Benefit Insights

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A non-technical review of qualified retirement plan legislative and administrative issues **October 2010**

Record Retention

The record storage business is booming. A Google search yields pages and pages of links to companies offering to safely and securely store vital personal and/or business records.

As the regulatory environment in which businesses operate becomes increasingly complex, the need to maintain thorough records of various activities becomes increasingly important. Employee benefit plans are no exception. The rights afforded to plan participants are protected by strict legal standards, which means plan sponsors must be able to document that all promised benefits have been provided.

With the number of employees that come and go over time, benefits documentation can pile up very quickly, leading many plan sponsors to ask, "When can I get rid of all this stuff?" As with most questions related to benefit plans, the answer is a resounding "it depends."

The Rules

Both the Internal Revenue Service (IRS) and Department of Labor (DOL) have rules that provide some basic guidance on record retention. Some of these guidelines are derived from the timeframe during which one of the agencies can conduct an audit of an employee benefit plan. This is referred to as the statute of limitations.

IRS Statute of Limitations

Generally speaking, the IRS statute of limitations runs for a period of three years from the date Form 5500 is filed for a given year. The Form 5500 must be filed no later than the end of the 7th month following the close of a plan year. That deadline may be extended by an additional 2½ months. That means that a calendar year plan may file its Form 5500 as late as October 15th of the following year.

Example: A calendar year 401(k) plan files its Form 5500 for the 2007 plan year on October 15, 2008. The IRS statute of limitations remains open, allowing them to audit the 2007 plan year until October 15, 2011.

Those who have been through an IRS audit of their 401(k) plan can confirm that the information requested is quite extensive and covers the entire range of plan operations from plan document maintenance to properly enrolling new

participants to withholding the appropriate taxes from distributions.

ERISA Record Retention Requirements

In addition to the IRS statute of limitations, ERISA includes several sections focusing on record retention. ERISA Section 107 requires that anyone filing an employee benefit plan report, such as Form 5500, must maintain sufficient records to support all information included on the report for at least six years from the date the report is filed.

Example: Using the same assumptions from the above example, records to support all data on the 2007 Form 5500 must be retained until October 15, 2014–7 years and 9½ months from the start of the 2007 plan year.

So, does that mean it is finally safe to clean out the filing cabinets every 8 years? Unfortunately, ERISA makes it a little more complicated than that. Section 209 imposes an additional obligation to maintain all records necessary to determine benefits that are or may become due to each employee. In 1980, the DOL issued proposed regulations interpreting this section to mean that records must be retained "as long as a possibility exists that they might be relevant to a determination of the benefit entitlements of a participant or beneficiary."

The Devil is in the Details

The length of time records might be relevant to determine benefits varies from plan to plan and from employee to employee, making it very challenging for plan sponsors to know if and when they can finally dispose of historical plan records. There are any number of situations that may arise well beyond the 8-year timeframe described above.

Schedule SSA/Form 8955-SSA

Consider this example. Employers are required to file Schedule SSA with each year's Form 5500 to report former participants with balances remaining in the plan. Although the Schedule SSA has been discontinued, the IRS is developing Form 8955-SSA to replace it. While the Schedule SSA did allow employers to "un-report" these participants once they take distributions, it was optional to do so. As a result, it has been somewhat common practice to only add newly terminated employees to the list without ever removing those who have received their benefits.

The information from the schedule is provided to the Social Security Administration. When retirees apply for Social Security benefits, the SSA database notifies them that they may be entitled to benefits from the previous employer's plan. Without clear records showing the participant already received his plan benefits, it can be very difficult to convince a now-retired, former employee (possibly from several decades ago) that the letter he received from the government is incorrect. The matter can be further complicated when it involves the beneficiary of a deceased former employee.

Beyond Benefits

The need to reference historical records to determine benefits can be triggered by issues extraneous to the plan. Employment disputes are a prime example. The infamous court case involving Microsoft's misclassification of employees as independent contractors arose from a 1989-1990 IRS payroll-tax audit of the company.

Once it was determined these workers were employees, the question of entitlement to benefits quickly followed. It was not until 1999 that the Ninth Circuit Court of Appeals settled the dispute and awarded back benefits to the misclassified workers. The Microsoft case illustrates how a payroll-tax issue required review of records more than 10 years old to determine benefits.

So, What is the Solution?

Because of the countless variables that exist, there is no one-size-fits-all solution; however, there are several steps plan sponsors can take to point themselves in the right direction.

Take Inventory

One of the first steps to take is to determine what records currently exist and where they are stored. Some may be electronic; some may be in binders; and some may be in boxes in storage. That inventory will highlight any gaps that may need to be filled and provide some perspective to allow the assessment of alternative retention options.

A service-provider's recordkeeping system may be utilized to track and house information on historical plan activity; however, the determination of benefits is ultimately the responsibility of the plan sponsor. Therefore, copies of all reports generated by the recordkeeper should be maintained. This is especially important when changing service providers as typically they are only required to retain records for a limited period of time.

Review Operational Policies and Procedures

If a plan operates efficiently and consistently, there are likely to be fewer issues that require digging into the archives. For example, consider a review of all previous Schedules SSA that have been filed. If any previously reported participants have received their benefits, un-report them on the next filing and establish a process to do so each year.

As current employees leave the company, take steps to process distributions quickly. Terminated participants with vested balances below $5,000 can generally be forced out of the plan with 30-days advance notice. Any former employees who receive distributions prior to the filing deadline for the Schedule SSA/Form 8955-SSA do not have to be reported.

Use Electronic Storage

Physical storage space can be expensive, so many plan sponsors have turned to electronic storage for some or all of their plan records. While there are no absolute restrictions on maintaining electronic records, there are some practicalities to consider.

Records must be easily accessible. Unreasonable delays in retrieving information can provoke an already disgruntled former employee to take the next step and call his attorney. If the dispute is already being litigated, delays can have a negative impact on the proceedings.

Security is very important. Plan records include everything a thief needs to abscond with the identities of all the participants: social security numbers, birth dates, addresses, etc. Therefore, electronic storage must be secure. This could range from placing inherently unsecure media under lock and key to employing various forms of encryption. Although benefit plans are primarily the purview of federal law, many states are implementing stringent new laws governing the protection of personal information. Employers must be mindful of any such state laws that may be applicable.

Technology changes…quickly. Not only have storage media changed significantly in only the last 15 years but data encryption has also advanced at lightning speed. Just because plan records are securely backed-up using the technology du jour does not mean out-of-sight-out-of-mind. As there are advancements in technology, record retention policies should provide for the occasional migration to more current systems to preserve the integrity and security of the data.

Seek Professional Assistance

Depending on the circumstances and the volume of information in question, it may be prudent to work with an attorney or consultant specializing in record retention requirements. In addi-

tion to helping craft a policy, such a professional may also be able to make recommendations for vendors or technologies to most cost-effectively implement the policy.

Records to Retain

Records that should be maintained include (but are not limited to) the following:

- Plan documents, including amendments and determination letters/opinion letters;
- Summary Plan Descriptions and Summaries of Material Modification;
- Company resolutions declaring match and/or profit sharing contributions;
- Participant notices and documentation of the dates and method of delivery;
- Participant elections such as deferral and investment elections;
- Census information including payroll data and employment history;
- Nondiscrimination test results;
- Form 5500 including schedules and attachments;
- Plan account and financial statements;
- Recordkeeping/valuation reports at both the plan and participant level;
- Participant loan documentation including amortization schedules and promissory notes; and
- Participant distribution forms including special tax notices, election forms and 1099-R forms.

Conclusion

Corralling benefit plan records may seem like a daunting task, especially considering the relative infrequency that information must be accessed. Beyond the required seven- to eight-year timeframe plan records must be maintained, it only takes one claim to demonstrate the value of an organized system. As the saying goes, some careful planning and knowledgeable advice will allow creation of an "ounce of prevention" policy to minimize the likelihood of the "pound of cure" dispute years in the future.

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