IVINS, PHILLIPS & BARKER
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Employee Benefits Update

March 2016

HIGHLIGHTS

Terminating the Employer Stock Fund: RJR Court Outlines Template for Prudent Process

Fiduciaries seeking to terminate the employer stock fund need a prudent process to support the decision. The district court in the lengthy *Tatum v. RJR Pension Inv. Comm.* litigation has endorsed at least one approach as the template for a prudent process. The template is similar to the one developed by Ivins, Phillips & Barker. See, e.g., Barker and O'Brien "Hold It or Fold It: Keeping or Closing the Employer Stock Fund".

(Ivins did not advise RJR or the RJR Pension Investment Committee in this litigation or with respect to the plan or fund at issue.)

The 4th Circuit last year held that the fiduciary imprudently terminated the Nabisco stock fund without a prudent process. It directed the district court to award damages measured as the difference between what the breaching fiduciary did and what a prudent fiduciary "would have" done. The district court held damages were zero. It accepted defendants' analysis that a hypothetical prudent fiduciary "would have" decided to liquidate the Nabisco stock fund, because defendants were able to establish that this single-stock fund was the plan's most volatile. And the district court further accepted that a hypothetical prudent fiduciary "would have" sold the stock—which defendants established traded in an efficient market—at the market price, as did the actual fiduciary. *See* 2016 WL 660902 at *26 (M.D.N.C.).

In This Issue

For an analysis of a substantially similar process, and why this process should be prudent according to the capital market theories underlying ERISA's duty of prudent investing, see Barker and O'Brien "Hold It or Fold It: Keeping or Closing the Employer Stock Fund". As noted in that publication, a similar process—also relying on the efficient market hypothesis—is available to support the fiduciary's decision to keep the employer stock fund open.

Fidelity Challenged for Keeping 'Float' Income in 401(k) Plans

The Department of Labor (DOL) has filed an amicus brief in the appeal of *Kelley v. Fidelity Mgmt Trust Co.*, opposing Fidelity's practice of keeping so-called 'float' income earned from its 401(k) plan clients. In a 401(k) plan, assets pending disbursement typically are moved temporarily to overnight accounts invested in short-term investment funds. The undisclosed income generated by these funds until the check is presented for payment – known colloquially as 'float' income – was retained by Fidelity as compensation for services rendered.

The district court in *Kelley* dismissed the claims against Fidelity, citing *Tussey v ABB* for the proposition that float is not a plan asset because the disbursement account is not owned by the plan. *See* 746 F.2d 327, 339 (8th Cir. 2014), *cert. denied,* 135 S.Ct. 477 (2014). The DOL, however, says that such focus is misplaced. The central issue is not whether the float is a plan asset, argues the DOL, but whether Fidelity unilaterally used its fiduciary authority to transfer 401(k) assets to the disbursement account in order to generate income for itself without permission.

The DOL has previously addressed float income, recognizing it as a common industry practice. *See, e.g.,* DOL Adv. Op. 93-24A (Sept. 13, 1993); DOL McCormick Info Ltr. (Aug. 11, 1994); DOL FAB 2002-3 (Nov. 5, 2002). In its guidance, the DOL has reiterated that a plan fiduciary does not engage in prohibited self-dealing where it retains float income, **so long as this practice is disclosed and agreed-to as part of the fiduciary's overall compensation**. Complying with this requirement can require detailed documentation and disclosures including, for example, provisions in service agreements, annual 408(b)(2) Covered Service Provider disclosures, and Form 5500 Schedule C reporting.

The float question has bigger implications for qualified plans, however.

If it is improper for a fiduciary to use plan assets to benefit itself (absent detailed disclosures), then how should we treat other common practices that benefit the record-keeper or trustee in a way that is difficult to quantify? For example, 401(k) plan fiduciaries commonly aggregate plan data to provide insights that improve the efficiency and marketing of their own business. If the same ERISA duties apply to a fiduciary's analysis of, say, the savings patterns of millennials, this use of plan data might need to be disclosed in detail to the plan as indirect compensation. At a minimum, plan sponsors need to be attentive to this aspect of fiduciary compensation when negotiating their service agreements.

IRS Reduces VCP Fees (Again); Encourages Plan Corrections

General Fee Reduction. Plan sponsors who submit corrections through the IRS Voluntary Correction Program (VCP) will now face a reduced general fee schedule from the IRS. The new fees generally result in a 25%-40% cost reduction for most qualified plan sponsors, with the largest employers (5,000+ participants) now saving $10,000 on their VCP filings. (Plans with 101-500 participants are not affected.) This is the latest change being made as part of efforts by the IRS to encourage plan sponsors to correct plan failures and maintain plans' tax-qualified status.

The IRS has posted the new fee schedule online. Note that the fee reduction will not apply to corrections filed before February 1, 2016, and the IRS will not issue refunds for earlier filings that are withdrawn and resubmitted.

Targeted Fee Reduction. The latest reduction in VCP user fees follows on last year's targeted fee reduction, part of IRS Rev. Proc. 2015-27, which provided special reduced fees for VCP corrections associated with required minimum distributions and plan loans.

Trap for the Unwary. The IRS has announced that it is still working to update the VCP Form 8951, so plan sponsors are advised to ignore the stated fees on Form 8951 for now, and instead refer to Section 6.08 of IRS Rev. Proc. 2016-8 for user fees.

Recouping Overpayments: Lessons Learned from Recent Cases

Recent case law may limit an employee benefit plan's ability to recoup overpayments made to plan participants.

Erroneous Pension Estimates. In *Paul v. Detroit Edison*, the Sixth Circuit granted summary judgment to a pension plan participant who had relied on his employer's erroneous early retirement benefit estimates for his decision to retire early. 2016 WL 808105 (6th Cir. Mar. 2, 2016). Although such estoppel claims rarely succeed under ERISA, the court concluded that the plaintiff in this case had reached the high bar of demonstrating "extraordinary circumstances" and thus was not obligated to repay $14,429 to the plan. The court held that the employer had misrepresented the plaintiff's benefit amount multiple times (both in writing and orally), and that the employer's failure to ascertain the true facts was "gross negligence" amounting to constructive fraud. The plaintiff was unable to independently verify these calculations and had relied to his detriment on the employer's repeated assurances. (The source of the error? The employer had counted the plaintiff's entire service history (23 years) rather than his service as a union-represented employee (20 years) when calculating the pension benefit.)

Although cases like *Detroit Edison* may be uncommon, calculation errors unfortunately are not. This case underscores the importance of confirming an employee's eligible service and compensation history *before* issuing a written pension estimate. Internal audits and spot-checking should be performed to ensure that automated systems can generate correct pension estimates, especially for complex cases. Where a participant has a complex employment history – due to rehire, reclassification as union/nonunion, or transfer between multiple controlled group entities – pension estimates should be double-checked manually as well.

Timing of Recovery. In *Montanile v. Board of Trustees*, the U.S. Supreme Court held that the plan can enforce a repayment obligation only if the overpayment is traceable to funds or property in the participant's possession, such as an IRA or bank account. 136 S.Ct. 651 (2016). If the participant has "dissipated" the funds – i.e., spent the money on rent, medical care, tuition, food, etc. – the plan cannot recover the overpayment from the participant's general assets, under ERISA or any other law.

This traceability condition poses a problem for qualified plans, and particularly for those offering lump sums. In order to recoup the overpayment as a single sum, the plan administrator needs to act quickly before the assets are dissipated by the participant. This rush to action may run counter to typical qualified plan administration. In a pension or savings plan, it often takes several years for the plan administrator to realize that an overpayment has occurred. These overpayments may result from a programming error that affects multiple participants; additional time may be needed to identify the participants affected and to calculate the amounts involved. Ensuring that the overpayment is corrected in accordance with IRS rules under EPCRS can add to the delay.

The bottom line, however, is that plan sponsors will need to move quickly once an overpayment is discovered. In *Montanile*, the Court faulted the Board of Trustees for its failure to act immediately; the trustees had waited six months to file suit seeking recovery after negotiations with the opposing party broke down. The Court also criticized the Board of Trustees for its failure to respond to an arbitrary 14-day deadline imposed by the opposing party during settlement negotiations.

Fortunately, *Montanile* does not prevent the plan sponsor from recovering overpayments in other ways. The plan administrator often can recoup overpayments from the participant's IRA rollover, or deduct the overpayment amount incrementally from future monthly benefits payable to the participant.

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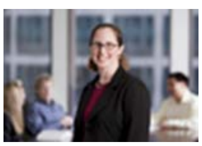

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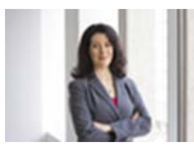

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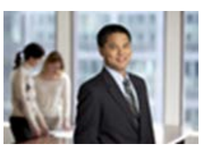

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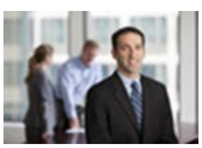

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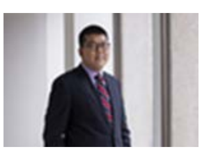

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IPB In The News

Robin Solomon and Jonathan Zimmerman speak on 401(k) Fee Litigation, Stock-Drop Litigation, and Pension De-Risking (February 24, 2016)

Rosina Barker invited to join the American Benefits Council ("ABC") Policy Board of Directors

Ben Grosz quoted by Fiduciary News on 401(k) fee litigation and plan sponsor reaction (February 23, 2016)

Robin Solomon and Ben Grosz quoted by U.S. News & World Report on Tax-Advantaged Employee and Fringe Benefits (February 12, 2016)

Ivins alum Robert Stack honored as Tax Person of the Year for 2015. Mr. Stack was appointed Deputy Assistant Secretary of the Treasury for International Tax Affairs in 2013. Finalists also included Robert Wellen, an Ivins alum who was appointed IRS Associate Chief Counsel in May 2015.

Coming Soon...

Jodi Epstein to present on Minimizing 401(k) Plan Litigation Risk at the Defined Contribution Institutional Investment Association ("DCIIA") public policy forum (April 5, 2016)

Ben Grosz to chair and moderate ABA Business Law CLE program discussing Employee Benefits topics; Steve Witmer to speak as panelist (April 28, 2016)

EB Update Archives

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