

Plan Document Foul-ups Can Cost You As A 401(k) Plan Sponsor

By Ary Rosenbaum, Esq.

Once joked that if you wanted to hide something from somebody when I worked at a third-party administrator (TPA), you should hide it in a plan document file. Seriously, as a plan sponsor, there are many things you don't know about your plan document and you really should because the plan documents could be a major culprit in what ails your 401(k) plan.

Plan document has to be written and updated every few years

A 401(k) plan like every qualified plan under the Internal Revenue Code needs to be written, it's not the oral Torah. The plan document is a legal document, so it needs to be signed contemporaneously and kept. Every few years (usually 6 years), the Internal Revenue Service (IRS) will require you to amend and restate your plan to a new plan document. This amendment and restatement aren't optional, it must be done when the IRS says it needs to be done. Currently, we are under the Cycle 3 restatement cycle and you plan must

be updated by July 31, 2022. Make sure it's updated for that deadline. The new plan document will contain all the necessary provisions to reflect the changes in the law and regulations that the IRS requires for that particular restatement. Also, the IRS may require a certain amendment to the plan to reflect a change in the law or regulations that they want all plan documents to incorporate besides the scheduled restatement. So while it seems that the restatement and amendment requests seem to be a great way to feed TPAs and ERISA at-

torneys, I assure you that these amendment and restatement directives aren't requests, they are mandated by the IRS. If you fail to amend and/or restate your plan at the time subscribed by the IRS, that might be a disqualifying event that may force you to lose previous tax deductions and for participants to have immediate taxable income of their retirement savings. The IRS does have a Voluntary Compliance Program to correct these plan document amendment and restatement failures that can be corrected with thousands of dollars paid to

The plan operation must conform to what the plan document says. Otherwise (as later discussed), you might have a compliance problem since you have to follow what the plan document says. The plan document is controlling, all the time except maybe in one instance. One huge problem is when the plan document and the Summary Plan Description (SPD) are inconsistent. The SPD, as you would think, is a summary of the plan document. Under ERISA, participants must receive an SPD when they are eligible to participate in the plan and

anytime that the SPD is restated as part of a plan document amendment and restatement. There is no ERISA requirement for participants to see the plan document. So if the SPD has better provisions for the participants, then the plan document may not be controlling in the eyes of the court. There have been cases where the SPD was determined to be controlling and the participants got the better provision that the plan document didn't have. A better provision could be eligibility, but it also could be required

employer contributions that you thought weren't part of your plan (because it isn't in the plan document). While you may win a case like that when participants sue over an SPD, why run that risk of the litigation in the first place? If you make sure that the plan document and SPD are consistent in their provisions, then you can avoid unnecessary litigation over your SPD.

Any change in the plan might need an amendment

When reviewing plan documents, I find



the IRS for the compliance program fee. So it's important that when your TPA or ERISA attorney tells you it's time to amend and/or restate, you should get it done.

The Plan Document is controlling, except there might be an SPD problem

To take off on that previous biblical reference, let's just say that the plan document is controlling as the Ten Commandments. Of course, since plan documents are written by attorneys, they are certainly not as clear and direct as the Ten Commandments.

many times that one of the trustees listed in the plan document or SPD either left the firm or died. There is no reason to have a dead trustee listed in the plan or the SPD. I have also seen provisions in the plan document that aren't consistent with the plan's operation. The address in the SPD of your business might be incorrect, as well as the telephone number. Yet so many plan sponsors don't know it or are just too lazy to make the

change to their plan. A plan document is like the United States Constitution is a living and breathing and controlling document. If changes need to be made like the Constitution, you need to make sure that an amendment to the plan document is done and that a Summary of Material Modifications (SMM) is done when there has been a material change in the plan through an amendment or when the information provided in the SPD has changed. Whatever updating needs to be done with the plan document and the SPD, make sure it's done.

The biggest plan document error I see

While occasionally I see plan sponsors that fail to timely amend and restate their plan document, there is one error that has been popping up lately in frequency. The error deals with the definition of compensation. The definition of compensation is a really important provision to get right because participants' ability to defer as well as any employer contributions are dependent on the defined form of compensation. The problem is when you have an exclusion from compensation in your mind and practice, but the plan document says something completely different. For example, it might be your intent that you don't want employees to get a contribution on overtime or other taxable forms of income such as a car allowance. If practice says you exclude that form of compensa-



tion, but your plan document says something completely different, you may owe corrective contributions for missed deferral opportunity and employer contributions on that form of compensation that you never intended to be available for such contributions in the first place. If you have any other variation of compensation you recognize than W-2, make sure that the plan document and your practice are the same.

Other plan provision errors

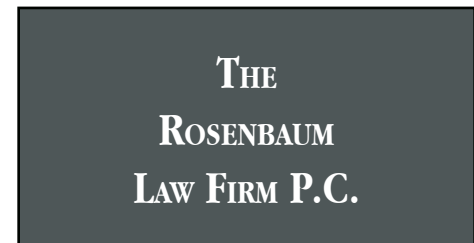
In addition to compensation, there are a whole host of plan document provisions that might be inconsistent with your practice that could certainly give you heartburn. Eligibility is one provision that if you get wrong could cost you more corrective contributions if the plan document is more liberal than your practice. That would be the same with vesting if you got that wrong, as well as an accrual of benefit for employer contributions (such as if your plan document doesn't require 1,000 hours of service for the contribution that you do in your practice). Regardless of the provision (some are less painful errors than others), you must get the plan document and plan practice on the same footing.

Get your plan document reviewed

When it comes to your health, you get a checkup. It may not be annual, but you get it done. Same with your teeth. It may go a few years between dental visits, but you

do it. The reason you do it is that a checkup goes a long way in detecting problems before they become major problems. You should treat your 401(k) plan document like your health. While it's not the same as your health, a checkup of your plan document goes a long way in detecting problems early and avoiding greater harm later. Any mistakes you can fix through self-correction or the IRS Voluntary Compliance Program are

more cost-effective than any mistakes that are detected on an IRS or Department of Labor (DOL) audit. Costs to fix problems through self-correction or voluntary compliance programs are a lot less than penalties you get from an IRS or DOL agent. I offer a Retirement Plan Tune-Up for \$750 where the plan document is reviewed. Whether you hire me or another retirement plan provider, have your plan document reviewed so that you can be sure that the provisions under the plan document and what you are doing in operation are the same.



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