Which Common Plan Fees Can (& Should) We Pay From Plan Assets?

Facts

We are reviewing our company expense budget to identify any that we can eliminate or reduce. We've read that it is possible to pay expenses related to maintaining company retirement plans out of plan assets. We sponsor both a 401(k) plan and cash balance plan for our employees, so shifting some of those fees from the company to the plan would be great for our bottom line. Admittedly though, the more we read, it is less clear these rules become.

Question

Can you help us understand some of the most common plan maintenance expenses and which can be paid out of the plan?

Answer

This (or a variation of it) is a pretty common question we receive. When considering paying plan expenses from plan assets, there are really two over-arching questions – can you and should you? We'll run through a few scenarios below to shed some light on both.

Let's Start With "Can" You?

The general rule is that if a service is for the benefit of the plan, then the plan can pay the associated expense. However, if the service benefits the company, the company must pay for it. For a general reference on what can be paid from plan assets, check out a past Question of the Week here. And one more familiar note, the first place to check when it comes to options for paying fees from the plan is your plan document. The rest of our answer below assumes that, where possible, the document allows expenses to be paid from the plan.

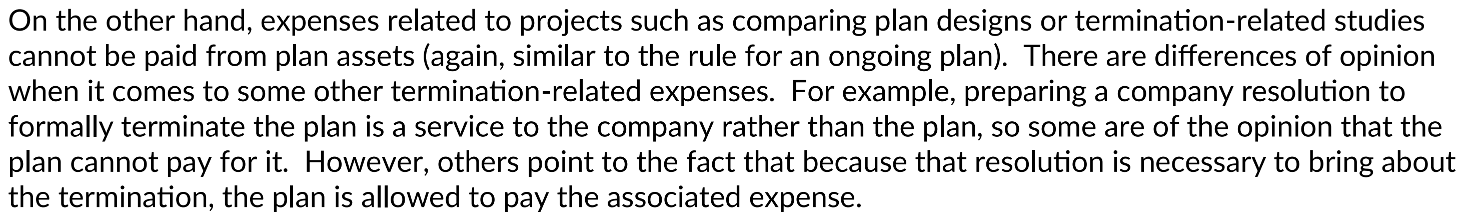
Plan Document Amendment/Restatement Fees

Whether or not this category of expenses can be paid from plan assets depends on the reason for the amendment or restatement. If an amendment/restatement is mandatory to update the document for changes in law, then the plan is allowed to cover the associated costs. Examples include amendments for the recently updated hardship distribution regulations and the Cycle 3 plan document restatements.

If, instead, the amendment is to make a voluntary change, e.g. to change eligibility from one year to six months, the plan cannot pay for it, and the company must cover the associated costs. Similarly, any type of projections or analyses to review the pros and cons of making changes are deemed to benefit the company (not the plan), so the company must pay for those expenses.

Plan Termination Fees

Similar to amendment/restatement fees, it's necessary to look at the specifics of termination-related expenses to determine if the plan is allowed to pay for them. Those related to "regular" services such as performing testing and preparing the 5500 for the final year can be paid from the plan just as they could be if the plan is ongoing.



On the other hand, expenses related to projects such as comparing plan designs or termination-related studies cannot be paid from plan assets (again, similar to the rule for an ongoing plan). There are differences of opinion when it comes to some other termination-related expenses. For example, preparing a company resolution to formally terminate the plan is a service to the company rather than the plan, so some are of the opinion that the plan cannot pay for it. However, others point to the fact that because that resolution is necessary to bring about the termination, the plan is allowed to pay the associated expense.

Expense Reimbursement Accounts

Many recordkeepers offer expense reimbursement accounts to hold dollars that would otherwise be paid as revenue sharing to service providers. This reimbursement account is then available for the plan sponsor to either pay plan-related expenses and/or have those funds allocated back to participant accounts as additional gains. Because the monies held in the expense reimbursement account are still plan assets, they are subject to the same plan versus company fee payment restrictions as other plan assets. That means these funds are available to pay for annual administration, qualified independent audits, required plan document amendments or restatements but not plan corrections, design studies, or discretionary plan amendments.

Cash Balance Fees

Cash balance plans (as well as all other defined benefit plans) provide participants with a specified benefit at retirement. When the actuary completes his/her calculation of a participant's benefit based on the plan document, the participant must receive that entire benefit amount. This benefit cannot be reduced for any distribution related fees. We've seen this sneak up when companies use a recordkeeper (similar to a 401(k) plan) to maintain their cash balance plans. While a plan sponsor may not pass along actuarial distribution fees to participants, the default for many recordkeepers is to charge their distribution fees to participants. Therefore, it's important to make sure this default is turned off to ensure any such fees are billed directly to the sponsor.

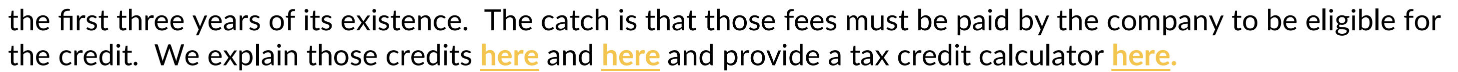
Sharing Fees Between Plans

Since you mentioned that you sponsor both a 401(k) and cash balance plan, its critical to make sure one plan does not pay any expenses associated with the other plan. For example, the 401(k) plan cannot pay cash balance expenses and vice versa. Similarly, you cannot use forfeiture or expense reimbursement accounts in your 401(k) to pay actuarial fees for the cash balance plan. If you work with the same service provider(s) for both plans and receive a consolidated invoice, it will be necessary to get a breakdown of the expenses that apply to each plan separately to ensure any fees paid by plan assets are accounted for correctly.

You "Can," but Should You?

With a better idea of the types of fees you can take from the plan, you're still left with the question of whether it makes sense to do so. Granted, what may make sense one year may differ the next, and we know that as a business owner, you're making these decisions with many other variables in mind. So, while we can't say whether you "should" pay expenses from the plan, we can offer a few things to consider as you make your decision.

One of the first considerations if you just started your plan in 2020 is whether there are any tax credits available. The SECURE Act increased tax credits for expenses associated with setting up and maintaining a new plan for



the first three years of its existence. The catch is that those fees must be paid by the company to be eligible for the credit. We explain those credits here and here and provide a tax credit calculator here.

Second, if the fee is being paid from participant accounts, it's most likely to be paid pro rata based on account balance. This means that the individuals with the largest balances pay a higher dollar amount than those with smaller balances. Typically, it is the business owner(s) who have the highest balances and, therefore, pay the highest amount of fees in this scenario. If this sounds like your situation, you may find it preferable to pay the expenses from the company and enjoy the additional tax deduction instead of having the funds come from your tax deferred retirement account.

Let's go back to another nuance for cash balance plans. Chances are, when you put that plan in place, the additional tax savings opportunities were a big driver. If you pay your plan expenses from the plan rather than from company funds, you lose out on the benefit of the potential tax deductions associated with those expenses. Moreover, because cash balance plans are required to satisfy certain funding requirements to maintain a minimum level of assets (in relation to promised benefits), reducing the assets to pay plan fees may create a larger funding obligation. In the end, this means you'll have to put more money in the plan to account for the money withdrawn for fees, so why not just pay those expenses from the company to begin with?

This plan expense grab bag can't cover all the potential expenses you might incur during the life of your plan. The facts and circumstances around a particular service or fee as well as your tax and financial situation at the time will play a major role in whether a fee *can* and *should* be paid from the plan. If you have a plan expense scenario you need to review, reach out to the DWC Team and we'll be glad to walk through it with you.

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