

## Benefit and Advisory Compliance

### Bulletin

February 2010

December 2009 and January 2010 saw significant 401(k) plan developments, given the recognition that more needs to be done to ensure participants do not outlive their 401(k) account balances. In addition, the Internal Revenue Service (IRS) released its much anticipated 409A document correction program and announced its intention to establish a 403(b) determination letter program. On another front, the Department of Labor (DOL) released its safe-harbor ruling on plan asset deposits. Other developments over the last two months covered in this *GCA Update*: the DOL ruling on target-date funds (TDFs) and the Supreme Court's refusal to hear a controversial 401(k) excess fee case.

### Legislative Developments

#### Annuity calculations for 401(k) plans

Senator Bingaman [D – NM] introduced the Lifetime Income Disclosure Act, which requires 401(k) plan sponsors to provide an annual statement projecting a participant's account balance as a monthly benefit commencing at normal retirement age. The legislation also directs the DOL to issue factors that employers may use in calculating an annuity equivalent, as well as a model disclosure.

**Insight:** Protecting participants from outliving their 401(k) balances is a major concern of the Obama administration (see related article, below). While this bill focuses on making participants aware of the value of their account balance, other recent bills require plan sponsors to offer an annuity form of distribution.

A copy of the bill can be found [here](#).

#### Obama administration's fiscal-year 2011 budget proposal

The administration has proposed the following initiatives concerning retirement plans:

- A requirement for employers to establish automatic IRAs where they do not otherwise offer a retirement plan
- Simplification and expansion of the refundable tax credit, known as the Saver's Credit
- Enhanced 401(k) fee disclosure
- Unbiased investment advice made available by employers

- Promotion of annuities under 401(k) plans
- Requirements for clear target-date fund disclosure

**Insight:** Enhanced fee disclosure, unbiased investment advice and annuities have been topics of interest to the DOL and the subject of legislation introduced in Congress over the last year. The budget proposal supports the DOL and legislative efforts in these areas (see related article in Regulatory Developments, below).

In addition to fee reviews being a hot-button issue in the courts and for fiduciaries in general, competition among 401(k) vendors is at an all-time high. That's why now is an opportune time for plan sponsors to take advantage of market conditions to review and renegotiate their vendor fees (see related article in Court Decisions, below).

An official summary of the retirement provisions in the budget proposal can be found [here](#).

## Regulatory Developments

### 403(b) plan determination letter program

The IRS intends to establish programs under which 403(b) plans (both prototypes and individually designed plans) can obtain IRS review of the form of the plan document. Employers will be given a remedial amendment period to retroactively make any changes requested by the IRS during its review.

**Insight:** The IRS did not extend the December 31, 2009 deadline by which 403(b) plan sponsors were required to adopt a written plan document. Towers Watson's Governance Compliance and Advisory Group can assist plan sponsors in submitting their 403(b) plan once the program is under way.

The IRS announced the development of this program in Announcement 2009-89, which can be found [here](#).

### Cycle E cumulative list

The IRS published the cumulative list of required plan amendments for Cycle E determination letter filers (plans with sponsors whose EIN ends in 5 or 0, and certain other plans). Requests for determination letters for Cycle E plans must be submitted between February 1, 2010 and January 31, 2011.

The cumulative list, published in Notice 2009-98, can be found [here](#).

### Target-date fund update

The DOL has opined that assets held in a fund of funds (i.e., a mutual fund that invests in the shares of affiliated funds) are not "plan assets" under ERISA. Specifically addressing target-date and life-cycle mutual funds, the DOL noted that holding "shares of affiliated mutual funds does not, on that basis alone, make the assets of the target-date or life-cycle mutual fund 'plan assets' under ERISA."

**Insight:** The opinion reinforces the DOL's long-standing position that underlying mutual fund assets are not ERISA "plan assets." Given the increased target-date fund scrutiny by the media and industry groups, and the performance of some of these funds, now is an opportune time for plan sponsors to review whether the target-date funds offered as their plan's default investment are appropriate.

A copy of the Advisory Opinion 2009-04, can be found [here](#).

### **Safe harbor for remitting employee contributions**

The DOL's final rule providing a safe harbor for employers to remit employee contributions does not apply to large pension plans (i.e., generally those with at least 100 participants). The DOL also considered a safe harbor for large plans, but has decided against it at this time.

**Insight:** As a result of this ruling, large plans must remit participant contributions in accordance with the general plan-asset rule. Under the general rule, employers must remit employee contributions to pension plans as soon as they can be reasonably segregated from the general assets of the employer, but no later than the 15th business day of the month following the month in which contributions are received or withheld by the employer. This rule is not a safe harbor. Contributions must be transferred to the plan as soon as possible. Now is a good time for plan sponsors to review their deposit procedures.

A copy of the DOL's rule can be found [here](#).

### **IRS introduces 409A plan document correction program**

Released after much speculation and anticipation, the new program:

- Provides transition relief for document failures corrected by December 31, 2010, generally without any income inclusion or application of the 20% tax
- Allows plan sponsors to correct certain document failures at any time without income inclusion or the 20% tax, if the provision being modified does not affect actual operation of the plan for a period of one year following the correction
- Allows plan sponsors to treat certain ambiguous, but relatively common phrases (e.g., "as soon as practicable" and "termination of employment") as compliant with 409A if they have not been interpreted in a manner that is inconsistent with the requirements of 409A
- Allows plan sponsors to make corrections to certain document failures without any income inclusion or application of the 20% tax during a limited period after the adoption of a new plan, provided the plan is the first one of that type the sponsor has ever maintained

The correction program is not available to stock options or stock appreciation rights, and is available to certain linked plans only on a transition basis through 2011.

**Insight:** Along with the operational correction program and the transition relief, plan sponsors should consider a 409A compliance review before the end of 2010, especially since the IRS has started to audit nonqualified deferred compensation plans. (The IRS began 409A audits in October 2009.)

A copy of the program, in Notice 2010-6, can be found [here](#).

### **Encouraging annuity options in retirement plans**

The DOL and IRS issued a request for information (RFI) to help determine whether (and, if so, how) they could enhance, by regulation or otherwise, the retirement security of participants in retirement

plans by facilitating access to, and use of, lifetime income or other arrangements designed to provide a lifetime stream of income after retirement.

In general, the request seeks:

- Information on current plan practices and employee behavior
- Feedback on whether lifetime income payments could be fostered through new kinds of participant education and disclosure, product changes or rule changes concerning qualified joint and survivor annuities, spousal consent, minimum distributions, purchases of lifetime income from defined benefit plans, annuity provider selection, ERISA section 404(c) and qualified default investment alternatives

**Insight:** In an individual account plan, plan sponsors can make annuities available in the following ways:

- Offer annuities as an investment option
- Purchase annuities for plan participants upon retirement or termination of employment
- Work with an annuity provider to make a wide range of annuities available for participants to purchase (at a lower purchase price than the participant could get in the open market)

In addition, products are available that are not annuities but have similar characteristics, such as predictable year-to-year payments. Legal changes over the last few years have made it easy for defined contribution (DC) plans to eliminate annuity forms of distribution. However, an increased reliance on DC plans as a primary source of retirement income has heightened the focus on their role in providing security throughout participants' lifetimes. When reviewing the distribution options offered under their DC plan, employers should think holistically about how well the current design meets the needs of employees and the objectives of the company's retirement program. Towers Watson's Governance and Compliance Advisory Group can help plan sponsors determine the best approach for both their organization and plan.

A copy of the RFI can be found [here](#).

## Court Decisions

### Supreme Court declines to review 401(k) fees case

The Court's refusal to review *Hecker v. Deere & Co.* leaves standing a Seventh Circuit decision that held, among other things, that there is no duty under ERISA to disclose a revenue-sharing arrangement.

**Insight:** While this ruling is certainly good for plan sponsors, fee litigation is still rampant. Although revenue sharing may be off the table (at least in the Seventh Circuit), many other types of excess-fee cases are currently being litigated. That's why plan sponsors should seriously consider taking advantage of the current competition between vendors to review and renegotiate their fees.

This document is incomplete without the accompanying discussion by a Towers Watson consultant. All materials and intellectual capital contained within are property of Towers Watson. This publication was prepared to support our clients' need for information on the issues discussed. Recipients should understand that this publication does not constitute, and should not be used as a substitute for, legal, accounting, actuarial, tax or other professional advice. If such advice is required, the recipient should engage the services of the appropriate professional.

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