A CHANGING RETIREMENT PLAN ENVIRONMENT: THREE THINGS I NEVER THOUGHT I'D SEE

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I. RETROACTIVE ADOPTION OF NEW QUALIFIED RETIREMENT PLANS

A. Under the Setting Every Community Up for Retirement Enhancement ("SECURE") Act of 2019, Congress has extended the date for employers to adopt new retirement plans.

1. Prior to SECURE, the IRS's position was that new qualified retirement plans must be adopted no later than the last day of its tax year.

2. Under SECURE, this was extended to allow an employer to adopt a new plan at any time through the due date of its tax year's return (plus extensions).

a. Under prior law for a calendar-year employer, the plan must have been adopted by December 31st.

b. Schedule for the adoption of calendar year plans under SECURE:

Tax Status	Filing Deadline	Extended Deadline
S Corporations and LLCs taxed as S Corporations	March 15	September 15
Partnerships and LLCs taxes as Partnerships	March 15	September 15
C Corporations	April 15	October 15
Sole Proprietorships	April 15	October 15

3. This provision of SECURE applies to both defined benefit and defined contributions plans; however, it may not be utilized by a 401(k) plan to allow participants to retroactively defer contribution amounts.

B. Employers may now defer any decision on the adoption of a new retirement plan until they've determined earnings for the prior year and which type of plan best suits them.

C. Under prior law, the only option an employer had to retroactively adopt a new plan was adopting a SEP. SEPs, of course, are limited in such areas as contributions, eligibility, vesting, etc.

D. What can't be done under SECURE?

1. Plans can't be retroactively amended (such as changing eligibility or the method of allocation of contributions).

2. Freezing accruals for the plan. Not only may a plan not freeze accruals after the plan year end, but accruals must be frozen no later than the date a participant actually accrues a benefit.

E. The IRS has announced that for employers who retroactively adopt a new plan after a year end, the plan can skip filing a Form 5500 for the first year and begin filing it for the plan's second year.

II. <u>CRYPTOCURRENCIES AS AN INVESTMENT OPTION FOR PARTICIPANTS IN QUALIFIED RETIREMENT PLANS</u>

A. The availability of cryptocurrencies as an investment option has expanded, but it is still not widely available:

1. Although not a qualified retirement plan, there are increasing numbers of custodians/sponsors that have platforms that will allow IRAs (both traditional and Roth) and SEPs to invest in a wide variety of cryptocurrencies and cryptocurrency related funds.

2. A few financial service companies have offered vehicles whereby participants in self-directed defined contribution plans have been offered vehicles that allow investments directly in cryptocurrencies, funds that invest in cryptocurrencies and funds that invest in technology related to cryptocurrencies.

    a. This is done by simply offering access to these funds as part of a menu of available investment alternatives.

    b. In other cases, participants are offered brokerage windows, where they are given access to an account that allows them to invest directly in individual securities or certain commodities.

3. Who are the players?

    a. The first financial services company to offer various cryptocurrency alternatives was ForUsAll in 2021.

    b. Earlier this year, Fidelity announced that before the end of 2022, it will allow 401(k) plans to offer to participants various funds that will give them access to Bitcoin investments and companies that are engaged in digital asset technology. They have even indicated that digital asset accounts will be available alongside traditional investment accounts.

    c. On the other hand, Vanguard has released its own public statement indicating "We don't think that … [crypto investing is] a great way to construct a long-term portfolio for clients."

B. The Department of Labor ("Department") through the Employee Benefits Security Administration ("EBSA"), recently weighed in during March by its issuance of Compliance Assistance Release No. 2022-01: 401(k) Plan Investments in "Cryptocurrencies" ("CAR").

1. The CAR starts out by citing ERISA to require plan fiduciaries to act prudently; and if they violate the prudency standards, they can be held personally liable.

2. It further cites the fact that in defined contribution plans where participants choose their own investments, fiduciaries are required to conduct evaluations as to whether an investment is prudent, even if only included in a menu of investments from which participants can choose.

3. The CAR next indicates that the Department "has serious concerns" about the prudence of a fiduciary's decision to expose 401(k) plan participants to direct investments in cryptocurrencies.

4. It then cites the following reasons for its position:

a. Cryptocurrencies are speculative and volatile investments.

i. The Securities and Exchange Commission characterizes cryptocurrencies as "highly speculative."

ii. The Department's concerns include publicity of fictitious trading, theft, and fraud.

iii. For participants approaching retirement, the extreme volatility can have a devastating impact upon their retirement benefits particularly where substantial allocations have been made to cryptocurrencies.

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b. The Department's concern about the ability of participants to make informed decisions.

   i. Based upon publicity concerning its tremendous profits, participants will not be able to, nor inclined to determine what the facts may actually be.

   ii. Simply by including an investment option in cryptocurrencies, participants may be led to believe that such investments are prudent.

c. Record keeping and custodial concerns for cryptocurrencies:

   i. They are especially vulnerable to hackers and theft.

   ii. The currencies exist as computer code in a digital wallet and not in the form of other traditional investments.

d. Cryptocurrencies pose unique valuation concerns.

   i. Crypto assets valuation is challenging and difficult to do reliably and accurately.

   ii. There are unique valuation issues compared with traditional investments.

e. The regulatory environment for cryptocurrency investments is constantly evolving at this time.

   i. Promotors may fail to abide by new and future regulations.

   ii. Evolving securities laws may lead to inadequate disclosures being made to plan participants.

   iii. Furthermore, evolving securities laws may expose plan fiduciaries to greater liabilities.

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5. In order to emphasize the Department's serious concern over the potential proliferation of cryptocurrencies in 401(k) plans, they have indicated that they expect to conduct "an investigative program aimed at plans that offer participants investments in cryptocurrencies and related products, and to take appropriate action to protect the interest of plan participants and beneficiaries with respect to these investments."

C. In a case filed shortly after the issuance of the CAR, ForUsAll, a cryptocurrency provider, asked the court to set aside the CAR, prohibit the Department from implementing it and prohibit any special investigations caused by cryptocurrency investments.

1. ForUsAll argued that the Department failed to follow the Administrative Procedures Act by their failure to follow correct notice and comment procedures.

2. ForUsAll also noted in its complaint:

    a. The Department rushed the CAR because it feared that the cryptocurrency Super Bowl ads would encourage participants to invest and put their retirement benefits at risk.

    b. That the CAR was contrary to the Biden Administrations' Executive Order that various agencies move forward to review cryptocurrency investments, but do so in accordance with appropriate regulations. It was noted that to date, only the Department accelerated the process.

    c. That because of the guidance, approximately one-third of their clients that had been discussing cryptocurrency investments decided against it because of the fear set forth in the CAR.

3. The Department argued that this is sub-regulatory guidance and does not have the force of law or makes new law. As such, it is simply guidance that provides further interpretation of the fiduciary provisions of ERISA.

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D. Introduction of the Financial Freedom Act and the Retirement Savings Modernization Act.

1. In response to the CAR, members of Congress have recently introduced legislation "to bolster Americans' retirement savings by allowing workers to diversify the assets included in defined contribution plans." In large part, support for the legislation has been divided along party lines with the Republicans introducing legislation and supporting a number of these bills.

2. Generally, the legislation is designed to protect plan sponsors from regulatory investigations and allow participants greater freedom to invest in cryptocurrencies and other non-traditional assets. In order to do this, however, ERISA could be amended to provide protections to fiduciaries who select cryptocurrencies and even permit greater fees to be charged for these types of investments.

3. In response to these legislative initiatives, responses from top Democrats and the administration have included Ways and Means Committee Chair, Richard E. Neil, Senator Elizabeth Warren, and Secretary of Treasury, Janet Yellen. Generally, these responses have been supportive of the Department, the CAR and the clear indication that cryptocurrencies need regulation.

III. A NEW PRE-EXAMINATION COMPLIANCE PROGRAM

A. Over the years, the IRS has successfully developed various programs designed to facilitate self-correction of retirement plan compliance errors.

1. With dwindling resources, the IRS has developed a number of successful programs in the retirement plan area seeking compliance at the least cost and burden to the agency.

a. The IRS publishes and updates Fix-it Guides designed for retirement plans to find, fix, and avoid common mistakes.

b. The Employee Plans Compliance Resolution System ("EPCRS") has been frequently characterized as the most successful compliance program in IRS history.

i. It allows plan sponsors to make reasonable corrections to plan failures without penalties when operational or plan document failures are voluntarily identified.

ii. In many cases, self-correction is possible even without filing with the IRS. If self-correction is not available, procedures describe the form of application and the required user fee to file with the IRS which leads to the issuance of a Compliance Letter.

iii. EPCRS is regularly updated by the IRS and is currently described in Rev. Proc. 2021-30.

c. The Audit Closing Agreement Program ("Audit CAP") is designed for plan sponsors who have significant problems identified during a plan audit but are willing to correct and preserve the tax benefit associated with a properly maintained plan. To be eligible, the plan sponsor must:

i. Correct the plan failure.

ii. Enter into a Closing Agreement that describes their responsibilities.

iii. Pay a negotiated monetary sanction that "will not be excessive and will bear a reasonable relationship to the nature, extent and severity of the failure." This is typically done by starting with determining the total tax cost of the plan's disqualification (maximum payment amount) and then negotiating a sanction based upon a percentage of the maximum payment amount.

2. On June 2, 2022, the IRS announced the implementation of a new pre-examination compliance program. The new program is designed to give plan sponsors a final opportunity to correct plan failures voluntarily before the plan is subjected to audit.

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B. How the new program will work.

1. The IRS will send letters to plan sponsors notifying them of an upcoming audit.

2. The sponsor will be given 90 days to review its plan to identify any operational or document errors and report those errors along with the required correction to the IRS.

3. Errors that are identified may be self-corrected, if permitted under ERCRS. If not eligible for self-correction, the plan sponsor will then enter into a Closing Agreement to make the required correction and pay a fee comparable to the correction fee paid under EPCRS when required.

4. The IRS may then close the matter; however, it reserves the right to conduct a limited or full scope audit.

C. The essence of the program is:

1. To give plan sponsors a 90-day warning to self-correct.

2. “Deputize” the entire retirement plan practitioner community to conduct audits on behalf of the IRS.

D. Some practitioners have expressed concerns that the program may actually be counterproductive. If a 90-day warning is made available as a matter of course, there will be little incentive for a plan sponsor to use EPCRS to voluntarily correct, knowing they will get the same deal if they are chosen for audit.

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