



FIVE TIPS FOR ERISA COMPLIANCE

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Employee Retirement Income Security Act (ERISA) sets minimum standards for establishing, administering, amending and terminating pension benefit plans and welfare benefit plans maintained by most private sector employers. ERISA generally covers retirement income; deferred compensation; medical, sickness and vacation benefits; scholarship funds; and apprenticeships or training programs.

The statute, and supporting case law, can be daunting, but the following five tips follow recent trends we have seen to help you remain compliant.

Tip One: Employer's Response to Overfunded/Underfunded Employee 401(k) Accounts

Retirement plan sponsors need to periodically audit their 401(k) plans. One of the biggest issues we have seen lately is an employer's discovery that an employee's 401(k) account has been over- or underfunded.

Underfunded Employee Accounts

In situations where an employee's retirement account is underfunded, the employer should reallocate the balance for the missing period. There is no tax liability for the underfunding, but there is risk that an employee otherwise paid taxes on money that should have been sheltered in their 401(k).

Overfunded Employee Accounts

In situations where an employee's 401(k) fund has been overfunded, an employee will face a 6% penalty for the overfunded amount. This can be avoided if the employer recovers and redistributes that money before April 15 of the tax year the fund was misallocated. If discovery is made after April 15, then the overfunded portion will need to be retracted, which includes the amounts earned on the excess funding for the calendar year. This should be done immediately to help the employee avoid double taxation,

whereby they get taxed on the overfunded portion now, and when they withdraw the funds or otherwise receive a distribution. If possible, the overfunded amount can be allocated to the employee's account to the following year.

Employer response

In both scenarios, employer will need to issue amended W-2 forms. Likewise, the 401(k) plan will need to file an amended return to reflect the proper participant allocation.

Finally, even if the overfunding/underfunding issue occurs by the fault of a third-party administrator, the tax and penalty liability will flow to the employer as the benefit plan sponsor. However, the employer should examine whether its third-party administrator has an obligation to indemnify the employer in such situations.

Tip Two: Ensure Your Fund Manager's Actions are Without Self-interest.

ERISA requires benefit plan administrators to manage financial investments as a reasonably prudent business professional, balancing manageable risk with protection of plan assets, without self interest. This is generally accomplished by investing in established investments and investment vehicles with a trusted history of performance.

Commonly, benefit plan managers will outsource fund management to a non-party investment manager and delegate proxy voting authority. Recent trends have raised concern that outsourced benefit plan managers are not always acting without interest, including investing in funds they will benefit from.

To avoid this concern, benefit plan managers should:

- When selecting a manager – conduct a thorough review of a manager's voting record prior to their selection.
- For current managers – confirm they are exercising financial prudence in managing plan assets through arm's length transactions; exercising the highest duty of loyalty to the plan and its participants; and managing assets without any undue influence or conflict of interest.
- Consider – passing the voting responsibilities directly to plan participants and their beneficiaries.

Tip Three: Handing of Non-vested Employee Benefits

There has been an uptick in litigation attacking an employer's use of 401(k) forfeitures to offset employer contributions. Often times, employers will use non-vested amounts from employees who leave before fully vesting toward employer contribution requirements. This can be seen as a form of self-dealing and a violation of the fiduciary requirements in managing a 401(k) plan. Especially when an employee is making a termination decision and chooses one employee over the other to avoid full vesting – and thus free funds to allow for contribution toward the employer's requirements.

Tips Four and Five: Medical Plan Considerations

Coverage Decisions for Medicare-Eligible Workers

Employers may not reduce, carve out or eliminate benefits to their Medicare/Medicaid eligible employees. This includes encouraging employees that are Medicare/Medicaid eligible to opt out of the employer-provided health care plan to transfer to Medicare/Medicaid or a specific bridge to obtain such care. This conduct can be found to violate the ADEA and ADA.

Coverage Decisions when an Employee has Overly High Medical Expenses

Employers cannot create a separate insurance plan, or carve out, when an employee has overly high medical expenses. When presented with an employee with individual needs, or family needs, for care that exceeds the needs of other employees, employers must still treat this individual equally, providing the same level of care under the employer's medical plan. Treating an employee differently for the employee's elevated needs can also be found to violate the ADA.

In sum, ERISA can be complex to navigate, especially considering its scope covering many forms of employee benefits. Stay tuned for additional guidance from Bell Nunnally's ERISA compliance team.

Related Practices

Labor and Employment

Practice Area Contact

Sydney A. Shimkus