usually charge $2,000, all in), you may get what you paid for. Therefore, it might make sense to contract an ERISA attorney who should review the Plan within a couple of billable hours (don't spend more than $500).

The Plan is not being operated according to the terms of the Plan document.

Qualified retirement plans need a written plan document, as required by the Internal Revenue Code and ERISA. In addition, the Plan is required to be operated according to the terms of their plan document. While that seems simple, poor plan drafting and/or administration can make that difficult. When I used to work for a certain TPA, I used to joke that if you ever wanted to hide something from an administrator, they should have placed it in a plan document file. Many TPAs never read the plan documents they are supposed to administer, so if they enter the Plan information incorrectly on their computer system, they will always administer the Plan incorrectly. The problem is that with these incompetent TPAs, the error is usually only discovered during a conversion to a new TPA. As part of my Retirement Plan Tune-Up review for $750 (cheap plug), I go over the plan provisions and review it for the plan sponsor to make sure they understand their provisions and that the

Plan was administered according to their terms. Regardless of whether they should go with a Tune-Up, it would be advisable for the TPA and a plan sponsor to go over the terms of the plan document and make sure that they are both on the same page as to what the plan documents says and whether that is actually consistent with how it is being administered.

The plan document says one thing and the summary plan description says another thing.

ERISA requires all plan sponsors to hand out summary plan descriptions to plan participants. What is a summary plan description? An SPD is what it is, a summary description of the plan document. One of the major plan errors out there that has resulted in much litigation is when the SPD says one thing about participant's rights and benefits under the Plan, while the plan document says something else. Prior cases held that if there was a discrepancy between the two, the SPD would control because that was the document that the participant was provided and relied on. However, the tide has turned in the view, so the SPD is no longer controlling in any discrepancy with the Plan. The Supreme Court in Cigna Corp. v. Amara ruled that SPDs are not as legally binding as a plan document. "To make the language of a plan summary legally binding could well lead plan administrators to sacrifice simplicity and comprehensibility in order to describe plan terms in the language of lawyers," Justice Stephen Breyer wrote in the opinion for the court. "Consider the difference between a will and the summary of a will or between a property deed and its summary. … None of this is to say that plan administrators can avoid providing complete and accurate summaries of plan terms in the manner required by ERISA and its implementing regulations." In English, plan sponsors aren't off the hook for providing inaccurate SPDs, but the plan document is the legally binding document. So to avoid any confusion as to what should be the plan provisions and to avoid any potential litigation, plan documents and SPDs should be reviewed to confirm their consistency and they are not creating benefits, rights, and features that should not exist or conflict.

The plan document was not drafted to facilitate plan administration, but to impede it.

Years ago, as a TPA attorney, I reviewed an amendment that changed the matching provision in a 401(k)'s plan that was drafted by another ERISA attorney. It took me about three separate readings of the amendment to fully understand what the ERISA attorney was trying to do, but I wished him luck in trying to have it administered correctly. While plan documents should be drafted to meet the needs of the plan sponsor, it should also be drafted in a way that will help TPAs administer the plans correctly. This may be accomplished just by drafting provisions in language that is easy to understand as well as avoiding plan provisions that often lead to administrative errors. Such troublesome plan provisions could be a loan provision that allows for unlimited plan loans (more loans outstanding lead to repayment errors and omissions) or a stated match formula that may inadvertently require a matching contribution that an employer could no longer afford or a matching formula that matches on a different pay period than when the employer actually makes the contribution. A plan document should be reviewed for any ambiguous or difficult provisions to understand so that the administration of the plan can go smoother.

The plan document no longer fits the plan sponsor's needs.

Retirement plans should be tailored like suits; they should be tailored to fit the plan sponsor's needs. Of course over time, a company's needs do change either through expansion or contraction. So a plan document needs to be updated if the employer can make more employer contributions or less or if their discrimination testing is now starting to fail. It is advisable that the plan sponsor work with their TPA to see if the type of plan and its provisions still fits the needs of the plan sponsor. If not, then the TPA should work with the plan sponsor in either amending the current plan document or perhaps terminating it in favor of another qualified plan or no plan at all. Plan sponsors may discover that certain plan provisions were drafted for a mistaken reason or assumption many years ago. Plan documents that have provisions that no longer meet the plan sponsor's needs may require employer contributions that are inefficient or wasteful or aren't used to maximize the savings of highly compensated employees. Annual plan document reviews will have the effect of having the Plan become the right fit for the employer sponsoring it.

Whether it's a contract or will or legislation, any poorly drafted legal document has some unfortunate legal consequences. The same can be said of a retirement plan document which could expose the plan sponsor to a lot of grief and a lot of liability. A simple plan document review could go a long way to avoiding a lot of headaches for the plan sponsor.

The Rosenbaum Law Firm P.C.

The Rosenbaum Law Firm P.C.
734 Franklin Avenue, Suite 302
Garden City, New York 11530
(516) 594-1557

http://www.therosenbaumlawfirm.com
Follow us on Twitter @rosenbaumlaw