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ERISA Disclosure Requirements

One of the major goals of the Employee Retirement Income Security Act (ERISA) was to make sure employers provide participants with plain language explanations of the provisions in their qualified retirement plans.

The preapproved defined contribution EGTRRA plan document restatement process for master, prototype, and volume submitter plans that begins in 2008 (and will run until April 30, 2010) requires that employee disclosures be updated. This article is a review of the basic ERISA disclosure requirements.

Summary Plan Description. The Summary Plan Description (SPD) is a plain language description of the retirement plan provisions that must be disclosed to participants according to ERISA. The specifics of the disclosures are elucidated in the Department of Labor (DOL) regulations. The SPD must be written so it can be understood by the average plan participant (generally at no more than an eighth grade reading level). An SPD must generally be furnished no later than 90 days after an employee becomes a participant in the plan, or, for a beneficiary receiving benefits under the plan, within 90 days after the beneficiary first receives benefits.

Every five years, participants must be provided with an updated SPD that incorporates new plan amendments made during the five-year period, even if a Summary of Material Modifications (SMM) was provided. The updated SPD must be distributed no later than 210 days after the end of the fifth year after the previous SPD was issued. If there have

been no plan amendments, then the SPD must be updated and redistributed every 10 years. Note that there has never been a 10-year period without amendments. And it is not likely to occur in the future due to ongoing required interim amendments.

Once a plan is restated onto the new EGTRRA plan document, an SPD must be provided by the 210th day after the close of the plan year during which the plan was restated. For example, the new SPD for an EGTRRA restatement of a prototype plan in 2008 is not required until 210 days after the close of the 2008 plan year. Employers will most likely want to provide an updated SPD sooner.

Potential Foreign Language

Requirement. If a plan has participants who are literate only in a particular foreign language, the plan administrator may be required to provide a notice written in that language, along with the SPD, stating that assistance in understanding the SPD is available. (The employer need not provide an SPD written in that language.) The notice must



include the plan administrator's phone number and information about where and when the assistance will be made available.

The foreign language requirement applies in the following instances. For plans with fewer than 100 participants as of the beginning of the plan year, the requirement applies if 25% or more of participants are literate only in a particular foreign language. For plans with 100 or more participants as of the beginning of the plan year, the requirement applies if *the lesser of* 500 participants or 10% of the total number of participants are literate only in a particular language.

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Summary of Material Modifications.

If an amendment is not a major modification that creates a new SPD, then participants must receive a Summary of Material Modifications. An SMM reports a change in any of the information that is provided in the SPD and is generally due within 210 days after the close of the plan year in which the change became effective.

If a new participant is to receive an SPD that has been modified by an SMM, the SMM also must be provided. Once the information in an SMM is incorporated into an updated SPD, the SMM is no longer required.

Two changes have occurred after the start of the EGTRRA document process, and each will require an SMM: the final 415 regulation plan amendment and the Pension Protection Act of 2006 plan amendment slated for 2009.

Summary Annual Report. The Summary Annual Report (SAR) is a summary of financial transactions, number of participants, and other plan-related information. An SAR is to be provided within 60 days after the filing deadline of a plan's Form 5500.

Effective with the 2008 plan year, defined benefit plans are exempt from

the SAR requirement, but are now subject to an annual funding notice disclosure requirement. (Both changes are mandated by the Pension Protection Act of 2006.)

Participant Requests for Plan

Documents. ERISA requires employers to make documents available for participant review, including the plan document, the SPD, the participant's beneficiary designation, Form 5500 and schedules, etc. Information about other participants may not be provided. When a participant or the beneficiary of a deceased participant submits a written request for copies of plan documents, the copies must be provided within 30 days. A reasonable fee may be charged to cover the cost of copying and providing the documents.

Note: There have been a number of court cases involving participant requests for plan documents that were not met within a reasonable time (such as within 30 days). Employers in these cases have been subject to a per-day late fee for violating ERISA. Such fees can quickly multiply into substantial penalties.

DOL Rules for Electronic Disclosures.

The DOL permits employers to use electronic media to provide qualified plan disclosure materials, including SPDs, SMMs, SARs, and all other

notices required under Title I of ERISA. In addition, the IRS has disseminated electronic delivery rules for certain notices, consents, and elections. To use electronic media to distribute plan-related materials, DOL regulations state that the plan administrator must:

- Ensure that participants actually receive the transmitted information by using a return-receipt electronic mail feature or by conducting periodic surveys designed to confirm the integrity of the electronic mail delivery system;
- Prepare the electronic disclosures in a manner that is consistent with the style, format, and content of the written documents;
- Notify each plan participant (including retirees, terminated employees with vested benefits, and beneficiaries) electronically or in writing which documents are provided electronically; and
- Inform participants and beneficiaries that they have the right to receive paper copies of each document free of charge.

In general, ERISA requires that those parties who are required to provide reports or disclosures must retain records of such reports. ❖

Direct Rollover to a Roth IRA

The Pension Protection Act of 2006 permits the direct rollover of a qualified plan distribution to a Roth IRA for the first time in 2008. In Publication 575, the IRS provides general rules for making such a rollover. A participant can roll over distributions directly from a qualified retirement plan to a Roth IRA if both of the following requirements are met for the tax year of the distribution: 1) the participant's modified adjusted gross income for Roth IRA purposes may not be more than \$100,000 and 2) the participant is not a married individual filing a separate return.

The participant must include in his or her gross income all distributions from a qualified retirement plan that would have

been included as income if the funds had not been rolled over into a Roth IRA. After-tax contributions are not taxed again. In addition, the 10% tax on early distributions does not apply.

The rules that apply to a traditional IRA that is converted to a Roth IRA also apply to amounts rolled over to a Roth IRA. For more information, see Chapter 1 of IRS Publication 590 (Converting From Any Traditional IRA Into a Roth IRA).

Participants must be made aware of the fact that they will have to pay income taxes on amounts rolled over to the Roth IRA. Thus, they will need additional resources available outside of the plan and the IRA to cover the resulting tax payments. ❖

QJSA Distributions: A Review

When the qualified joint and survivor annuity (QJSA) rules apply to a plan, a participant's spouse must consent in writing to waive the joint and survivor annuity when a distribution — *other than* a qualified joint and survivor annuity — is requested by the participant. The consent must be witnessed by either a notary public or plan representative.

An Overview of the QJSA Rules. The QJSA rules were created to protect retirement benefits for surviving spouses of participants in defined benefit plans. Benefits were often lost when participants selected a single life annuity. Defined benefit plans, target benefit plans, and money purchase plans — all considered to be pension plans — are required to use the QJSA rules. The normal form of distribution for a married individual in a plan subject to the QJSA rules is a joint and survivor annuity. For unmarried individuals, the normal form is a straight life annuity.

Profit sharing and 401(k) plans may be — and often are — safe harbored from the QJSA rules. However, participants in a defined contribution plan that is subject to the QJSA rules (such as a money purchase plan) frequently do not want a joint and survivor annuity form of payout. Thus, at the time of distribution, the joint and survivor annuity payout is typically waived by both the participant and spouse.

The spousal consent rules do not apply when the participant's entire vested account balance is less than the involuntary payout amount of \$5,000. Otherwise, spousal consent is needed for any type of distribution in a form other than an annuity, such as required minimum distributions, direct rollovers, plan termination distributions, etc. If permitted by the plan, the spousal consent may be a blanket consent if it is limited to a specific beneficiary and/or form of payment, such as a consent to all required minimum distributions. Electronic media may be used to satisfy the written consent requirements if the spouse has consented in person before a notary or a plan representative.

Follow the Assets. Once spousal consent has been given and the assets have been distributed, the spousal consent rules have been exercised and do not apply again. Thus, if the participant rolls the assets into a plan that meets the safe harbor requirements to avoid the QJSA rules such as a profit sharing plan,



401(k) plan, or IRA, no spousal consent is needed for a subsequent distribution from those plans.

When a money purchase plan is *merged* with a profit sharing plan or 401(k) plan, however, the money purchase funds retain the QJSA rules, and spousal consent is still needed to distribute those funds. If the money purchase assets are kept separate from the rest of the plan's assets (i.e., profit sharing or 401(k) sources), the non-money-purchase assets may still be safe harbored from the QJSA rules. But, if the money purchase plan assets are not separately maintained from the rest of the plan's assets, then the entire plan will be subject to the QJSA rules — even if those assets had been safe harbored prior to the merger.

The Decline of Money Purchase Plans. The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) included provisions (such as the increase of the profit sharing deduction limit to 25%) that virtually eliminated the need for money purchase plans. Between 2002 and 2004, many money purchase plans were eliminated. They were either merged with another plan (such as a profit sharing or 401(k) plan), converted into a profit sharing or other plan, or terminated.

Under the merger and conversion methods, the QJSA rules are brought into the surviving plan. If the plan is terminated, participants and their spouses are required to exercise the QJSA rules at the time of distribution by either waiving the rules or receiving a joint and survivor annuity. Once exercised, the rules are gone. So, if assets are rolled into an employer plan without QJSA rules, the QJSA rules do not follow.

It is important to remember that the Pension Protection Act of 2006 gave participants more options in determining the percentage a surviving spouse will receive. ❖

recent developments

■ **Supreme Court Decides 401(k) Case.** The Supreme Court ruled 9-0 in favor of LaRue, the employee in *LaRue v. DeWolff*. The case involved an employer “making up” an employee’s investment losses, which occurred due to administrative error. The employee had directed the employer to change his investment options, and the direction wasn’t followed. The market then went into a downturn (in the early 2000s) before either party noticed that the change had not been made.

Typically, an ERISA suit seeks “recovery on behalf of the plan.” In this case, the employee was seeking

to make his individual account whole. The employer argued that this was not what was meant by “recovery on behalf of the plan.” In its ruling, the Supreme Court stated that the idea of being able to sue only over losses for the entire plan was in the context of a defined benefit plan and is beside the point in a defined contribution plan. Thus, the Court ruled that although ERISA does not provide a remedy for individual injuries distinct from plan injuries, it does authorize recovery for fiduciary breaches that impair the value of plan assets in a particular participant’s individual account.

■ **IRS Permits Waiver of 50% Penalty.** The 2007 Form 5329,

Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts, reflects a change in IRS policy for taxpayers who miss taking their required minimum distribution from an IRA or qualified plan because of a reasonable error. Taxpayers who feel they meet the reasonable cause criteria set out in IRC Section 4974(d) are now allowed to *not pay* the 50% excise tax when they file their Form 1040. The instructions for Form 5329 (under Waiver of Tax on page six) tell taxpayers to attach a statement of explanation, complete Part VIII of the form, make the appropriate “RC” annotation, and enter the amount they want waived on line 52. ❖

The general information in this publication is not intended to be nor should it be treated as tax, legal, or accounting advice. Additional issues could exist that would affect the tax treatment of a specific transaction and, therefore, taxpayers should seek advice from an independent tax advisor based on their particular circumstances before acting on any information presented. This information is not intended to be nor can it be used by any taxpayer for the purpose of avoiding tax penalties.

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