Quick Takes:

Q1 2024 Review of Defined Contribution Regulation, Legislation, & Litigation

endeavor retirement

Regulatory Updates

Proposed Fiduciary Rule

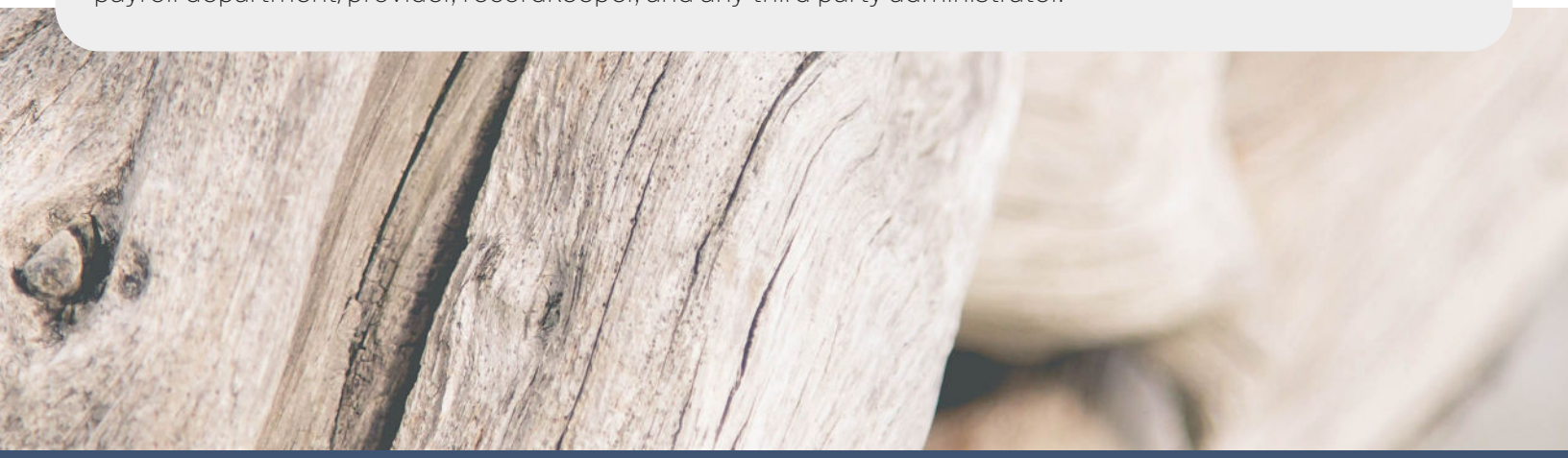
Last quarter's Quick Takes described the Department of Labor's (DOL's) publication of a proposed regulation that would broaden the scope of when a financial professional would be an "investment advice fiduciary." The proposal's most significant impacts – described in overly general terms – would be to extend fiduciary status to recommendations to take a rollover, take a distribution, and how to invest those rollover or distribution proceeds. Following the issuance of the proposal, the DOL held public hearings and received numerous public comments.

On March 8, 2024, following its consideration of the feedback, the DOL sent a final version of the rule to the Office of Management and Budget (OMB) for its review. Although many OMB reviews take up to 90 days, many expect the DOL to release the final rule within 30 to 60 days.

Long-term Part-time Employees: New Coverage Rules

Last quarter's Quick Takes also addressed the new long-term part-time (LTPT) employee coverage rules added by the SECURE Act of 2019 (SECURE 1.0) and modified by the SECURE 2.0 Act of 2022 (SECURE 2.0). While the IRS's LTPT proposed regulation remains in proposed status, plan sponsors may rely on it for vesting, testing, and other issues relating to their LTPT employees.

In the meantime, it is important for plan sponsors and service providers to ensure that the necessary coverage of LTPT employees commenced on January 1, 2024. This will involve a lookback to 2021, 2022, and 2023, and identifying those employees who were credited with at least 500 hours in each year and not otherwise eligible to participate in the plan. This process may require coordination with an employer's payroll department/provider, recordkeeper, and any third party administrator.



Legislative Updates

CITs in 403(b) Plans?

Over the last decade, 401(k) plans have experienced a significant increase in their access to collective investment trusts (CITs). Despite that trend, the law continued to prohibit 403(b) plans from offering CITs to their participants. SECURE 2.0 sought to remedy that inconsistency by making the Internal Revenue Code changes necessary to permit CITs in 403(b) plans. Those tax-related changes were only half of the battle; federal securities laws continued to prohibit CITs in 403(b) plans.

On March 7, 2024, the U.S. House of Representatives approved a law that would place 403(b) plans on the same level as 401(k) plans with respect to the use of CITs. The "Retirement Fairness for Charities and Education Institutions Act" would amend federal securities laws to allow many 403(b) plans (excluding 403(b) custodial accounts) to invest in CITs. Although the Act passed with bipartisan support, it will likely be considered by the Senate as a part of a larger legislative package. Until that time, 403(b) plans remain unable to utilize CITs.

SECURE 2.0 "Grab Bag" Guidance

SECURE 2.0 created many unanswered questions. On December 21, 2023, the IRS attempted to answer many of those questions through a "grab bag" of guidance in the form of Notice 2024-2.

The guidance addressed 12 SECURE 2.0 sections, including:

- ***De minimis* financial incentives** to encourage plan participation, which may be up to $250 (perhaps in the form of gift cards);
- **Tax treatment and eligibility of Roth employer contributions,** which will be reported on a Form 1099-R; exempt from Federal income tax, FICA, and FUTA withholding; and only available to a participant who is fully vested in the contribution at the time the contribution is allocated to the participant's account;
- **The application of the new automatic enrollment requirements** applicable to plans established on or after December 29, 2022, in various merger and spinoff contexts; and
- **Expanded and clarified requirements for the self-correction** of automatic enrollment failures.

Plan sponsors and committees may now discuss the practical availability of *de minimis* financial incentives. They also will have a clearer roadmap to self-correcting automatic enrollment failures, particularly those involving participants who have terminated employment before the correction is made.

SECURE 2.0 Emergency Savings Account Guidance

SECURE 2.0 creates the possibility of a "Pension-linked Emergency Savings Account" (PLESA). In general terms, it permits a plan sponsor to amend its plan to permit participant contributions of up to $2,500 (in total – not measured annually) into a PLESA. Through Notice 2024-22 and a set of FAQs, the IRS and DOL, respectively, issued interpretive guidance relating to the emergency savings account option provided by SECURE 2.0. The IRS guidance is limited in scope to the possibility that a participant may manipulate emergency savings account rules to receive excess matching contributions. The more expansive DOL guidance provides extensive practical guidance in a Q&A format.

From a practical perspective, access to PLESAs remains quite limited. At a time when many other provisions of SECURE 2.0 have eaten up service provider resources, recordkeepers, TPAs, payroll providers, and payroll departments have been exploring the allocation of resources, programming needs, and other costs associated with PLESAs. However, the IRS and DOL guidance provides sufficient ground for plan sponsors and committees to include PLESAs within their consideration of various emergency savings account options.

Litigation Updates

Plan Forfeitures: The Details Matter

The recent wave of lawsuits alleging fiduciary breaches in connection with the use of plan forfeitures continues. In 2023, fiduciaries of multiple household name plans (e.g., Qualcomm, Intuit, Clorox, and Thermo Fisher Scientific) faced lawsuits alleging that they breached their fiduciary responsibilities when using plan forfeitures to offset employer contributions. In *Barragan v. Honeywell, Int'l Inc.,* plaintiffs filed the latest such lawsuit against Honeywell fiduciaries on February 13, 2024.

This recent wave of lawsuits relates to plan documents that provide plan administrators a choice between various permissible uses of forfeitures, including (but not necessarily limited to) plan expenses or offsetting employer contributions. In February of 2023, the IRS published a proposed regulation that would generally require that plan administrators use forfeitures no later than 12 months after the close of the plan year in which the forfeitures arose. While the Honeywell and other cases remain pending, fiduciaries of other plans have a timely opportunity to consider the following four steps: (1) review their plan document language regarding the use of forfeitures; (2) monitor the use forfeitures to ensure they are used only in a permitted manner; (3) document the use of forfeitures; and (4) consider the timeline on which forfeitures are being used and whether it would be timely under the regulation proposed by the IRS in February of 2023.

Proprietary Fund Usage: Large Settlement

ERISA section 404(a) imposes upon fiduciaries a duty of loyalty, which requires that a fiduciary discharge its duties solely in the interests of the participants and beneficiaries. In October of 2023, the parties reached a settlement in *Kohari v. MetLife Group, Inc.*, a case in which plaintiffs had alleged that the defendant fiduciaries had breached those responsibilities when they "stocked the Plan's investment menu with their own proprietary index funds." The last decade of retirement plan fee litigation has brought heightened awareness around the use of a plan fiduciary or service provider's proprietary funds within a plan's investment lineup. Plan fiduciaries may wish to review the plan's lineup for the inclusion of any proprietary funds and to consider whether their presence would be consistent with ERISA's duty of loyalty.

Excessive Recordkeeper Fee Allegations

ERISA section 404 also imparts a duty of prudence upon plan fiduciaries. The United States Supreme Court has confirmed that this duty is ongoing, including a duty to monitor and to incur only costs that are reasonable. In late 2023, plaintiffs filed an excessive 401(k) fee lawsuit in ***Ruebel v. Tyson Foods.*** The lawsuit is similar to the scores of lawsuits filed in recent years. For example, it includes the allegation that the fiduciary defendants caused the participants to pay "over a 75% premium per-participant" for recordkeeping and administrative fees.

Although this suit is merely at the allegation stage, it is noteworthy because it reflects that plaintiff attorneys have adjusted their pleading approaches in response to some courts' recent dismissal of similar lawsuits. The complaint asserts that the fees were too high because of the "fungibility and commoditization" of the associated services. Plan fiduciaries may be inspired to benchmark their recordkeeping and administrative services – not necessarily with an eye toward making a change, but in an effort to distinguish the level of services and to memorialize a step consistent with their duty of prudence.