McCready and Keene, Inc. Actuaries and Employee Benefit Consultants for Over 70 Years

Employee Benefit News

October 19, 2009

2010 COLA LIMITS - NO CHANGE FROM 2009

LIMITATION	2009	2010
401(k) and 403(b) Deferrals	$ 16,500	$ 16,500 *
457 Deferrals	$ 16,500	$ 16,500 *
415 Limits		
Defined Benefit Plans	$ 195,000	$ 195,000 **
Defined Contribution Plans	$ 49,000	$ 49,000
Highly Compensated Employee (HCE)	$ 110,000	$ 110,000
Compensation Limit - 401(a)(17)	$ 245,000	$ 245,000
Social Security Limits		
OASDI Tax Rate	6.20%	6.20%
OASDI Taxable Wage Base	$ 106,800	$ 106,800
Hospital Insurance Tax Rate	1.45%	1.45%
Hospital Insurance Taxable Wage	No Limit	No Limit
ESOP Limits		
Maximum balance subject to the 5-year distribution period	$ 985,000	$ 985,000
Amount for addition of one year to 5-year distribution period	$ 195,000	$ 195,000

* $5,500 additional catch-up for participants over age 50 by December 31, 2010, if plan allows.

** Reduced for retirement prior to age 62.

Note: In 2010, a Highly Compensated Employee will be any employee who earned over $110,000 in 2009 or who was a 5% owner in either 2009 or 2010, unless a special election was made to only include the top 20% of employees as Highly Compensated Employees.

DB/K IS COMING TO TOWN!

The Pension Protection Act of 2006 permits a new type of hybrid plan, available in 2010, which is a combination of a defined benefit plan and a 401(k) plan. Under this new type of plan, assets are held in a single trust and must be clearly identified and allocated between the defined benefit portion and the 401(k) portion. The rules typically applicable to defined benefit plans (for example, funding, joint and survivor annuity, and 415 limits on benefits) apply to the defined benefit portion, and the rules typically applicable to 401(k) plans (for example, separate participant accounts and limits on contributions) apply to the 401(k) portion. This plan type is only available to "small employers." A "small employer" is an entity that employs fewer than 500 employees.

Other requirements are:

- The defined benefit portion of the plan must provide a minimum benefit of 1% of final average compensation per year of service up to 20 years, regardless of whether the participant makes a contribution under the 401(k) portion.
- Benefits under the defined benefit portion and any profit sharing contribution under the 401(k) portion must be fully vested within 3 years.
- The 401(k) portion must provide for automatic enrollment at a rate of at least 4% of compensation and a fully-vested matching contribution equal to at least 50% of the employee's contribution up to 4% of compensation.

Neither the defined benefit portion nor the 401(k) portion is subject to the top heavy rules.

CHANGES TO 2009 FORM 5500 (FILED IN 2010)

GENERAL DISCUSSION

The government has announced revisions to the 2009 Form 5500 annual return/report to be filed in 2010. As a result, plan sponsors will need to gather additional information to complete the revised 2009 forms. You may want to consider these new requirements as you work on year-end accounting for 2009.

One of the purposes of the revisions is to give plan sponsors a better understanding of plan fees. Those changes are reflected on Schedule C. (More detail is provided below.) Another significant change for the 2009 forms is that electronic filing is required for all plans, and any employer that has an intranet website for communicating with employees MUST post the Form 5500 on their intranet. Other changes for the 2009 Form include:

- 403(b) plans must file the full Form 5500 and applicable schedules, including an independent audit for 403(b) plans with over 100 participants (note: certain fully vested contracts with no employer contributions after January 1, 2009 are excluded when determining the participant count), and
- Schedules H & I include blackout notice requirements and benefit payment failures.

SCHEDULE C REPORTING

The new fee-related reporting rules apply generally to plans with 100 or more participants. Under the new rules, all **direct compensation** and all **indirect compensation** paid to service providers who received payments exceeding $5,000 must be reported on Schedule C. There is an exception for **eligible indirect compensation**.

Some definitions would be helpful:

Direct compensation is compensation paid directly from the plan to a provider for services rendered to the plan. For example, direct compensation would include payments made from a forfeiture account (or other plan assets) to a record keeper, such as McCready and Keene.

Indirect compensation is compensation paid to service providers from sources other than directly from the plan or plan sponsor. Indirect compensation includes, but is not limited to, sub-transfer agency fees, shareholder servicing fees, account maintenance fees, and 12b-1 fees that are paid to service providers. For example, McCready and Keene's record keeping expenses are offset and sometimes paid in full by such investment charges.

If certain written disclosure requirements are met, indirect compensation is treated as **eligible indirect compensation**. To satisfy the requirements, the disclosure must provide a description of the service(s) provided, the amount (or estimated amount) of compensation or the formula used to calculate the compensation, and the name and EIN of the parties paying and receiving the compensation. Whether indirect compensation is "eligible" is important because such classification impacts the amount of information that is required on the Schedule C.

Eligible indirect compensation includes, but is not limited to, fees and/or expense reimbursement payments charged to investment funds, finder's fees, soft dollar revenue, and brokerage commissions not paid directly by the plan or plan sponsor. Any indirect compensation that is not eligible indirect compensation is **non-eligible indirect compensation.**

This article is continued on page 3.

CHANGES TO 2009 FORM 5500 (FILED IN 2010) continued

With respect to any direct or indirect compensation, a plan must report the following:

1. the identity of all persons receiving payments in excess of $5,000,
2. a code describing the services provided, and
3. with respect to each person in item 1:
    a. the total amount of direct compensation paid to the person,
    b. whether the person received any indirect compensation,
    c. whether the person received any eligible indirect compensation and, if so, whether a formula was used to determine compensation as opposed to an actual amount (or an estimated amount),
    d. the total amount of non-eligible indirect compensation, and,
    e. any relationship such person has to the employer or certain key people associated with the employer.

What employers should do now:

1. identify the persons who receive **direct compensation** from the plan in 2009,
2. determine whether the plan pays **indirect compensation** to any service providers and if so, whether the disclosure requirements described above have been satisfied,
3. identify actual amounts, estimated amounts, or the formula for **eligible indirect compensation**, and
4. identify the amount of any **non-eligible indirect compensation**.

More detailed information can be found at http://www.dol.gov/ebsa/faqs/faq_scheduleC.html.

NEW GUIDANCE DESIGNED TO INCREASE RETIREMENT SAVINGS

The Obama Administration and the Treasury Department have issued new guidance designed to increase retirement savings. You may have heard about these changes in the press. Although we do not think the changes will have a significant effect on your qualified retirement plan, we nevertheless want to keep you informed. The four primary areas of change are:

- A 401(k) plan with automatic enrollment provides that, in the absence of an affirmative election by an eligible employee, the employee is treated as having made a 401(k) deferral election. Final regulations clarify the operation of automatic enrollment programs in qualified defined contribution plans. Sample language has also been provided to aid in the amendment of plans to add an automatic enrollment program or update an existing one.

- At the end of each plan year or upon severance of employment, an employer may require or permit an employee to contribute to the employee's 401(k) account the dollar equivalent of unused paid time off. Such contributions are included in determining if the 401(k) deferral limits are satisfied. As with other 401(k) deferrals, the employee is not taxed on the contribution until withdrawal.

- The IRS has updated the notices which are provided to participants at the time of distribution which explain the participants' rollover options. We include this required notice when we prepare benefit applications for participants.

- Taxpayers will be able to direct the IRS to use their tax refunds to purchase U.S. Savings Bonds.

IRS ANNOUNCED SIGNIFICANT NEWS FOR DEFINED BENEFIT PLANS FOR 2009

In our April 30, 2009, newsletter, we reported that the IRS had issued guidance that could provide relief for sponsors of calendar year defined benefit plans in the areas of funding requirements, benefit restrictions, and Pension Benefit Guaranty Corporation ("PBGC") variable rate premiums and filing requirements. As we explained, employers may select one of the following interest rates to determine funding targets which in turn determine whether a plan is subject to benefit restrictions, amortizations and variable rate premiums:

- Option 1: three different "segment rates" that are based on a 24-month average of corporate bond yields. Employers can choose whether to use the 24-month average for the month which includes the valuation date or any of the preceding four months.
- Option 2: a full "yield curve" which is the interest rate under the corporate bond yield curve for the month which includes the valuation date or any of the four months preceding the month in which the plan year begins.

Because corporate bond rates were unusually high in October and November of 2008 (resulting in lower liabilities), option 2 would be very attractive to many plan sponsors maintaining calendar year plans. However, there was one significant drawback. Under the original guidance, once a plan sponsor chose a yield curve month, the choice was locked in, unless the IRS approved a change. As a result, using the yield curve method may present a risk for 2010 and later years due to the importance that would be put on one month's rate. For example, if an employer selected the October of 2008 interest rate for 2009 and October's rate for 2009 happened to be abnormally low, then the liabilities for 2010 and PBGC variable rate premiums would be higher than necessary.

In final regulations issued this month, the IRS granted significant relief by providing automatic approval for a new choice of interest rates for the 2010 plan year. Thus, plan sponsors may take advantage of the high rates for October and November of 2008 and use this yield curve for 2009 without being locked into it for 2010. In addition, sponsors may also make an election to use the valuation rates to determine the variable rate premium for the 2009 plan year. This results in lower PBGC variable rate premiums if the yield curve for 2008 was used for the valuation! (Note that the election for the variable rate premium does lock the plan sponsor into using the valuation results to determine the variable rate premium for four additional years.)

In 2010, plan sponsors will be able to use the 24-month average segment rates for future valuations, if desired, which will avoid the volatility that would have existed had the plan sponsor been locked into using the yield curve. The IRS is issuing this automatic approval for 2010, because the final regulations do not allow a plan sponsor to choose a look-back month (such as October or November for a January valuation date) when electing to use the yield curve in 2010 or later.

Because the corporate bond rates were <u>not</u> unusually high in months other than October and November of 2008, the yield curve will result in much less relief for non-calendar year plans, but could still result in lower PBGC variable rate premiums.

AGE 70½ AND OTHER REQUIRED MINIMUM DISTRIBUTIONS FROM DEFINED CONTRIBUTION PLANS FOR 2009

As we mentioned in our July 31, 2009, newsletter, the Worker, Retiree, and Employer Recovery Act of 2008 gives an employer sponsoring a defined contribution plan options regarding the required age 70½ and death benefit distributions for the 2009 calendar year. One option permits the employer to suspend required distributions for 2009. We are adopting this option for plans we draft, unless an employer contacts us requesting one of the alternative approaches outlined in our July 31, 2009, newsletter.

If you follow our standard approach, please notify any of the participants in your defined contribution plan who would otherwise receive a 70½ required distribution this December, that the required distributions have been suspended. The suspension also applies to participants whose required beginning date is April 1, 2010. The suspension does not prohibit participants from receiving other types of distributions otherwise available under the employer's plan.

If McCready and Keene does not draft your plan document, please contact the drafter regarding the approach to take for required minimum distributions for 2009 and any forms necessary to implement the approach.

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

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