

THE ERISA LAW GROUP, P.A.

205 North Tenth Street, Suite 300 · P.O. Box 853 · Boise, ID 83701
208.342.5522 · Fax: 208.342.7672 · Toll Free: 1.866.ERISALAW (374.7252)
www.erisalawgroup.com

ERISA NEWSLETTER

TO: CLIENTS AND COLLEAGUES
DATE: NOVEMBER 2008

This Newsletter discusses –

- the Heroes Earnings Assistance and Relief Tax Act of 2008,
- Department of Labor proposed regulations regarding new mandated disclosures to participants (page 3),
- the benefits of proper completion of Form 5500 (page 4),
- the 2009 cost-of-living increases (page 4), and
- last chance for deferred compensation plan compliance (page 5).

For more information, please contact Jeffery Mandell or John Hughes.

HEART ACT

The Heroes Earnings Assistance and Relief Tax Act of 2008 (“HEART”), signed into law on June 17, 2008, makes several changes affecting your plan. These changes might impact your plan’s operations now, and will in the future require a plan amendment. Your summary plan description should be amended shortly.

Death Benefits. HEART provides that any benefits provided under a qualified plan, 457(b) plan, or 403(b) plan to a participant who dies while actively employed must also be provided to a participant who dies while in qualified military service. That means that such employee might have to become 100% vested (the vesting schedule would not apply). The provision is effective for participants who die on or after **January 1, 2007**. Because such individual is treated as having been employed on his or her death, the employee who died while on military leave might also have to receive an employer contribution including for 2007 and/or 2008. If you had an employee in this circumstance, or have one or more in the future, please contact us for further guidance.

Differential Wage Payments. Differential wage payments are amounts employers voluntarily pay to employees called to duty to supplement the employee’s military pay. HEART requires that if an employer makes differential wage payments to a participant who is on active duty for more than 30 days, the differential pay must be treated as compensation for plan purposes. That means that the employee could make and would receive a contribution with respect to such pay. Employees receiving differential pay are treated as employees; i.e., they are not treated as having incurred a severance of

employment for plan purposes (with some exceptions, such as for distributions). Differential pay will now be subject to income tax withholding that must be reported on Form W-2.

These provisions are mandatory for plan years beginning after, or payments made after, December 31, 2008, if an employer makes differential wage payments.

Distributions. HEART provides that participants called to active duty for more than 30 days will be treated as having severed employment for purposes of obtaining distributions of certain employee contributions and employer contributions under certain plans. If the participant elects a distribution, he or she cannot make employee contributions for six months following the distribution.

The Pension Protection Act of 2006 temporarily exempted the 10% early distribution penalty for distributions made to individuals who were called to military service for at least 180 days. The Act makes this exemption permanent.

Service Credit. The Uniformed Services Employment and Reemployment Rights Act (“USERRA”) already provides that participants who return to employment from qualified military service must be credited for their time away from employment for vesting and benefit accrual purposes. HEART extends this rule to participants who are unable to return to employment on account of their death or disability while in service. This provision is optional; that is, an employer may amend its plan to implement it but is not required to do so.

Employer Contributions. Another optional provision allows plans to make contributions on behalf of participants who are unable to return to employment due to death or disability. In this regard, the participant in certain employee contribution plans (such as a 401(k) plan) will be treated as having made contributions based on an average rate of his or her contributions prior to departing for military service. This provision is effective for participants who die or become disabled on or after January 1, 2007.

Cafeteria Plans. HEART also makes changes to cafeteria plans (i.e., Internal Revenue Code Section 125 plans). The Act provides an exception to the “use or lose” requirement that amounts contributed to a health flexible spending account be forfeited if not used for qualified medical expenses. The exception allows distributions of all or a portion of the participant’s unused flexible spending account balance that is not used for medical expenses. A distribution is available only if the participant is a member of a reserve component called to active duty indefinitely or for at least 180 days. This provision may be effective for distributions made on or after June 17, 2008 so long as certain requirements, including the adoption of a plan amendment, are satisfied.

Action Required. If an employee died (or dies) in service on or after January 1, 2007, contact us. The employee’s beneficiaries may have to receive certain benefits not otherwise provided under the plan. If you have any employees serving in any of the military branches, their treatment under HEART also must be examined. You will be required to amend your plan or plans within the extended IRS deadline, whether or not you ever have an employee in military service, and you may need to do so now if you have employees serving. Finally, the new rules are not uniformly applied to all types of plans; thus, the aforementioned requirements and conclusions may vary from plan to plan.

**PROPOSED DOL REGULATIONS REGARDING DISCLOSURES
FROM PLAN FIDUCIARIES TO PARTICIPANTS**

Recent legislative, regulatory, and judicial activities increasingly have focused on disclosures to both plan fiduciaries and plan participants. Predominately, the developments require that more and clearer information be provided relative to plan fees and investments.

The initiatives and activities include: (1) proposed Department of Labor (“DOL”) regulations regarding disclosures from plan service providers to plan fiduciaries (expected to be final in November 2008); (2) revised Form 5500 Schedule C (effective for plan years beginning in 2009); (3) class action litigation relative to arrangements with service providers and the payment of fees; (4) various legislative proposals; (5) new requirements under the Pension Protection Act of 2006 to furnish participant benefit statements (effective now); and finally and most recently, (6) proposed DOL regulations requiring disclosures from plan fiduciaries to plan participants in participant-directed individual account plans.

The proposal requiring additional disclosures from fiduciaries to participants in participant-directed individual account plans was issued by the DOL on July 23, 2008. The regulations, proposed to become effective for plan years beginning on or after January 1, 2009, will only affect plans in which the participants direct their investments. In summary, the proposal requires fiduciaries to provide all participants with:

- (a) General information about how to invest under the plan and associated limitations.
- (b) Explanations regarding fees and expenses for plan administrative services (e.g., legal, accounting, and recordkeeping), and the actual amounts charged.
- (c) Explanations of fees and expenses that may be charged against individual accounts, and the actual amounts charged.
- (d) Investment-related information including fee and expense information, past performance data, comparable benchmark returns, and a website address. Much of this information may be disclosed in a chart. The DOL developed a model chart which is attached as an appendix to the regulation.

Some of the information may be included in other documents such as the summary plan description or the participant benefit statements.

Action Required. There is no immediate action that you must take under this initiative. When the final regulations are issued, you will need to take action, but there should be ample time to ensure compliance. The failure to comply will carry steep consequences.

In the meantime, if you receive information from your recordkeepers, third party administrators, or investment managers/brokers/consultants regarding these issues, please let us know *before* acting upon it. Finally, if we have not checked your plan recently for fiduciary compliance under ERISA, now would definitely be a good time to do so.

PROPER FORM 5500 PREPARATION PAYS DIVIDENDS

Our firm with regularity reviews Forms 5500. A Form 5500 is the annual return a plan sponsor files with the Internal Revenue Service and/or Department of Labor. Our review arises in a variety of circumstances; for example, when there is a life change with the plan (establishment, merger and acquisition, significant design change, termination, etc.). Almost without exception, we recommend changes to the Forms 5500 we review. The changes range from the arguably minor correction of an incorrect employer or plan name, to more significant items such as using the wrong plan codes. For example, often the plan is coded not as an ERISA § 404(c) plan when the plan certainly should be coded as an ERISA § 404(c) plan to protect fiduciaries.

Aside from the requirement that the Form 5500 be truthful and accurate, it is important that it be correct for another reason: a Form 5500 is the primary tool by which ERISA plans are reported to the government, thus providing a critical resource for the government's audit of plans. Although the Form 5500 may, to a layman, seem perfunctory and without an abundance of information, it in fact contains a wealth of information that serves the government's objectives, not the least of which is to further its examination activities. A mistake, even seemingly minor, on a Form 5500 itself may lead to an audit. More notable, moreover, is our understanding that the Service believes that a strong correlation exists between Form 5500 errors or incongruities, even minor ones, and overall plan noncompliance. Noncompliance in turn may lead to violation of the law, and resulting loss of qualified tax status.

In short, although entering the wrong business code on a Form 5500 may seem innocuous, it may mean quite a bit more to the government. Avoiding the costs and required resources to respond to an IRS or DOL examination, without even considering the risks of the government's adverse findings, is strong incentive to carefully review plan Forms 5500 before their filing. A very little amount of time and adjustment to the Form 5500 could provide significant savings.

PLAN LIMITATIONS FOR 2009

Various retirement plan limits are subject to annual cost-of-living and/or statutory adjustments. Here are some of the more commonly applicable limits for 2009.

1. Maximum Contribution to 401(k), Profit Sharing and other Defined Contribution Plans. Increases from \$46,000 to **\$49,000 for 2009**. For most plans, the limit will apply for the plan year January 1 to December 31, 2009. *Warning. Participants of small employers may not be able to receive the \$49,000 allocation.*

2. Pre-Tax 401(k), 403(b) or 457(b) Employee Contribution Limit. Increases from \$15,500 for to **\$16,500 for 2009**.

3. Age 50 Catch-up Contribution. Increases from \$5,000 to **\$5,500 in 2009**.

4. Maximum Annual Recognized Compensation. Increases from \$230,000 to **\$245,000 for 2009**. To limit retirement plan accumulations for high paid employees, as well as to increase contributions for non-high paid employees, retirement plans generally may only recognize compensation up to this limit.

5. Highly Compensated Employee Threshold. Increases from \$105,000 to **\$110,000 for 2009**. Under ERISA's nondiscrimination rules, the employee population is divided into two groups – the highly compensated employees and the nonhighly compensated employees. A highly compensated employee generally is an employee who owns more than 5% of the employer sponsoring the plan or whose compensation in the preceding year exceeds the dollar threshold.

6. Defined Benefit Plan Limit. Increases from \$185,000 to **\$195,000 for 2009**. In a defined benefit plan, the law limits the annual pension payable to the participant upon retirement (as opposed to limiting the annual additions going into a defined contribution plan). *If you desire to accumulate possibly significant retirement benefits over and above the \$49,000 annual defined contribution limit, a defined benefit plan should be explored.*

7. Social Security Tax Wage Base. Increases from \$102,000 to **\$106,800 for 2009**. This change in the wage base will affect the way in which employer contributions are allocated to participants in “integrated” plans.

LAST CHANCE FOR DEFERRED COMPENSATION COMPLIANCE

Deferred compensation plans of most all types must comply with Internal Revenue Code § 409A. Section 409A has spawned a new regime of complex regulations generally effective since 2005. Compliance means a number of things beyond the scope of this warning, and noncompliance means severe adverse tax consequences. For several years now, we have been helping our clients to achieve compliance with the new regulations.

The final last deadline for compliance is December 31, 2008. A written document in conformance with the regulations must be executed on or before such date. If you have not yet considered your deferred compensation arrangements, of any kind, under 409A, now is your last chance to do so without incurring significant penalties and risks.

FIRM NEWS

Eric Scott joined The ERISA Law Group, P.A. as an attorney in August 2008. Eric obtained his J.D., *cum laude*, from Willamette University College of Law in 2007 where he was a member of the *Willamette Law Review*. After law school, Eric clerked for Justice Warren Jones of the Idaho Supreme Court.

John C. Hughes spoke to the Boise Chapter of the Western Pension & Benefits Conference in October 2008 about the proposed Department of Labor regulations on disclosures from plan service providers to plan fiduciaries and other fee disclosure related issues.

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This bulletin is intended to provide general information only and does not provide legal advice. This bulletin does not discuss potential exceptions to the above rules. The application of ERISA laws can be complex. For information regarding the impact of these developments under your particular facts and circumstances, please call us.