



Electronic Dispatch

# Employee Benefits Law Action Memo

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## U.S. DEPARTMENT OF LABOR PROPOSES A SAFE HARBOR FOR DEPOSITS TO SMALL PLANS

Recognizing that the rule on the timeliness of deposits of employee contributions to pension and welfare plans is often misunderstood and frequently violated, the Employee Benefits Security Administration (EBSA) of the U.S. Department of Labor recently proposed a safe-harbor rule for deposits to certain plans that are subject to the Employee Retirement Income Security Act (ERISA). Under the proposed safe harbor, employee contributions to a pension or welfare plan with fewer than 100 participants at the beginning of the plan year will be treated as made on a timely basis, if the contributions are transferred to the plan no later than the seventh business day following the date the amounts are withheld from pay (or within seven days of receipt by the employer, if a participant is making a direct payment, for example, by a personal check). The safe harbor would also apply to deposits of plan loan repayments to small plans (under 100 participants).

The new rules will not be effective until published in final form. However, EBSA has indicated that it will not assert a violation of ERISA for late deposits to small plans where contributions and loan repayments have been transferred in accordance with the proposed seven business day safe harbor.

### Requirement to Make Timely Deposits

If the proposed safe harbor does not apply (for example, for large plans, or for small plans that cannot comply with the seven business day rule), Department of Labor regulations specify that amounts that an employee has withheld from wages or otherwise pays to a pension or welfare plan become "plan assets" on the earliest date that the contributions can reasonably be segregated from the employer's general assets. Under this standard, if payroll can be processed and the participant contributions identified and withdrawn from the employer's assets on the business day immediately following payday, for example, then the contributions must be transferred to the plan on that same day. Unfortunately, employers who are particularly prompt with plan transmittals may find that their diligence penalizes them when they deviate from their usual timeliness, because they have set a high standard for when amounts "can reasonably be segregated." Anything later than customary practice may be deemed to be untimely and may expose the employer to sanctions (see below).

What makes this "as soon as possible" standard confusing is the portion of the regulation that provides that employee contributions to a pension plan must be transmitted to the plan not later than the 15<sup>th</sup> business day of the month following the month in which the contributions were received by the employer or withheld from pay (or, for a SIMPLE plan, not later than the 30<sup>th</sup> calendar day after the month the contributions were withheld from wages). Many employers view the 15<sup>th</sup> business day as the "due date" for deposits of employee contributions to pension plans. However, this rule is not a safe harbor; if contributions can be withdrawn from the employer's general assets earlier, a deposit on the 15<sup>th</sup> business day of the following month will be late.

Contributions to welfare plans, such as group health plans and life insurance, must be transferred to those plans not later than 90 days from the date received by the employer or withheld from pay. Again, this 90-day standard is not a safe harbor and is overridden by the "as soon as possible" rule.

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## Late Deposits are Prohibited Transactions

The consequence of failing to deposit employee contributions on a timely basis is that the contributions become "plan assets" while in the employer's possession. Generally, plan assets held by the employer are deemed to be a loan between the plan and a "party in interest," which is a prohibited transaction under ERISA. Late deposits must be disclosed on the Annual Return/Report on Form 5500. Prohibited transactions are subject to a 15% excise tax under Section 4975 of the Internal Revenue Code each year until corrected.

## Correcting a Late Deposit

There are two avenues for correction of late deposits: self-correction with payment of the excise tax, and EBSA's Voluntary Fiduciary Correction Program, under which the excise tax may be waived. In either event, the employer must transfer all the late contributions to the plan. In addition, any earnings lost (or profits gained by the employer by using the deposits for its own benefit) as a result of the late deposit must be restored to the plan and, if applicable, allocated to participants' accounts. Any penalties, late fees or similar charges must be paid by the employer, and may not be paid from participant contributions or the plan.

## Summary

The proposed seven-day safe harbor for deposits to small plans is welcome relief from a confusing requirement. EBSA indicates that it is open to extending the safe harbor to larger (100 or more participant) plans, if it receives compelling arguments during the comment period for the proposed regulations. In the meantime, employers and plan trustees should review the timeliness of deposits and take action to correct any delinquencies discovered.

If you have any questions about this memorandum, please contact Amelia M. Klein in our Albany office (518-533-3217; [aklein@bsk.com](mailto:aklein@bsk.com)) or any of the other members of our Employee Benefits Law Practice Group listed below:

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