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# the dana report

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## ABOUT THE FIRMS

Dana Consulting Group, Ltd. and Jennings Law Firm, Ltd. were established to provide employers with a single source of comprehensive legal and consulting services relating to retirement plan and employee benefit matters.

## QUOTES

Nothing is ever always wrong. Even a clock that stops is right twice a day.

- Anonymous

I cannot give you a formula for success, but I can give you the formula for failure which is: Try to please everybody.

- Herbert Bayard Swope

An effective way to express appreciation: "If you don't like what I do, tell me. If you like what I do, tell my boss."

- Anonymous

Route To:

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## ***Fiduciary-Level and Participant-Level Fee Disclosure Rules Extended***

The US Labor Dept has extended again the final regulations to April 1, 2012 relating to disclosure rules relating to qualified retirement plans. On July 16, 2010 the Labor Dept issued interim final regulations (the "408(b)(2) regulations") that require ERISA plan service providers to disclose information to enable fiduciaries to understand the reasonableness of fees charged against plan assets. [Fees paid by the plan sponsor are not subject to these regulations.] On October 20, 2010, the Labor Dept issued final rules relating to disclosure of plan fees and expenses that must be furnished to plan participants (these are called the "participant-level disclosure regulations").

The Labor Dept has extended the effective date of the 408(b)(2) regulations to April 1, 2012, which is three months later than the most recent effective date. Moreover the Labor Dept has tied the effective date of the participant-level disclosure regulations to the 408(b)(2) regulations and, accordingly, the effective date of these regulations are also extended to April 1, 2012. ■

## ***When Do Retirement Plans Require Certified Audits?***

Qualified retirement plans covering fewer than 100 participants are generally exempt from the requirement to engage a CPA to perform an annual audit of the plan's financial statements. However, in situations where more than 5% of the plan's assets are not invested in "qualifying plan assets," an audit is required unless certain requirements are met. The most important

requirement is that there is an ERISA bond covering the entire value of the non-qualifying assets. We have seen an increase in retirement plans investing in non-qualifying assets (e.g., gold coins or real estate) and it is essential that the plan's fiduciaries review the plan's bond coverage to ensure that the bond amount is sufficient. We have posted a firm memo on our website at [www.danaconsulting.com](http://www.danaconsulting.com) under the Education Center summarizing these rules. As an added service for those plans that do need an audit, we have also posted a list of CPA firms we have worked with who can conduct the audit on a cost-effective basis. ■

## ***The Future of Defined Benefit Plans***

Senator Thomas Harkin (D-Iowa) is chairman of the Senate Health, Education, Labor and Pensions Committee and he is asking questions about why the number of defined benefit (DB) plans has decreased from 112,000 in the mid-1980s to 27,000 in 2008, a drop of almost 76%. Senator Harkin is conducting hearings on the matter and heard witnesses described reasons such as overregulation to adverse accounting rules. According to one preliminary analysis of the impact of defined benefit plans on the US economy conducted by the National Institute on Retirement Security, a Washington, DC think tank, private and public DB plans had a total economic impact of \$756 billion and supported over 5.3 million US jobs, and generated over \$121.5 billion in annual federal, state and local tax revenue in 2009.

*Our Comment.* Senator Harkin's committee is where much legislation originates that affects

qualified plans. Thus, it is good to see the chairman is trying to take a serious look at resuscitating defined benefit plans. Large corporate America is unlikely to bring back their terminated DB plans and so if Congress wants to see these plans survive and grow, it is up to smaller employers to do it - provided the legislative environment changes for the better. We follow Congress on legislative matters closely and we have observed numerous times in the past that Congress does not move quickly on big issues. Retirement plan legislation in the US is a BIG issue and we don't expect any earth shattering legislative changes soon. However it is good to see that an important senator is taking a hard look at this issue. DB plans and their hybrid sister - the cash balance plan - are still in certain ways niche plans but where they work, they work very well. More and more of our clients are establishing these plans, not only to create substantially larger tax deductions for owners and key employees but also to provide more effective retirement programs for their employees. We regularly report on the sorry state of the Social Security trust fund and Congress's lack of appetite to reform that system (at least for the next 30 years according to Senator Harry Reid). Thus Congress needs to continue with their baby step moves to improve the legislation rules governing qualified retirement plans. Employer-based plans will continue to provide the foundation for many working Americans' retirement security and if Congress wants to alleviate the growing pressure on Social Security, further and ongoing changes affecting employer plans should continue. Hopefully Senator Harkin's hearings demonstrate this ongoing progress. ■

### ***Form Over Substance under ERISA***

There is a well known doctrine under US tax laws that the IRS can ignore transactions undertaken with no apparent purpose other than to create tax benefits. This doctrine is sometimes referred to as Substance over Form, or the business-purpose doctrine. The court decision is Gregory v. Helvering, 60 F2d 809 (2<sup>nd</sup> Cir. 1934) and the opinion written by Learned Hand, one of the greatest judges to ever serve, is a marvelous read. The Fifth Circuit recently issued its opinion in Brown v Continental Airlines Inc. (5<sup>th</sup> Cir. No. 10-20015, 7/18/11) indicating in effect that substance over form is not applicable under ERISA. Here are the facts: In May 2009, Continental sued nine pilots and their spouses alleging the pilots and their spouses obtained sham divorces for the sole purpose of obtaining lump sum pension distributions the pilots could not have otherwise obtained without terminating their employment. The couples divorced and submitted qualified domestic relations orders (QDROs) assigning their entire pension benefits to their spouses which the Continental plan permitted to be paid immediately in lump sums. After paying all of the lump sums, Continental discovered the pilots had remarried their former spouses, and further the couples had concealed the divorces from their families and friends, and shockingly even continued living together.

There never seemed to be any doubt that the divorces were shams and entered into solely to obtain pension benefits the pilots could not otherwise receive without terminating their employment. The court acknowledged that sham

transactions can be disregarded under tax, bankruptcy and immigration laws but indicated that Congress had not expressly made QDROs subject to a sham transaction rule and, therefore, the court had no authority to do so now. The court indicated that the plan administrator's sole authority was to determine whether the divorce orders complied with the statutory requirements to qualify as QDROs and nothing more. The motives, proper or not, were irrelevant to whether the orders would be complied with.

*Our Comment:* The Fifth Circuit encompasses Texas, Louisiana and Mississippi and so is not binding in Illinois, where most of our clients reside. Illinois is in the Seventh Circuit and we are aware of no similar court opinion issued here. The opinion, however, could have significant impact on how plan administrators carry out their duties. For example, a participant requests a hardship withdrawal by properly completing the paperwork but the plan administrator clearly knows the participant has not incurred any hardship. We believe the IRS would take a dim view of approving sham hardship withdrawals but the Fifth Circuit could preclude the plan administrator from denying the withdrawal request. The opinion imposes no good faith requirement on the participant in how he deals with the plan. Plan administrators, however, are fiduciaries and have affirmative duties to administer the plan prudently and solely in the interest of plan participants. This opinion in our view creates a conflict in fiduciaries' duties and will be something our firm monitors closely. ■



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