Retirement PLAN news

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Handling QDROs **for Your Retirement Plan**

When couples divorce, one spouse's retirement benefits may be divided as part of a property settlement. Although federal law generally does not allow plan participants to assign or alienate their retirement plan interests, there is a limited exception. Retirement benefits may be assigned to a spouse, former spouse, child, or other dependent to satisfy family support or marital property obligations through a domestic relations order if the plan administrator determines it is a qualified domestic relations order (QDRO).

Definitions

Knowing how the law defines "domestic relations order" is the first step in making a proper determination. A domestic relations order (1) is a judgment, decree, or order, including the approval of a property settlement agreement, (2) is made pursuant to state domestic relations law, and (3) relates to the provision of child support, alimony, or marital property rights to a spouse, former spouse, child, or other dependent of a plan participant (called "alternate payees"). A QDRO is a domestic relations order that creates or recognizes the existence of an alternate payee's right to, or assigns to an alternate payee the right to receive, all or a portion of a participant's plan benefits and that meets certain additional requirements.

Required Information

A QDRO must contain the following information:

- The name and last known mailing address of the participant and each alternate payee
- Each retirement plan affected by the order
- The dollar amount or percentage of the benefit to be paid to the alternate payee or the method for determining the amount or percentage
- The number of payments or the time period to which the order applies

Certain Provisions Not Allowed

Before making a determination that a domestic relations order is qualified, the plan administrator must make sure that the order does not require the plan to provide any form of benefit, or any option, that is not otherwise provided for under the plan.

Additionally, the order may not require the plan to pay an alternate payee benefits that are required to be paid to another alternate payee under a previous QDRO.

QDRO Procedures

Your retirement plan should have written procedures for determining whether any domestic relations orders it receives are QDROs and for administering distributions pursuant to QDROs. When a domestic relations order is received, the plan administrator should promptly notify the plan participant and alternate payee that the order has been received and provide a copy of the QDRO procedures.

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Keys to Avoiding Compensation Errors

The plan's definition of "compensation" is important for many different aspects of plan administration — including elective deferrals, allocations, and discrimination testing. Plan sponsors need to be certain that the definition of compensation is properly applied. Failure to do so could result in an operational failure and possibly affect the plan's qualified status.

Mistakes may arise because many plan sponsors operate their plan based on a plan summary of the definitions and operational requirements. But as the plan is amended, the compensation definition may change while the plan continues to operate as it had previously. To avoid compensation-related mistakes, the IRS recommends the following:

- Review your plan document for the definition of compensation for each plan purpose.
- Use the statutory definition of compensation when required.
- Ensure that your payroll processor and plan administrator receive accurate compensation data.
- Simplify your plan's definition of compensation by considering using one definition for all plan purposes.
- Review your plan for errors and use the IRS correction programs to fix them as quickly as possible.

In addition, your plan may avoid mistakes by properly training the plan personnel who determine compensation to confirm they understand the plan document.

Handling QDROs for Your Retirement Plan (continued)

The procedures should describe any time limits for making a determination, which must be accomplished within a reasonable period after receipt of the order. Include the steps the administrator will take to protect and preserve retirement assets or benefits upon receipt of a domestic relations order. (Note that during the determination period, the plan administrator is required to separately account for the amounts which would have been payable to the alternate payee during such period.) The procedures should also describe the process for obtaining a review of the administrator's QDRO determination.

As part of the procedures, a plan can include an explanation of the information the plan will make available to prospective alternate payees to assist with QDRO preparation, such as participant benefit statements and the summary plan description. According to the U.S. Department of Labor, a plan administrator may condition disclosure of this information on an alternate payee's providing the plan with sufficient information to reasonably establish that the disclosure request is being made in connection with a domestic relations proceeding.

Payment Timing

If an alternate payee is to receive a separate interest under a QDRO, the order may specify the time the alternate payee will receive the interest or assign to the alternate payee the same right the participant would have had under the plan with respect to payment timing. Either way, the QDRO may not provide for payment to be made to the alternate payee any earlier than the participant's "earliest retirement age" (unless the plan permits payments at an earlier date).

Generally, a participant's earliest retirement age is the earlier of two dates:

(1) the date on which the participant is entitled to a distribution under the plan or

(2) the later of either

   (a) the date the participant turns 50 or

   (b) the earliest date on which the participant could begin receiving benefits under the plan if the participant separated from service with the employer

Conclusion

The QDRO rules contain other details not covered in this broad overview. Since failure to follow proper QDRO procedures can have serious repercussions, including potential disqualification of your plan, you may want to review your plan's procedures with a professional advisor to ensure that all bases are covered.

Determining 401(k) Plan **Eligibility Requirements**

Establishing eligibility requirements for plan participation requires consideration of both the broad range of available options and the potential effects that different sets of eligibility requirements may have on hiring, retention, and administrative costs. Following is a brief overview of the applicable rules.

Conditions of Eligibility

Federal law establishes the limits of what conditions may be set on eligibility. Generally, plans may require employees to attain any age up to 21 years old before they may become participants in the plan. Plans may also require up to one year of service before employees may make elective contributions. If a 401(k) plan also provides for other types of employer contributions (such as matching on nonelective contributions), it may require that employees complete up to two years of service before being eligible to receive these contributions. In such cases, however, the employees must be 100 percent vested in the employer contributions.

1,000 Hours-of-Service Rule

Generally, a "year of service" is a 12-month period during which an employee completes the number of hours of service specified in the plan. A plan may not specify more than 1,000 hours for this purpose.

An employee's first year of service is measured during a 12-consecutive-month "initial eligibility computation period," which begins on the employee's "employment commencement date." For periods after the initial eligibility computation period, the plan must measure service for participation purposes either during the 12-consecutive-month periods that begin on the anniversaries of the employment commencement date or during the plan years that include such anniversaries.

Elapsed-time Method

The elapsed-time method is an alternative for retirement plans to define crediting service for eligibility. In this system, a year of service is completed when the employee completes 12 months or 365 days of service, regardless of how much he or she actually worked during that period. This system is easier to administer because it does not require keeping track of actual or equivalent hours of service during distinct 12-month periods.

Instead, the employer monitors the period beginning with the employee's date of hire through the date the employee meets the eligibility requirements. This method requires only that the employee be employed on both the original hire date and on the last date of the eligibility period established by the plan.

Effect of Service Spanning Rule

The IRS has service spanning rules that apply under the elapsed-time method. Generally, under these rules, the employee is not penalized for absences of less than 12 consecutive months. For example, assume a company has a one-year elapsed-time eligibility requirement. If an employee is hired on June 15, 2016, leaves the company on August 20, 2016, and then is rehired on February 10, 2017, he or she fulfills the one-year service requirement since the absence was less than one year.

Setting Eligibility Terms

When choosing eligibility requirements, retirement plan sponsors should consider such issues as the number of part-time employees they have, the goals of their 401(k) plans, and how different eligibility requirements might affect administrative costs. For example, if a company has high employee turnover, it may choose longer service requirements to reduce its administrative burdens. For similar reasons, an employer with numerous part-time employees may wish to avoid the elapsed time method. On the other hand, sponsors may want to consider whether raising the eligibility requirements might make hiring top talent more difficult and/or impair their employees' ability to prepare for retirement.

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Recent **Developments**

IRS Proposal for Plan Forfeitures

The IRS has proposed new regulations regarding the use of forfeitures by 401(k) plans to fund qualified non-elective contributions (QNECs) and qualified matching contributions (QMACs). Plan sponsors typically use QNECs and QMACs to correct testing failures. Under existing rules, the QNECs and QMACs must be nonforfeitable *at the time of contribution*. This requirement limits their use, because forfeitures are typically subject to a vesting schedule at the time of contribution. Under the proposed regulations, contributions will qualify as QNECs or QMACs if they meet the nonforfeitability and distribution requirements *at the time they are allocated to participants' accounts*, rather than when they are first contributed to the plan.

Retirement Health Expenses

The latest estimates from the Employee Benefit Research Institute show that a married couple retiring in 2016 needs $165,000 to have a 50% chance of being able to cover health costs in retirement. A 65-year-old man would need $72,000 in savings and a 65-year-old woman would need $93,000 to have a 50% chance of having enough money saved to cover health expenses in retirement. These projections assume median drug expenses throughout retirement. The study excludes long-term care expenses and health care expenses not traditionally covered by Medicare.

Fairly Confident for Retirement

A recent *Ipsos/USA Today* survey of Americans between the ages of 45 and 65 found that 77% feel strongly or somewhat agree that they will need to save more to afford the type of retirement they prefer. But 59% feel very or somewhat prepared for retirement and 55% are very or somewhat confident that they will have enough money to get them through retirement. To help get them to the retirement lifestyle they want, 65% of those surveyed state they are very or somewhat likely to contribute at least $100 toward their retirement savings in the next six months. To fund their retirement, 42% plan to rely mostly on their savings or benefits.

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