

# Employee Benefit News

January 30, 2009

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## COMING IN 2009

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- All non-government plans (including individually designed, prototype, defined benefit, defined contribution, and 403(b) plans) will need to be amended in the 2009 plan year for PPA. (Government plans will need to be amended in 2011.)
- An individually-designed plan with an EIN ending in 4 or 9 and all multiemployer plans need to be restated and submitted to the Internal Revenue Service by January 31, 2010.
- For the first time, all defined benefit plans are required to issue annual benefit statements to participants. Defined contribution plans with participant directed investments will continue to provide participant statements on a quarterly basis.
- Calendar year defined benefit plans will want to watch for certifications of the 2009 adjusted funding target percentage in March. Recall, if the adjusted funding target percentage is less than 80%, there will be restrictions on the payment of benefits.

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## FIDELITY BONDS

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In general, every fiduciary of an employee benefit plan is required to be covered by a fidelity bond. The purpose of the bonding requirement is to protect employee benefit plans from risk of loss due to fraud or dishonesty. The amount of the bond must be at least 10% of the plan assets. The Department of Labor has issued guidance on the bonding requirements in Field Assistance Bulletin No. 2008-04. You may access a copy of it at <http://www.dol.gov/ebsa/regs/fab2008-4.html>.

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## FEE DISCLOSURE UPDATE

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Our October newsletter contained a detailed article on the Department of Labor's three prong approach to fee disclosures. At that time, proposed regulations had been issued regarding fee disclosures by service providers to employers and fee disclosures by employers to participants. Most in the retirement plan community expected final regulations to be issued before the end of 2008. However, that time has come and gone, and there are no final regulations. At this point the fate of these regulations is unclear. They could still be issued in substantially the same form as proposed, they may be altered by imposing additional disclosure requirements, or Congress may preempt them by passing laws on the issue. The only thing that seems certain is that the proposed regulations will serve as a base regarding fee disclosure. Whatever final form they take, they will not have less disclosure requirements than the original proposals. Please review the October article if you would like more details on the proposals. McCready and Keene will continue to monitor developments in this area and will assist our clients in keeping their plans in compliance.

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## REMINDER

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A reduction in force may be an unfortunate consequence of this uncertain economy. Reducing the number of participants could result in a partial plan termination. Whether a partial plan termination has occurred is based on a facts and circumstances test. In general, if 20% or more of the participants in a qualified plan are terminated, there is deemed to be a partial plan termination. The consequence of a partial plan termination is 100% vesting for the terminated participants. Please let us know if you think you may have a potential plan termination, and we can assist you with the analysis.





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## WORKER, RETIREE, AND EMPLOYER RECOVERY ACT

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On December 23, 2008, President Bush signed the Worker, Retiree and Employer Recovery Act of 2008 ("Recovery Act") into law. The law provides some relief for individuals and plan sponsors to help them cope with the economic downturn, but not as much relief as was hoped. The American Benefits Council and other groups are continuing to lobby for additional relief for defined benefit funding requirements and benefit restrictions. The Recovery Act also includes technical corrections to the Pension Protection Act of 2006 ("PPA").

### **Defined Benefit Plans**

#### *Transition to new funding rules*

**PPA:** The funding target is increased from 90% to 100% of current liability. If the value of plan assets reduced by the credit balance is less than the funding target, the shortfall is amortized over 7 years. In a given year, the employer is required to fund the current year's amortized shortfall and the entire normal cost for the current year. Under PPA, plan expenses were not added to the target normal cost. In determining whether a shortfall has to be amortized, the 100% target is phased-in as follows: 2008 target – 92%; 2009 target – 94%; 2010 target – 96%; 2011 target – 100%. Under PPA, if a plan missed its funding target in any phase-in year, the target automatically increased to 100%. (For example, a plan that was only 90% funded as of 1/1/2009 would have to amortize the shortfall from 90% to 100% in 2009 and would have to continue to do so in 2010 even if they were over 96% funded.)

**Recovery Act:** The phase-in rule is modified to allow plans that miss their funding target in any year to retain the transition target instead of jumping to 100%. This adjustment applies for 2008, 2009, and 2010. (For example, a plan that was only 90% funded as of 1/1/2009 would only have to amortize the shortfall from 90% to 94% in 2009 but would be exempt from the amortization payment in 2010 if they were at least 96% funded.) Also, the PPA technical corrections clarified that anticipated plan expenses are to be added to the target normal cost and anticipated employee contributions are to be subtracted.

#### *Smoothing of Assets*

**PPA:** Up to a 24-month period may be used to average asset values. However, the final averaged value must be in the range of 90-110% of market value as of the plan's valuation date. When determining the values to be averaged from 12 months or 24 months earlier, only contributions, benefits, and plan expenses were included.

**Recovery Act:** Plans are permitted to "smooth" the value of their pension plan assets over a period not to exceed 24 months instead of using an averaging method. Smoothing allows the plan to take anticipated earnings into account in addition to contributions, benefits, and expenses. The change is intended to soften the impact of investment losses. However, the requirement that a smoothed asset would have to fall within 90-110% of the fair market value of assets still applies. For 2009, the smoothed value of assets for many plans will be above the 110% upper limit, which means this provision may not provide any relief for those plans in 2009. Another obstacle is that PPA does not allow employers to change their asset method from year to year, and the Recovery Act did not make an exception for 2009.

#### *Restriction on Benefit Accruals and Accelerated Payment Options*

**PPA:** Only half of the payment of lump sum benefits, installments, social security levelers, or the purchase price of an annuity may be made for plans at least 60% but less than 80% funded. Plans funded less than 60% may not make any payments in the form of a lump sum, installment, social security leveler or purchase of an annuity contract. In addition, benefit accruals are frozen if the plan is funded less than 60%.

**Recovery Act:** With respect to the restriction on benefit accruals, plans may look back to the previous plan year to determine their funded status. This modification is effective for the plan year beginning during the period October 1, 2008, through September 30, 2009. The restrictions on payment of benefits for plans less than 80% funded and for plans less than 60% funded continue to apply.



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## WORKER, RETIREE, AND EMPLOYER RECOVERY ACT (CONTINUED)

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### *Small Benefit Cash-Outs Not Restricted*

PPA: As indicated above, payment of lump sums is restricted if the plan is less than 80% funded.

Recovery Act: Effective for plan years beginning after December 31, 2007, payment of small benefits that are involuntarily cashed out is not restricted. Regardless of the funding status, a plan must pay small benefit cash-outs pursuant to the provisions of the plan.

### *415 Limits*

Recovery Act: The mortality tables used for benefit limitation calculations under Section 415 of the Internal Revenue Code are changed from the 1994 Group Annuity Table to the applicable mortality table described under Section 417 of the Internal Revenue Code for purposes of calculating lump sum distributions. It is anticipated that this change will have a minimal effect on the 415 dollar limit. This change in the Recovery Act is not a revision to PPA.

### *Multiemployer Plans*

PPA: There are additional funding rules on multiemployer defined benefit plans that are in endangered or critical status. If a plan is in endangered status, it must have a funding improvement plan. If a plan is in critical status, it must have a rehabilitation plan. The funding improvement plan and the rehabilitation plan are generally effective for 10 years, unless the plan emerges from critical or endangered status.

Recovery Act: For plan years beginning during the period October 1, 2008 through September 30, 2009, the sponsor of a multiemployer plan may elect to treat its status the same as its status for the prior year. In addition, the sponsor of a multiemployer plan may elect for a plan year beginning in 2008 or 2009 to extend the funding improvement or rehabilitation period by 3 years.

### **Defined Contribution Plans (including 403(b) plans and 457 plans)**

#### *Required Minimum Distributions Waived for 2009*

Current Requirements: Generally speaking, required minimum distributions must be made by April 1 of the calendar year following the year the participant attains age 70½. For participants who are not 5% owners, the plan may be written to extend the initial distribution date to the April 1 following the later of the calendar year in which the participant attains age 70½ or retires. There are also time limits for distributing death benefits. One option is to allow beneficiaries to take distribution by the December 31<sup>st</sup> of the calendar year containing the 5<sup>th</sup> anniversary of death (known as the 5-year rule).

Recovery Act: Required distributions for 2009 are not required, including those required to be made by April 1, 2010, because a participant attained age 70½ in 2009. Please note that distributions due by April 1, 2009 for 2008 are still required. Plans may allow participants who would have had a required distribution for 2009 to take it in cash, roll it over (unless the distribution is an installment payment that does not qualify for rollover), or leave it in the plan. If the distribution is taken in cash for 2009, the 20% mandatory withholding will not apply. Because employers will have options regarding this change, we will contact our clients with more information to assist them with the choice. Amendments reflecting this modification must be adopted by the end of the plan year beginning in 2011. The waiver also applies to required minimum distributions to beneficiaries under the 5-year rule, by extending the 5-year period by one year. The change in the required minimum distribution rules does not apply to defined benefit plans.



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## WORKER, RETIREE, AND EMPLOYER RECOVERY ACT (CONTINUED)

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### *Non-Spouse Beneficiary Rollover Required after 2009*

**PPA:** Plan sponsors had the option of treating distributions to designated non-spouse beneficiaries as eligible rollover distributions for the limited purpose of permitting a direct rollover into an IRA, subject to the inherited IRA rules. Mandatory 20% withholding and rollover notice requirements did not apply.

**Recovery Act:** For plan years beginning after December 31, 2009, non-spouse beneficiary rollovers are required and will be subject to all of the rollover rules, including 20% withholding and notice requirements.

### *Designated Roth Rollovers Permitted Regardless of Income*

**PPA:** Participants were permitted to roll over Roth Accounts from defined contribution plans into a Roth IRA. The earnings on the Roth Account were subject to taxation at the time of rollover, and the rollovers were restricted to participants with certain adjusted gross income levels.

**Recovery Act:** Rollovers of Roth Accounts after December 31, 2007, are not subject to income tax on the earnings or the adjusted gross income limits. The result is that rollover of Roth Accounts from 401(k) plans, 403(b) plans, and 457 plans are available to all participants, and the rollover will not be a taxable event.

### *No Distribution of Gap Earnings on Excess Deferrals*

**PPA:** For plan years beginning after December 31, 2007, gains or losses for the gap period (period between the end of the plan year and the distribution date) are not part of the corrective distribution for ADP or ACP failures. However, gap period earnings were still required to be included in the distribution to correct excess deferrals.

**Recovery Act:** With respect to gap period earnings, corrections of excess deferrals are treated the same way as corrections of ADP and ACP test failures. As a result, for plan years beginning after December 31, 2007, gap period income is not required to be included in distributions to correct excess deferrals.

### *Plans with Automatic Contributions Not Required to Satisfy Default Investment Rules*

**PPA:** A plan that qualifies as an Eligible Automatic Contribution Arrangement (EACA) must satisfy the Department of Labor's rules for a qualified default investment alternative for participants who do not make an investment election.

**Recovery Act:** Effective for plan years beginning after December 31, 2007, EACA plans no longer have to satisfy the rules for qualified default investment alternatives.

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If you have questions or would like additional information about the items presented in this newsletter, call your McCready and Keene consultant.

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*Employee Benefit News is not intended as legal advice. Readers should seek legal advice before acting on any of these subjects.*