



BENEFIT *Advisor*

In This Issue

In this second issue of the McGrawWentworth Benefit Advisor for 2006, we will discuss the ERISA requirement for certain plans to file a Form 5500. Many organizations are confused regarding their obligations to file a Form 5500. This Advisor will outline the basics regarding 5500 forms and the process for filing the form.

We welcome your comments and suggestions regarding this issue of our technical bulletin. For more information on this Benefit Advisor, please contact your Account Manager or visit our web site at www.mcgrawwentworth.com.

“Form 5500 - To File or Not to File?”

The answer to this question is not particularly clear to many plan sponsors. Filing an annual Form 5500 is a main ERISA Title I requirement. However, the requirement applies only to certain employers and specific benefit plans. Often organizations are unsure whether they need to file a Form 5500.

This Advisor analyzes the following aspects of the Form 5500 in depth:

- The basics, including the purpose of the form, filing time frames, and the benefits to include in filing.
- Exemptions for filing 5500s, including small employer exemptions and cafeteria plan requirements.
- The schedules, including the schedules you may need to attach to your Form 5500.
- The process for completing the Form 5500.
- The penalties for not filing the Form 5500.

Filing 5500s can be tedious, as many ERISA plans have several components. Plan sponsors need to know when they must file the report and all the specifics involved.

The Basics

Title I of ERISA imposes various reporting requirements on welfare benefit plans, MEWAs (multiple employer welfare arrangements) and plans that use VEBAs (voluntary employee benefit associations).

The main reporting requirement for welfare plans is the Form 5500 annual filing. Plan administrators must submit the form and any required attachments annually.



Certain employers and benefit plans are exempt from these requirements (see the next section). However, most employer plans must file the report.

Often, organizations confuse insurance policies with ERISA plans. ERISA plans are employer-established plans that can include a number of benefits. The employer creates a Master Plan Document establishing the ERISA plan name, plan year, plan number, plan benefits and so on. For welfare plans, the plan number must be a 500 series number. A Form 5500 needs to be filed on each ERISA plan that has been established. This can include medical, dental, vision, life, long term disability, and even in some cases, employee assistance programs (if counseling services are a covered expense).

The Form 5500 must be filed by the last day of the seventh month after the close of the ERISA plan year. For plans based on a calendar year, the Form 5500 must be mailed by July 31. The date the form is mailed is considered the filing date.

Employers may use Form 5558 to request an extension of up to 2 ½ months if they cannot meet the initial deadline. The extension will be granted automatically if the Form 5558 is filed by the normal Form 5500 due date. If an employer has multiple ERISA plans, the Form 5558 must be filed independently for each plan.

Exemptions from Filing Requirements

The requirements for filing a Form 5500 generally applies to all ERISA plans. If a plan is not subject to ERISA, there is no requirement to file a 5500. The Department of Labor (DOL) may exempt various welfare plans. The DOL exempts small unfunded plans, small insured plans or a combination of small insured and unfunded plans. In order to be considered a "small" plan, the plan must have fewer than 100 covered participants at the beginning of the plan year. The exemption applies even if the number of covered participants goes above 100 during the plan year.

Interestingly, if a plan has over 100 participants, files a 5500 and then drops below the 100 minimum threshold, the plan can discontinue filing the Form 5500. There is a special code that must be entered on the last 5500 filed to indicate the plan has fallen below the 100

participant minimum and will not be filing the 5500 in the next plan year.

For the 100 participant threshold, only covered participants in the ERISA plan are counted. A participant is an employee or former employee who becomes covered on the earlier of:

- The date the plan says participation begins.
- The date the individual becomes eligible to receive a benefit under the plan.
- The date an individual makes a plan contribution.

COBRA participants are counted when determining the number of plan participants.

The exemption applies to insured and "unfunded" self-funded benefit plans. An unfunded plan is a plan that pays benefits solely from the sponsoring employer's general assets. A plan becomes funded when it pays benefits using "plan assets." In theory, cafeteria plans funded by participant contributions should be considered funded. However, according to the

DOL's Technical Release 92-01 if the plan is considered funded solely because employees contribute to it, the DOL will not enforce the 5500

reporting requirement. Plans using trusts to pay benefits are considered to have plan assets. Separate accounts used to pay benefits are considered plan assets unless they are separate accounts in the employer's name. The actual Form 5500 definition of "trust" is "any fund or account that receives, holds, transmits or invests plan assets,

other than an account or policy of an insurance company."

Small insured plans must meet the following requirements to qualify for the exemption:

- They must pay benefits exclusively through an insurance arrangement.
- Employers must pay premiums directly from their general assets or from participant contributions. Participant contributions must be sent to the insurance carrier no later than 3 months after being withheld from pay.
- Employers must send any refunds to plan participants within 3 months of the contribution.

Although fringe benefit plans originally were required to file a Form 5500, they are now exempt. Fringe benefit plans include Section 125 cafeteria plans, educational assistance plans, or adoption assistance plans. The fringe benefit plans were required to complete certain sections of the 5500 form and a Schedule F had to be attached to the 5500. In April 2002, the IRS suspended the filing requirements for all fringe benefit plans for all future and *past* filing years.

This was good news for employers but it created some confusion as well. The IRS has suspended the requirements for these fringe benefit plans; however, group health plans with 100 or more participants are still required to file Form 5500 under ERISA. Be sure to remember the IRS suspension does not apply to ERISA requirements for group health plans. Therefore, if an employer sponsors a cafeteria plan that includes a health care flexible spending account and has more than 100



participants in the health care flexible spending account plan, the employer must file a 5500 on the Section 125 plan to meet the ERISA requirements.

Generally, if organizations with fewer than 100 participants offer health care flexible spending accounts, they do not need to file a Form 5500 on the cafeteria plan. While this is usually true, it really depends on your ERISA plan structure. Remember, employers have great flexibility in setting up their ERISA plans. A few examples will help demonstrate how this works with various plan set-ups (see table below).

Other exempt plans include:

- Government plans
- Church plans
- Unfunded or fully insured welfare benefit plans that provide benefits to a select group of management or highly compensated employees, commonly called “top-hat” plans
- An unfunded, short-term disability income or salary continuation plan where the benefits are paid from the general assets of the employer. The DOL views these plans as payroll practice and not

welfare plans within Title I of ERISA

Your organization should review your ERISA plan arrangements to determine which plans will require a 5500 filing.

The Schedules

You may need to attach specific schedules to your organization’s Form 5500. Different plan arrangements require different schedules.

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	ERISA Plan Set-Up	Requirements
Scenario A	Employer has one ERISA Plan 501, it includes: - Medical, dental, vision, life and so on 500 plan participants - Cafeteria Plan with health care reimbursement account (HCRA), HCRA participants 80 Participants	- Employer must file a 5500 for Plan 501. - The employer needs to include HCRA participants in employee counts. - Employer does not need to attach a Schedule F.
Scenario B	Employer has one ERISA Plan 501, it includes: - Medical, dental, vision, life and so on 500 plan participants - HCRA 130 participants	- Employer must file a 5500 for Plan 501. - The employer needs to include HCRA participants in employee counts. - Employer does not need to attach a Schedule F.
Scenario C	Employer has two ERISA plans: Plan 501 - it includes: - Medical, dental, vision, life and so on 500 plan participants Plan 525 - it includes: - HCRA 80 participants	- Employer must file a Form 5500 on Plan 501. - Employer does not need to file a Form 5500 on Plan 525 because the HCRA has less than 100 participants.
Scenario D	Employer has two ERISA plans: Plan 501 - it includes: - Medical, dental, vision, life and so on 500 plan participants Plan 525 - it includes: - HCRA 120 participants	- Employer must file a Form 5500 on Plan 501 and Plan 525 separately. - Employer does not need to attach a Schedule F to the 5500 for Plan 525.

The following is a summary of the schedules that may apply:

- **Schedule A:** You must include a Schedule A if an insurance contract covers any part of the benefits provided by your pension or welfare plan. For any insurance arrangement, your organization will need to attach a Schedule A. If you have three insured HMO plans, one insured life plan and one insured disability plan under your ERISA master plan, you must attach a Schedule A for each HMO, one from your life carrier and one from your disability carrier. Carriers must provide the Schedule A information within 120 days of the end of the plan year.

If your organization's ERISA plan year differs from its insurance carrier's policy year, it may be



difficult to get the Schedule A information based on the ERISA plan year. The good news is the Schedule A information is not required to be reported on the ERISA plan year. When the plan and policy year differ, the Schedule A may be provided based on the insurance contract year, providing the contract year ends within the ERISA plan year.

- **Schedule C:** This schedule is required only for large plans (over 100 participants) and in situations where plan assets are used to pay service providers at least \$5,000 or more in compensation. If a plan is not funded (benefits are paid from the general assets of the employer), the Schedule C does not need to be provided.
- **Schedule D:** This schedule applies when a plan invests in certain "direct filing entities."
- **Schedule F:** This schedule is no longer required. It used to apply to fringe benefit plans.
- **Schedule G:** This schedule applies only in certain circumstances and an accountant or attorney will need to complete the specifics regarding various transactions relating to plan assets.

Many of the schedules listed above will not apply to your health and welfare ERISA plans. There are also additional schedules not listed above. These schedules generally need to be filed with the 5500s for your pension and retirement plans.

Process for Completing Form 5500

The Form 5500 is not static. Each year the government releases a Form 5500 for that year. The changes are

not substantial, but your organization should use the form for the appropriate plan year. The Form for 2005 can be found at <http://www.irs.gov/pub/irs-pdf/f5500.pdf>.

Currently, employers can submit hard copies of the forms and any necessary attachments to the IRS. However, several years ago the DOL created an automated filing process called EFAST. EFAST uses electronic elements in the filing process, and includes the following:

- Government printed "hand print" forms that must be filed on paper.
- Computer-generated forms with barcodes to encode data which can be filed on paper or electronically.

The DOL has issued proposed regulations that would require employers to file 5500 forms electronically. The proposed regulations would apply for plan years beginning on or after January 1, 2007, with the first mandated electronically filed forms due in 2008.

These proposed regulations have not been finalized. The Department of Labor would need to modify its electronic systems to allow filing over the Internet. Currently, very few plans file electronically and the cost to the IRS associated with processing all the paper filings is substantial. The electronic filing may not be mandated for plan years beginning on or after January 1, 2007; however, expect that it will become mandatory within five years.

Although many plans prefer to outsource the filing, your organization can complete a Form 5500 on its own. The reporting require-

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NOTABLE THOUGHTS

THE MAN WHO WINS IS THE MAN WHO THINKS HE CAN.

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ments can be completed by an informed human resources professional. An accounting firm can prepare your 5500 Form for a reasonable fee. In addition, the DOL maintains a list of approved software vendors offering computer programs you may use to help. The list of vendors can be found at <http://www.efast.dol.gov/software.html#vendors>. The DOL does not endorse any of these software products, but simply notes their capabilities in regard to electronic filing.

Penalties for Not Filing

Penalties for not filing a Form 5500 can be substantial. In addition, both the IRS and the DOL can impose penalties on an ERISA plan for failing to file or filing an incorrect 5500. The IRS penalties apply to a deferred compensation plans such as qualified retirement plans, certain trust and annuity plans and so on. The IRS penalty for failing to file an annual return is \$25 a day up to a \$15,000 maximum.

The DOL penalties are much more substantial. Penalties apply not only to plans that fail to file or file late; they also apply to incomplete or other deficient Form 5500s. The DOL penalty for failing or refusing to file a 5500 is up to \$1,100 a day. Penalties apply separately to each plan the employer establishes.

ERISA also contains criminal penalties for anyone who deliberately violates any Part I, Title I ERISA provision. Criminal penalties can include a fine of up to \$100,000 and up to 10 years in prison or both. The penalties apply to anyone who

knowingly and voluntarily violates the ERISA provisions.

The DOL offers a Delinquent Filer Voluntary Compliance (DFVC) program to encourage organizations to comply voluntarily with ERISA's annual reporting requirements. The program allows delinquent plan administrators the chance to "turn themselves in" and voluntarily pay a reduced penalty. The DFVC program applies only to plan administrators who have not yet been officially notified that they failed to file a 5500 on time. This means you cannot turn yourself in voluntarily, once you have been caught.

The advantage of "turning yourself in" is your penalty may be significantly lower. The reduction, however, applies only to DOL penalties, not necessarily to IRS penalties. Informally, the IRS is willing to provide some penalty relief to plans that take advantage of the DFVC program.

More information on this program can be found at <http://www.dol.gov/ebsa/newsroom/0302factsheet.html>.

Conclusion

Although filing 5500s is not the most exciting topic for a Human Resource professional, it is a necessary evil. The process for filing is detailed but not overly complex and the penalties for not filing are substantial. Your organization will need to collect the various schedules and participant counts that need to be included with the Form 5500.

As a human resource professional, your plate may already be full. In that case, your organization can easily outsource the filing requirement to an accounting firm. If your organization chooses to use in-house resources, software is available to make the process easier.

Because penalties can be substantial, it is important to file annually and on time. If your organization has failed to file the report in the past, consider taking advantage of the DFVC program.

If you have any questions regarding the Form 5500, please contact your McGraw Wentworth Account Manager. If you have not already done so, be sure to put a reminder in your calendar to begin gathering Form 5500 data a couple of months before your filing deadline.

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