

Compliance Update for Tax-Qualified Retirement Plans

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This Client Alert describes upcoming key deadlines and actions that must be taken by plan sponsors of tax-qualified retirement plans by the end of 2009 or beginning of 2010. In particular, many plan sponsors that maintain qualified plans must adopt certain amendments to comply with the Pension Protection Act by December 31, 2009. In addition, plan sponsors should ensure compliance with recent regulations and guidance on plan disclosures that apply to all qualified plans. These and other issues are described in more detail below.

Plan Amendments

PPA/WRERA – Amendments Required by 12/31/09

The Pension Protection Act of 2006 (“PPA”) and Worker, Retiree, and Employer Recovery Act of 2008 (“WRERA”) made numerous changes to the rules governing tax-qualified defined benefit and defined contribution plans. Plan sponsors of calendar-year plans must adopt the required amendments by December 31, 2009. Some of the required amendments include more rapid vesting for employer nonelective contributions under defined contributions plans, and a 75% “qualified optional survivor annuity,” funding-based restrictions, and revised assumptions for calculating the present value of accrued benefits under defined benefit plans. Sponsors of calendar-year plans that wish to implement certain optional features – such as expanded hardship distribution provisions and new automatic enrollment safe harbors – should also adopt these amendments by the end of this year.

HEART Act and Other Laws Affecting Participants in Military Service

The Heroes Earnings Assistance and Relief Tax Act of 2008 (“HEART Act”) requires retirement plans to provide certain survivor benefits (other than benefit accruals) on behalf of participants who die during active military duty. In addition, it provides plans with the option to provide benefit accruals on behalf of participants who die or become disabled during active duty. It also requires that differential pay to employees in the military be treated as compensation for all purposes under the terms of the plan.

In addition, a new PBGC regulation, effective December 17, 2009, amends the rules for terminating single-employer defined benefit plans with respect to participants who are serving in the military. Under USERRA, a plan participant who leaves employment for military service is generally entitled to benefits that he or she would have accrued as of the date of re-employment. Under the new rule, the

PBGC will treat the benefits of a participant who returns to employment within the USERRA-provided timeframes but after the plan's termination date as guaranteed through the plan's termination date.

Required Minimum Distributions Suspended in 2009

The WRERA provides that the required minimum distribution rules do not apply to defined contribution plans for 2009. The IRS has issued guidance on the suspension of these rules, including model amendments. These amendments give plan participants the option of consenting to receive a distribution or to waive a required minimum distribution for 2009, depending on which default rule the plan sponsor chooses to adopt. They also provide options for the treatment of these distributions as eligible rollover distributions. While plan sponsors have until the end of 2011 plan year to adopt the necessary amendments, plans must be operationally compliant with those amendments now.

Determination Letter Applications

Individually designed plans in "Cycle D" (generally, plans maintained by sponsors with an EIN ending in a "4" or "9" and multi-employer plans) may be submitted for determination letter applications by January 31, 2010. The filing deadline is extended for plans with a plan year ending after January 31, 2010.

For employers that adopt volume submitter and prototype defined contribution plans that are preapproved by the IRS, the deadline for adopting an amended and restated plan and, if necessary, filing an EGTRRA determination letter application, is April 30, 2010. The IRS has indicated that it will soon announce a deadline for adopting preapproved defined benefits plans and filing determination letter applications. To prepare for these applications, the IRS will temporarily stop accepting Form 5307 applications for preapproved defined benefit plans as of February 22, 2010.

Plan Notices

Eligible Rollover Distributions

The IRS recently issued new model "safe harbor" explanations that may be provided to recipients of eligible rollover distributions in order to satisfy Section 402(f) of the Code. Plan administrators who wish to continue to rely on the IRS safe harbor explanation must update their notices in accordance with the new model by no later than December 31, 2009. Notice 2009-68 reorganizes and simplifies the model safe harbor notice issued by the IRS in 2002, and also updates the earlier notice to reflect changes in the law since then. For example, the updated notices describe rollovers to Roth IRAs (that may be made without regard to the limits on modified AGI as of January 1, 2010), rollovers to non-spouse beneficiaries, and the elimination of the early withdrawal penalty tax on "qualified reservist distributions." In addition, Notice 2009-68 contains two model explanations: one that is designed for a distribution from a designated Roth account, and one that is not.

Benefit Statements

Under the PPA, effective for plan years beginning after December 31, 2006, defined benefit plans must automatically provide benefit statements to vested, active participants once every three years. For calendar-year plans, the first of these notices is due on or before December 31, 2009. Alternatively, defined benefit plans may satisfy this requirement by notifying participants at least annually how to obtain the information. Defined contribution plans must provide benefit statements to plan participants within 45 days of the end of each calendar year quarter.

Right to Defer Distribution

The PPA requires plans to inform participants of their right to defer distribution of retirement plan benefits if the benefit exceeds \$5,000. Plan sponsors are required to make a reasonable attempt to comply with this requirement. The IRS has recently issued proposed regulations and sample safe harbor language to comply with this notice requirement. Until final regulations are issued, plan sponsors should continue good-faith compliance.

Mutual Fund Prospectuses

Under new DOL guidance, plan fiduciaries may satisfy the disclosure requirements under Section 404(c) of ERISA by providing participants with a mutual fund's summary prospectus rather than full prospectus. Section 404(c) states that a plan fiduciary may be relieved of ERISA liability for any losses that are the direct and necessary result of investment instructions given by a participant. To qualify for this protection, a plan that offers mutual fund investments must provide participants with a copy of the most recent mutual fund prospectus provided to the plan. The DOL previously confirmed that this requirement was satisfied by the delivery of a profile prospectus, but early in 2009 the SEC issued rules that replaced the profile prospectus with a "summary prospectus." DOL Field Assistance Bulletin 2009-03 confirmed that disclosure of a summary prospectus will continue to satisfy the 404(c) disclosure requirements. Since a summary prospectus provides information about a mutual fund in simplified form, the DOL's guidance will hopefully facilitate employers' ability to satisfy Section 404(c) and plan participants' ability to understand their investment options.

ERISA § 204(h) Notices

The IRS has issued final regulations, effective November 24, 2009, on the application of the ERISA Section 204(h) notice requirements to amendments that significantly reduce the rate of future benefit accruals. ERISA Section 204(h) and Code Section 4980F impose an excise tax on plan administrators that fail to notify affected parties at least 45 days in advance of the amendment for most single-employer plans, and at least 15 days for small single-employer plans and multi-employer plans. The final regulations provide special timing rules for notifying participants of amendments that are retroactively effective, add amendments that eliminate retirement-type subsidies or early retirement subsidies to the list of 204(h) events, and provide that a defined benefit plan is not required to provide a 204(h) notice for an amendment that (pursuant to the PPA) changes the applicable interest or mortality assumptions in Code Section 417(e)(3).

Annual Funding Notices

Annual funding notices for defined benefit plans must be sent within 120 days of the end of the plan year (small plans, with 100 or fewer participants, must file their funding notice at the time of the annual report). The annual funding notice must contain detailed information on plan funding and be sent to the PBGC, plan participants, unions, and contributing employers. DOL Field Assistance Bulletin 2009-01 provides guidance on these requirements as well as model funding notices.

Other Issues

Automatic Enrollment

IRS Revenue Ruling 2009-30 allows plan sponsors to automatically increase participants' default contribution rate each year at the same time they receive a midyear pay increase. In certain

circumstances, the amount of the increase may even be determined with reference to the size of a participant's pay raise. The IRS also issued Notice 2009-65, which provides two sample amendments that 401(k) plan sponsors can use to add automatic enrollment features to their plans: one provides for a basic automatic contribution arrangement, while the other provides an eligible automatic contribution arrangement ("EACA") that allows participants to opt out of automatic enrollment and withdraw their automatic contributions within 90 days of enrollment.

Defined Benefit Plan Funding

The IRS issued final regulations governing defined benefit plan funding and benefit restrictions. The regulations provide new requirements governing minimum defined benefit funding standards and limitations on pension benefits for single-employer plans that are generally effective for 2010. The regulations specify how to calculate a plan's funding target (the present value of benefits accrued or earned under the plan as of the beginning of the plan year) and target normal cost (the present value of benefits expected to accrue or be earned under the plan during the plan year). The regulations also provide automatic approval to select new interest rates used for certifying the funding targets for defined benefit plans for a plan year beginning in 2010. They also allow plan sponsors to modify certain funding elections made with respect to the 2008 plan year. Plan sponsors should consult their actuaries regarding these and other aspects of the regulations.

Paid Time Off

The IRS has issued guidance for allowing an employee's unused paid time off (e.g., vacation or sick pay) to be converted into a nonelective profit sharing contributions, or to allow participants to make elective deferrals on these amounts. The guidance addresses two general scenarios: contributions of unused paid time off that would otherwise be forfeited at the end of the year, and contributions of paid time off that would otherwise be distributed to participants upon termination of employment.



If you have any questions concerning these developing issues, please do not hesitate to contact any of the following members of the Paul Hastings ERISA and Global Benefits practice:

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