MODERNIZING FORM 5500

In July of 2016, the Department of Labor (DOL), the Internal Revenue Service and the Pension Benefit Guarantee Corporation jointly released a set of proposed changes that will increase reporting requirements for nearly all retirement plans. Northern Trust is reviewing the proposal thoroughly with a view towards providing feedback to the agencies, and we encourage our plan sponsor clients to do the same.

OBJECTIVES

The agencies have laid out a series of objectives for the proposed rule changes.

- Modernize financial information reported by filers
- Improve data mineability for the regulators, plan sponsors, and third-party data collectors
- Expand reporting by all group health plans covered by Title I of ERISA
- Improve compliance and oversight through questions regarding plan operations, service provider relationships and financial management of the plans

Changes to Form 5500 were proposed in conjunction with the rebid for the ERISA Filing and Acceptance System (EFAST2) contract. The current contract runs through the 2018 filing year. EFAST2 is expected to begin processing the Plan Year 2019 Form 5500 Annual Return/Report beginning January 1, 2020. If adopted, the proposed changes would apply for plan years beginning on or after January 1, 2019.

OVERVIEW

The proposal to modernize Form 5500—which increases annual reporting requirements for nearly all retirement plans—is comprised of two documents that were published in the Federal Register on July 21, 2016, and a Technical Appendix that is available on the DOL's website.

- Proposed Regulations – ERISA Reporting and Disclosure
  - Proposed amendments to the DOL reporting regulations that conform to the proposed revisions to Form 5500 and Form 5500-SF
- Proposed Revision of Annual Information Return/Reports
  - Tri-agency proposal with 149 pages detailing 196 line item additions or revisions to Form 5500 and Form 5500-SF, including two new schedules and more than 20 new compliance questions
  - Appendix A: Data Elements for Forms and Schedules
  - Appendix B: Instructions for Form 5500
  - Appendix C: Instructions for Form 5500-SF
- Technical Appendix
  - Documentation of the Methodology Used to Calculate the Burden Associated with the Proposed Form 5500 21st Century Initiative

PROPOSAL COMMENTS

The proposed changes represent a major overhaul of annual reporting requirements, and the DOL is very interested to hear feedback and comments from stakeholders, providers and filers. The proposal comment period runs through December 5, 2016. The DOL is seeking feedback on a number of fronts, including:

- Data Elements: Are the definitions, categorizations and data fields—such as hard-to-value assets (HVA) or hedge funds—adequately delineated, meaningful and readily available?
- Costs: The costs and burdens to plans, participants and beneficiaries, plan fiduciaries, plan service providers, and other affected parties
- Alternatives: Comments and suggestions about alternative solutions, and whether and how such alternatives would be more or less beneficial compared to the proposed changes to the forms, schedules and instructions
- Additional comments on the existing forms, schedules and clarity of instructions that the Agencies have not proposed changing, but which may benefit from further guidance, especially with regard to how an

Plan sponsors are encouraged to provide feedback on the proposed changes through:

- Federal eRulemaking Portal: http://www.regulations.gov
- Email: e-ORI@dol.gov (Include "RIN 1210–AB63" in the subject line)

All comments will be made available to the public online and made available for public inspection.

existing provision or instruction would apply for a particular segment of the filing population

NEXT STEPS: PROVIDE FEEDBACK

Northern Trust is working with industry peers to comment on a number of these changes. We will focus on plan investments and other activities that relate to custodial records. We encourage plan sponsors to talk to their other service providers—record keepers, third-party administrators, etc.—to learn what challenges they are concerned about.

Further, we encourage plan sponsors to work with their industry peers to muster a strong, collaborative and well-supported response to the DOL's proposal, especially aspects of the proposal related to plan design and administration.

TOP 10 SCHEDULE MODIFICATIONS

Northern Trust has a team of specialists reviewing various aspects of the proposed changes and is working with industry groups to fully understand the impacts. Below are the top 10 schedule modifications affecting plan filers.

SCHEDULE C: SERVICE PROVIDER FEES

- Rewritten to align with service provider disclosures under ERISA 408(b)(2), regardless of the plan size
- A separate Schedule C is required for each service provider
- Requires service codes for all providers, regardless of direct and indirect compensation; service provider contact information (name, phone number and address), new codes to identify the provider's relationship to the plan, and codes to identify the type of fee or compensation arrangement
- Indirect Compensation
  - Eliminates the eligible indirect compensation distinction
  - Requires an estimated dollar amount for indirect compensation; eliminates the option to provide a formula
  - Provides flexibility to use a reasonable method for allocating indirect fees
- Additional questions such as:
  - Was an ERISA recapture or ERISA budget account used?
  - Did any service arrangements (e.g., recordkeeping) involve any "related party compensation"?

  - The existing Schedule C question regarding termination of actuaries and accountants was moved to Schedule H and expanded to cover termination of other service providers.

- The new breakdown of fees charged to participant accounts can now be found in Schedule H, Part II: Income and Expense Statement

SCHEDULE D: DIRECT FILING ENTITY (DFE) AND PARTICIPATING PLAN INFORMATION

- The information in Schedule D, Part I has been moved to the Schedule of Assets Held for Investment at End of Year
- Investments in Master Trusts
  - Plans must show their proportionate interest in each holding of the master trust in the new Schedule of Assets Held section
  - Eliminates master trust investment account (MTIA) reporting for plans
  - Master trust DFE filing is still required
- Common/Collective Trust (CCT) and Pooled Separate Account (PSA)
  - Underlying investments of CCTs and PSAs, which have been provided only to plan fiduciaries, are now part of the annual return/report data set, and will be filed either by the participating plans, the CCT or the PSA
  - CCTs and PSAs are required to file Form 5500 with the Schedule of Assets Held in order to provide participating plans/trusts relief from having to disclose underlying assets of the DFE
  - The current requirement to break out the assets of non-filing CCTs or PSAs remains in place

SCHEDULE E: EMPLOYEE STOCK OWNERSHIP PLAN (ESOP)

- Reintroduced as part of the proposed changes; used to gather information about ESOPs and provide information of interest to both the DOL and IRS
- Allows for all ESOP questions to appear on a single schedule
- Revised and new questions cover the following:
  - How was the ESOP stock acquired (i.e., securities acquisition loans)?
  - Is the stock readily tradable on an established securities market? If not, was an independent appraiser used?
  - What was the original amount and interest rate of any outstanding securities acquisition loan? Was any loan refinanced?
  - Did the ESOP hold preferred shares, and if so what is the method of conversion from preferred to common shares?
  - Is the ESOP maintained by an S corporation? If so, are there any disqualified persons?

SCHEDULE G: FINANCIAL TRANSACTION SCHEDULES

- Requires a breakdown of fixed-income obligations that are in default or uncollectible by sub-categories including, bonds, options, swaps, futures or forward contracts
- For defaulted instruments, plan filers must indicate whether the security interest was perfected
- Requires a description of steps taken, or to be taken, by the administrator to collect overdue amounts included in the schedule, rather than as an attachment
- For non-exempt transactions, filers must indicate whether the event was a one-time transaction or an ongoing engagement, and whether the transaction has been fully corrected

SCHEDULE H, PART I: ASSET AND LIABILITY STATEMENT

- The goal of modifying Schedule H is to improve data mineability and transparency, and reduce the “Other” category through the introduction of a structured data format and more granular asset categories, including:
- Fixed Income
  - “Investment Grade vs. High Yield,” replaces “Preferred and Other” (consistent with Schedule R for Large Pension Plans)
  - There are new categories for exchange-traded notes, asset-backed securities and foreign debt
  - Foreign government bonds moved from “Other” to a designated line for non-U.S. Government Securities
- Foreign investments
  - There are new categories for foreign equities, including American depositary receipts
  - Foreign investments, including ADRs, are mapped to a designated line
- Equities
  - Common and preferred stocks are now differentiated by publicly traded vs. non-publicly traded
    - Foreign government bonds moved from “Other” to a designated line for non-U.S. government securities
    - Other foreign investments, including real estate and currencies
- Partnerships and Joint Ventures
  - Includes new breakouts: Limited partnerships, venture capital operating companies, private equity and hedge funds
  - Comments are specifically requested about whether hedge funds and private equity are sufficiently defined

- Real Estate
  - Includes new breakouts: Developed real property, undeveloped real property, real estate investment trust (publicly vs. non-publicly traded), mortgage-backed securities, centralized mortgage obligations, real estate operating companies
- Insurance General Accounts
  - Expanded to include: Depository administration (DA), immediate participation guarantee (IPG), guaranteed investment contract (GIC)
  - Comments are specifically requested about whether more insurance categories are needed (e.g., variable annuity contracts)
- Derivatives
  - A new category has been established that requires further breakout by futures, forwards, options and swaps
- Self-directed Brokerage Accounts
  - There are separate subtotals for brokerage account investments in tangible personal property, loans, partnership or joint venture interests, real property, employer securities, and investments that could result in a loss in excess of the account balance of the participant or beneficiary who directed the transaction.
- Schedule H Attachments: Lines 4i(1) and 4i(2)
  - Schedule of Assets Held: Line 4i(1)
    - Security identifiers, such as Committee on Uniform Securities Identification Procedures (CUSIP), legal entity identifier (LEI) and financial instrument global identifier (FIGI), are now required
    - There is a new check box for HVA
    - DEFs with HVAs must be flagged as such
  - Schedule of Assets Sold: Line 4i(2)
    - Replaces the former Schedule of Assets Acquired and Disposed of During the Plan Year
    - Filers must now list all assets sold during the year (except those currently excluded), not just those acquired and also sold within the year
    - There is a new check box to identify investments that involve parties in interest and HVA
    - Filers need to add identifiers such as CUSIPs, central index keys (CIKs) and LEIs for each asset

SCHEDULE H, PART II: INCOME AND EXPENSE STATEMENT

- New administrative expense categories include:
  - Salaries

  - Independent qualified public accountant audit fees
  - Record keeping and other accounting fees
  - Trustee and custodial fees
  - Actuarial fees
  - Legal fees
  - Valuation/appraisal fees
  - Trustee fees and expenses (e.g., travel, seminars, meetings)

- New breakouts for participant-level vs. plan-level charges:
  - Total paid by the plan, except charges directly against participant accounts
  - Total payments charged directly against participant accounts
  - Transaction-based charges to individual participant accounts
  - Plan-level expenses apportioned among participant accounts
  - Plan filers must indicate how expenses are apportioned (i.e. per capita, pro rata by account balance or other)

- New earnings categories include:
  - Partnership/joint venture
  - Commodities
  - Derivatives
  - Employer securities
  - Foreign investments
  - Employer real property

SCHEDULE H, PART III: ACCOUNTANT'S OPINION

- Expanded questions about IQPA engagement
- Plan filers must identify the state in which the opinion was issued
- Asks whether the plan filer reviewed and discussed the IQPA report with the accountant
- Asks whether the accountant advised the plan filer about the IQPA report, including the financial statements and/or notes, or whether IQPA's communications with those who are charged with governance, disclosed any of the following:
  - Errors or irregularities
  - Illegal acts
  - Material internal control weaknesses
  - A loss contingency indicating assets are impaired or a liability incurred
  - That the plan sponsor may not be a going concern
  - The existence of plan qualification issues pursuant to the Internal Revenue Code
  - Any unusual or infrequent events or transactions occurring subsequent to the plan year end that might significantly affect the

  - usefulness of the financial statements in assessing the plan's present or future ability to pay benefits

- Asks whether the IQPA had a peer review performed in accordance with their state's requirements
  - If yes, provide name of the peer reviewer, the year of their last peer review and rating received, the number of years that peer reviewer has been the firm's peer reviewer, and whether the peer review covered employee benefit plans

SCHEDULE H, PART III AND IV: COMPLIANCE QUESTIONS

- Now contains more than two dozen new compliance questions
- Compliance questions are related to auditor signoffs, trustee certifications, plan design questions around participation rates, matching, etc., and plan mergers, terminations and consolidations
- Examples of the new compliance questions include:
  - Did the plan trust incur unrelated business taxable income?
  - Were all plan assets valued at least annually at fair market value?
  - Did any employer sponsoring the plan pay any of the administrative expenses of the plan that were not reported on Schedule H, Line 2i?
  - Did any person who is disqualified under ERISA Section 411 serve, or was permitted to serve, the plan in any capacity?
  - Were there any checks to participants or beneficiaries that were uncashed as of the end of the plan year? If so, describe efforts to monitor uncashed checks and to locate missing recipients.

SCHEDULE J: GROUP HEALTH PLAN INFORMATION

- Schedule J is a new schedule that was added to capture information about group health insurance plans, regardless of size or funding status (trust or unfunded)
  - Plans with fewer than 100 participants are required to file
  - Contains new plan design and compliance questions related to the following topics:
    - Consolidated Omnibus Budget Reconciliation Act (COBRA), health savings account (HSA), flexible spending account (FSA) or health reimbursement arrangement (HRA)
    - Service providers, including third-party administrators, pharmacy and mental health benefit managers, and independent review organizations
    - Stop loss

- Content compliance of summary plan description (SPD), summary of material modification (SMM) and summary of benefits and coverage (SBC)
- Assets held in trust by a qualified insurance company
- Whether the plan claims grandfathered status under health care reform or whether it is a high-deductible health plan, HRA or FSA
- Whether the plan sponsor received reimbursements, refunds or rebates from service providers
- Information regarding claims payments such as number of approvals and denials, including pre-service claims
- Any failures to pay claims during the year (carrier delinquencies)

SCHEDULE MB: MULTIEMPLOYER DEFINED BENEFIT PLAN & CERTAIN MONEY PURCHASE PLAN ACTUARIAL INFORMATION

- Provides more transparency to multiemployer plans and new data formatting requirements
- The instructions were modified to add RP-2000 and RP-2000 (with Blue Collar Adjustment) to the list of mortality tables for non-disabled lives that plans may report in Line 6c
- A new question has been added in Line 8b that requires large multiemployer plans (500 or more total participants as of the valuation date) to provide, in an attachment, a projection of expected benefit payments to be paid for the entire plan (not including expected expenses) for each of the next 10 plan years, starting with the plan year to which the filing relates
- All multiemployer plans are required to report the funded percentage for monitoring the plan’s status in Line 4
  - Previously, only plans in critical or endangered status were required to report this information
- As a result of the Multiemployer Pension Reform Act of 2014, Schedule MB and instructions are further modified to extend the reporting requirements in Line 4 for multiemployer plans in critical status and plans in critical and declining status, and require that additional information must be reported by plans that have been partitioned or have had benefits suspended.

NEW REQUIREMENTS FOR FILERS AND CERTIFYING ENTITIES

In addition to the 10 Schedule amendments listed above, the DOL also proposed changes surrounding limited scope audit engagements. Below is a description of the new requirements for filers and certifying entities.

- A new question was added to Schedule H, Part III: Accountant's Opinion. This question encourages plan administrators to obtain documentation consistent with the limited scope audit requirements. EBSA intends to "improve the quality of its audit documentation reviews by adding procedures to ensure that all plan assets are either certified by a qualifying financial institution or tested by the IQPA."
  - Did the IQPA perform a limited scope audit?
    - If "yes," attach a copy of the certification(s)
    - Do not attach an itemized list of certified assets
- Requirements of the certifying entity are amended as follows:
  - Provide a separate certification page
  - Describe the manner in which assets are held
  - If "current value" is not being certified for all assets, the assets for which current value is being certified must be separately identified and the certification must include a caution that the certification is not certifying current value information and stating the asset values provided may not be suitable to satisfy the plan's reporting obligations must be included
  - If certification is provided by an agent on behalf of a bank or insurance company, the certification must include a statement that the certifying agent is authorized to issue the certification and the bank or insurance company is taking responsibility for the accuracy and completeness of the certification and the underlying records

NEXT STEPS: PROVIDE FEEDBACK

Northern Trust is working with industry peers to provide comments on a number of these changes, which will focus on plan investments and other activities that are part of custodial records. We encourage plan sponsors to talk to their other service providers—record keepers, third-party administrators, etc.—to learn what challenges they are concerned about, and encourages clients to work with industry peers to muster a strong, collaborative and well-supported response to the DOL's proposal, including aspects of the proposal related to plan design and administration. Northern Trust's comments to this proposal will focus on plan investments and other activity that are part of custodial records.

Contact Northern Trust to Learn More

To learn more about Form 5500 or Northern Trust's relationship management services, contact your Northern Trust relationship manager, or visit northerntrust.com.