BENEFITS INSIDER
A Member Exclusive Publication

Volume 30, July 2007

WEB's ***Benefits Insider*** is a member exclusive publication providing the latest developments from the Nation's Capital on matters of interest to benefits professionals. The content of this newsletter is being provided as a result of a partnership with the American Benefits Council, a premier benefits advocacy organization, which provides its core content, and is edited by Corinne M. Tyler, Employee Benefits attorney and Senior Associate in the Cleveland Office of Baker & Hostetler LLP; ctyler@bakerlaw.com.

Articles in this Edition

RECENT LEGISLATIVE ACTIVITY **2**

GAO Releases Report on Conflicts of Interest and High Risk or Terminated Plans 2
Senate HELP Committee Approves Health IT Bill 2
Harkin Introduces Bill Tying Executive Compensation to Defined Benefit Plans 3
House Education and Labor Committee Approves Legislation Relating to Discrimination in Compensation and Benefits 3
President Bush Discusses Health Care, Open to Tax Credit as Alternative to Standard Tax Deduction 4
Senate HELP Committee Passes Bill Giving FDA Oversight of Follow-on Biologics 5
House Energy and Commerce Health Subcommittee holds Mental Health Parity Hearing 5
House Legislation Introduced to Expand HSAs 7
Military Tax Relief Bill Includes Expatriate Provision, Differential Pay Clarification and Tax-Free Distributions 8
New Legislation and GAO Report Address Hedge Funds and Pension Plans 8

RECENT REGULATORY ACTIVITY **9**

IRS Releases Guidance on Partial Plan Terminations 9
DOE Retracts Contractor Benefits Policy 10
IRS Issues Guidance on Staggered Remedial Amendment Periods 10
IRS Clarifies "Covered Employee" Definition under Section 162(m) 10
Treasury Department Issues Proposed Guidance on Comparable Contributions to HSAs, Accelerated Employer Contributions 11
IRS Clarifies 401(k) Safe Harbor under Mid-Year Addition of Roth Contribution Program 12
IRS Releases Revenue Procedure for Substitute Mortality Table Requests 12

RECENT Judicial ACTIVITY **12**

District Court Dismisses 401(k) Fee Suit Against Employer 12
Third Circuit Rules for EEOC in Retiree Health Case 13

RECENT LEGISLATIVE ACTIVITY

GAO Releases Report on Conflicts of Interest and High Risk or Terminated Plans

The Government Accountability Office (GAO) recently released DEFINED BENEFIT PENSIONS: Conflicts of Interest Involving High Risk or Terminated Plans Pose Enforcement Challenges in response to a request from House of Representatives Education and Labor Committee Chairman George Miller (D-CA) and Representative Edward Markey (D-MA). The report examines alleged conflicts of interest among pension consultants and other service providers and the effect these conflicts of interest have on defined benefit plan solvency and the likelihood of plan termination.

The report builds upon a Securities and Exchange Commission (SEC) 2005 staff report on pension consultants, which found that 13 of 24 registered pension consultants had undisclosed conflicts of interest. The GAO concludes these conflicts of interest may have adversely affected the funded status of the plans, noting the defined benefit plans using these consultants had earnings on average of 1.3 percentage points lower than other plans. The report goes on to say that although the findings are not necessarily applicable to all consultants and plans, the analysis "cautiously suggests an association with such undisclosed conflicts and plan performance."

The GAO report is also critical of the lack of formal coordination of enforcement efforts among the SEC as well as the Pension Benefit Guaranty Corporation (PBGC) and the U.S. Department of Labor (DOL), and recommends that:

- PBGC assess the risks for conflicts of interest;
- DOL expand enforcement to include a focus on PBGC-identified plans;
- Each agency share data on conflicts; and
- Congress consider amending ERISA to expand DOL's authority to recover losses from non-fiduciaries.

Legislation is expected to be introduced in the near future that will likely include expanded fiduciary liability and address such conflicts of interest.

Senate HELP Committee Approves Health IT Bill

The Senate Health, Education, Labor, and Pensions (HELP) Committee recently approved by voice vote the Wired for Health Care Quality Act (S. 1693) a health information technology (health IT) bill sponsored by Committee Chairman Edward Kennedy (D-MA) and Senators Mike Enzi (R-WY), Hillary Clinton (D-NY) and Orrin Hatch (R-UT). S. 1693 includes a broad range of provisions intended to encourage the development of standards for health IT and the adoption of health IT by providers, including:

- Establishing a public-private partnership known as the Partnership for Health Care Improvement to provide recommendations to the Department of Health and Human Services (HHS) regarding technical aspects of interoperability, standards,

implementation specifications, and certification criteria for the exchange of information; and

- Establishing the American Health Information Community as a body providing recommendations to HHS regarding policies to promote the development of an interoperable health information technology infrastructure.

The legislation also creates a series of funding mechanisms to encourage adoption of health information technology to improve health care quality and efficiency, including grants for the purchase of health IT systems to providers demonstrating financial need. A news release from the Senate HELP Committee includes a brief summary of the bill.

Senate leadership has been urged to bring the consensus legislation to the floor for consideration as soon as possible. Similar legislation passed the Senate and House of Representatives last Congress, but did not go to a conference committee to reconcile differences between the two versions. A joint letter to House and Senate leadership was recently sent to Congress urging swift passage of legislation to make widespread health information technology a reality.

Harkin Introduces Bill Tying Executive Compensation to Defined Benefit Plans
Senator Tom Harkin (D-IA) recently introduced the Restoring Pension Promises to Workers Act (S. 1725). According to a press release issued by Harkin's office, the bill would "[force] corporations that provide lavish executive pension arrangements to also provide a guaranteed, defined benefit plan for the rest of their employees." The bill would also institute a number of other broad pension policy reforms, including:

- Creating an "office of pension participant advocacy" within the DOL to address participant complaints, call for regulatory clarifications, and present ongoing recommendations for further reform;
- Prohibiting the elimination of accrued benefits during mergers and acquisitions;
- Establishing a three-year statute of limitations for plan sponsor claims on pension plan overpayments, and entirely eliminating claims in cases of participant hardship;
- Shielding retired workers from subsequent changes to pension benefits; and
- Protecting pension assets for surviving current and former spouses of deceased federal employees.

Plan sponsors are concerned, however, that the legislation would dramatically affect pension plan administration and could create a potentially untenable mandate for companies.

House Education and Labor Committee Approves Legislation Relating to Discrimination in Compensation and Benefits
After contentious debate, the House of Representatives' Education and Labor Committee recently approved the Ledbetter Fair Pay Act (H.R. 2831) by a vote of 25 to 20 along strict party lines. The bill would essentially provide a renewable statute of limitations for

claims of compensation discrimination. The bill potentially has significant implications for employee benefits as well.

The bill is related to the recent U.S. Supreme Court decision in *Ledbetter v. Goodyear Tire & Rubber Co. Inc.*, in which the Court rejected the so-called "paycheck rule" that would permit an individual to file a claim of compensation discrimination based on an alleged discriminatory act, which happened long ago, as long as the claimant still experienced the effects of that decision. The Court instead held that the limitations period begins when the discriminatory act occurs and is communicated to the individual and it does not re-start with each paycheck.

Education and Labor Chair George Miller (D-CA) and Representative Rob Andrews (D-NJ), chairman of the Subcommittee on Health, Employment, Labor and Pensions, fought off a number of amendments to the bill, including one that would have limited the scope of the legislation and one that would have specified that the provisions of the bill apply only to instances of intentional discrimination in compensation.

This legislation would have far-reaching implications for retirement plans. Prior to consideration by the committee, a chairman's substitute of the bill was presented with new language that said "this act is not intended to change current law treatment of when pension distributions are considered paid." Even with this provision, however, plan sponsors could still be liable for increased compensation when recalculating a benefit, and could be particularly costly in the event of a class action. Questions have been raised about how the bill would approach deduction limits, benefit limits under the Internal Revenue Code (IRC), company matches and earnings.

A Senate companion to the bill entitled the Fair Pay Restoration Act (S. 1843) was later introduced by Senators Edward Kennedy (D-MA) and Arlen Specter (R-PA).

President Bush Discusses Health Care, Open to Tax Credit as Alternative to Standard Tax Deduction

In an address at the White House on June 27 after a meeting with top health care advisors, President Bush discussed his priorities for reforming a system he called "too costly," "too confusing" and which "leaves too many people uninsured."

Many of his remarks were focused on the current Congressional consideration of the government-sponsored State Children's Health Insurance Program (S-CHIP). Democratic leaders are seeking a broad expansion of the program beyond the modest increases proposed in the president's budget. "This is a massive expansion of the program," the president said, "and as a result, many of these people would give up the private health insurance they have now as they move to government health care." An expansion of S-CHIP could have broader implications for national tax policy (and benefits tax policy in particular), since it would require greater federal revenue costs and could drive up the need for revenue-raising measures.

The president reiterated his support for his core health care reform principles such as:

- Expansion of "health savings accounts (HSAs), which allow people to save (tax free) for routine medical expenses and help reduce the cost of private insurance";

- Passage of "association health plans, so that small businesses can insure their workers with private coverage at the same discounts that big businesses get"; and

- Medical liability reform, "to stop junk lawsuits that drive up private insurance premiums and put good doctors out of practice."

In his Fiscal Year 2008 budget, the president had proposed a standard tax deduction for taxpayers with health insurance, applicable to both income and payroll taxes. While President Bush mentioned this proposal in his remarks, he acknowledged that a $5,000 tax credit might be an alternative way to address the treatment of health care in the tax code, while providing a greater incentive for lower-income individuals.

The president also indicated support for state health reform initiatives, saying that "[s]tates should make reforms to ensure that their citizens have access to basic private health insurance. It's a dual responsibility. If we want a better system, the federal government has a responsibility to reform, as do states." He did not mention any specific state programs such as the Massachusetts law that went into effect July 1.

Senate HELP Committee Passes Bill Giving FDA Oversight of Follow-on Biologics

The Senate Health, Education, Labor and Pensions Committee recently approved the Biologics Price Competition and Innovation Act of 2007 (S. 1695), giving the Food and Drug Administration (FDA) power to approve "follow-on" generic versions of biotech drugs for introduction into the marketplace following the expiration of an initial brand biotech drug product. A summary of the bill was released on June 22 by Committee Chairman Edward Kennedy (D-MA), who brokered the compromise agreement along with Senators Orrin Hatch (R-UT), Hillary Clinton (D-NY) and Michael Enzi (R-WY).

Many employers have expressed significant interest in this issue because biotech drug products are likely to become an increasingly important means by which to treat a wide range of health care conditions, and the availability of generic "follow-on" versions could reduce drug costs.

Under the terms of S. 1695, pharmaceutical companies would get 12 years of market exclusivity for new biotech drugs, after which generic versions could be approved and enter the marketplace. The first generic "follow-on" to be approved would get one year of exclusivity. The FDA would have responsibility for determining whether a biologically similar drug is as safe and effective as the original, without any transitional effects.

The House of Representatives is also developing legislation governing biologic "follow-ons."

House Energy and Commerce Health Subcommittee holds Mental Health Parity Hearing

On June 15, the House Energy and Commerce Health Subcommittee held a hearing on the Paul Wellstone Mental Health and Addiction Equity Act (H.R. 1424). Testimony provided at that hearing made clear that many employers believe strongly in the value of well-managed mental health benefits and are deeply concerned that H.R. 1424 would not only fail to meet the needs of employer health plan sponsors, but appears to go far beyond a mental health parity requirement in that it opens the door for the states to develop separate enforcement and remedy schemes for all types of health benefits

coverage. By contrast, the Senate's Mental Health Parity Act (S. 558) appears to better address the main employer priorities.

Testimony directed the Subcommitee's attention to the more balanced S. 558, developed by Senators Edward Kennedy (D-MA), Mike Enzi (R-WY) and Pete Domenici (R-NM) and approved by the Senate Committee on Health, Education, Labor, and Pensions. The compromise bills allows employers the flexibility to design plans, makes clear that medical management of benefits may not be prohibited, and attempts to provide uniformity between federal and state parity requirements.

During opening statements, Subcommittee Chairman Frank Pallone, Jr. (D-NJ) and Ranking Member Nathan Deal (R-GA), as well as numerous other subcommittee members, repeatedly cited the importance of mental health treatment during opening statements. The first panel of witnesses was comprised of Representatives Patrick Kennedy (D-RI) and Jim Ramstad (R-MN), the original sponsors of H.R. 1424, who discussed their personal experiences with mental health treatment and promoted the approach taken in their bill.

Also appearing on the hearing panel were:

- James Klein, President of the American Benefits Council, who had the opportunity to voice many of the concerns related to the House Bill;
- James E. Purcell, President and CEO of Blue Cross & Blue Shield of Rhode Island, who supported the House bill based on his experience with Rhode Island's parity law but also urged improvements regarding medical management;
- Edwina Rogers, vice president of health policy for the ERISA Industry Committee, who addressed the potential costs of mental health parity legislation;
- Marley Prunty-Lara, a mental health advocate, who spoke in detail about her experiences with bipolar disorder; and
- Dr. Howard H.Goldman, a professor of psychiatry at the University of Maryland, whose study determined that parity did not increase costs in the Federal Employee Health Benefits Plan, where management of mental health benefits is performed.

There was also a question-and-answer period which focused on the differences between the House bill and the Senate bill and specifically on the necessity and consequences of the House bill's explicit requirements. The House bill was silent on the issue of medical management, while the Senate bill was not.

Supporters of H.R. 1424 are urging swift consideration so that the House can act prior to Senate consideration of S. 558.

Concerns that were expressed at the June 15th hearing related to several key issues which included:

- *Flexibility Needed in Covered Benefits:* The House bill dictates the use of the DSM-IV diagnostic manual to determine insurance coverage.

- *Protection Required for Medical Management Practices:* Even more important than what conditions should be covered, the House bill does not protect medical management practices to ensure that patients are receiving appropriate care.

- *Discretion Needed for Out-of-Network Coverage:* The House bill mandates coverage for mental health and substance-related disorders by "out of network" providers if the plan does so for certain categories of medical and surgical services, thereby exceeding the rules governing the Federal Employees Health Benefits Plan, where parity is only required for "in-network" services.

- *Changes Needed to Provisions Related to State Laws:* The House bill would authorize states to enact enforcement and remedy schemes beyond what federal law prescribes.

House Legislation Introduced to Expand HSAs

Representative Charles W. Boustany, Jr. (R-LA) recently introduced the Promoting Health for Future Generations Act of 2007 (H.R. 2639). The measure intends to build "intergenerational wealth for health" by allowing adult children to inherit individual-account health plans such as health savings accounts (HSAs) or medical savings accounts (MSAs). The bill also expands HSA access for veterans and Medicare beneficiaries.

According to a media release, H.R. 2639 would:

- Permit an adult child to inherit funds from an HSA or MSA without tax penalties;

- Increase the annual HSA contribution limit to $5,500 for individual coverage and $11,000 for family coverage;

- Allow seniors age 50 and over to make catch-up contributions of up to $2000 over the annual contribution limit;

- Allow Medicare eligible seniors and VA beneficiaries to continue to contribute to an HSA;

- Permit employees to contribute to an HSA even if their spouse has a flexible spending account (FSA). Under current law, an individual may not contribute to an HSA if his spouse has a FSA, even if the individual never seeks to be reimbursed for any medical expenses from the spouse's FSA;

- Permit HSA funds to be spent or used to purchase coverage under a Medicare supplemental policy;

- Permit families to receive a tax deduction for premiums for high deductible health plans purchased on the individual market;

- Allow coverage for prescription drugs before the deductible is satisfied;

- Permit Medicare Advantage MSA plans to provide coverage before meeting the deductible for Medicare-covered preventive services;

- Allow individuals enrolled in Medicare Advantage MSAs to make contributions into the account; and

- Permit seniors to use Medicare Advantage MSA funds for wellness and fitness programs.

Boustany (a former cardiovascular surgeon), is emerging as a strong voice on health care, although H.R. 2639 is unlikely to gain traction in Congress given the lack of support among Democrats for HSAs.

Military Tax Relief Bill Includes Expatriate Provision, Differential Pay Clarification and Tax-Free Distributions

The Defenders of Freedom Tax Relief Act (S. 1593) was introduced on June 12 by Senate Finance Committee Chairman Max Baucus (D-MT) and Ranking Member Charles Grassley (R-IA). S. 1593 includes differential pay clarification and tax-free distributions from retirement plans for reservists called to active duty as well as a tax provision that requires U.S. citizens who expatriate, or permanent residents who give up their U.S. status, to recognize income on unrealized gains in excess of $600,000.

The provision on differential military pay (the difference between a national guardsman's or reservist's military pay and their civilian pay, often paid by the employer while the employee is on active duty) would allow this compensation to be treated as a payment of wages. Currently the IRS treats these payments as benefits reportable on the Form 1099, which is burdensome for both the employee and the employer. Under the legislation, the payments would be reported on the Form W-2 and would subject the differential pay payments to withholding. This would also make it easier for employers to contribute to their employees' retirement plans while the employees are serving on active duty.

In addition, the legislation would allow reservists called to active duty to take penalty-free withdrawals from retirement plans. This provision would make permanent a 2006 exception permitting qualified reservists (called to active duty for at least 179 days) to make an early withdrawal without triggering the 10-percent early withdrawal tax. The reservist would have two years from the last day of the active duty period to contribute distributions to an IRA.

The provision targeting unrealized gains would include taxation on the present value of retirement benefits (including IRAs, tax-qualified plans, and 457(b) and 403(b) plans). When retirement benefits are subsequently distributed, the individual would not be taxed on the benefits previously included in income. The proposal also states that the plan "treats" the subsequent distribution as if it had not been subject to the expatriate tax.

Plan sponsors have expressed concern about the punitive affect of applying the expatriate tax to the qualified plan benefits of resident aliens who work in the United States but return to their home countries for retirement. The expatriate tax provision was previously included in the Senate version of the minimum wage bill but was dropped during negotiations with the House of Representatives.

New Legislation and GAO Report Address Hedge Funds and Pension Plans

On June 13, Representatives Mike Castle (R-DE) and Tim Mahoney (D-FL), both members of the House Financial Services Committee, introduced the Pension Security Act of 2007 (H.R. 2683), which would require defined benefit plans to disclose their hedge fund investments on the annual Form 5500. The bill would also direct pertinent

information regarding hedge fund investments be provided to the DOL to further ensure that plan sponsors are fulfilling their fiduciary duties.

The bill was referred to the House of Representatives Education and Labor Committee. It is unclear whether or when the Education and Labor Committee will consider the bill but quick action is unlikely.

In related news, the GAO recently contacted the Council as it develops a report on hedge funds, which GAO has been asked to prepare by the Senate Finance Committee. GAO is investigating:

- The extent to which public and private sector pension plan sponsors are investing in hedge funds and the net returns of these funds relative to other types of investments;
- The characteristics of pension plans investing in hedge funds and the funds themselves;
- The benefits and risks hedge fund investments pose to pension funds and their participants, and how plan sponsors evaluate these investments; and
- Existing mechanisms to regulate and monitor public and private sector pension plan investment in hedge funds, along with the expected role of the federal government.

The GAO report is still in the early research stages and final publication is not expected before the end of the year.

These developments represent growing congressional interest in the relationship between hedge funds and pension plans and will likely attract media interest as well in the coming months.

RECENT REGULATORY ACTIVITY

IRS Releases Guidance on Partial Plan Terminations

The IRS recently released Revenue Ruling 2007-43, addressing accelerated vesting as a result of partial termination of a retirement plan under IRC Section 411(d)(3). Under the ruling, if plan participation is reduced by at least 20 percent, a partial termination of that plan is presumed to have occurred. When there is a partial termination, all of the affected participants are required to be immediately vested.

Prior to Revenue Ruling 2007-43, the IRS had not articulated a clear standard for determining whether a partial termination under IRC Section 411(d)(3) had occurred, although the IRS used a 20-percent "rule of thumb." The 20-percent rule of thumb was widely relied upon by practitioners and has appeared prominently in a number of court cases involving partial terminations. Revenue Ruling 2007-43 endorses its official use and also casts some light on the mechanics of measuring the percent reduction in plan participation.

DOE Retracts Contractor Benefits Policy

The U.S. Department of Energy (DOE) has decided not to reissue its contractor benefits policy, initially proposed in April 2006, which would have denied its private sector contractors reimbursement for defined benefit pension plans and certain health benefits for newly hired employees. Instead, the proposed policy would have reimbursed contractors only for the costs of their market-based defined contribution pension plans and "market-based" medical benefit plans. A formal announcement of DOE's decision, however, has not yet been made.

Under pressure from lawmakers and groups submitting public comment letters, the DOE temporarily shelved this policy in June 2006. Now, after soliciting input and recommendations on how to address surging benefits-related contractor costs, the DOE has withdrawn the proposed policy indefinitely.

IRS Issues Guidance on Staggered Remedial Amendment Periods

The IRS recently issued Revenue Procedure 2007-44, updating previous guidance on staggered remedial amendment periods for individually designed and pre-approved qualified plans. Under the staggered determination letter filing system, first established in IRS Revenue Procedure 2005-66 plan sponsors (including sponsors of hybrid plans) generally file for determination letters within staggered cycles that depend on the sponsor's taxpayer identification number. These staggered periods are also used to process determination letter requests.

Section 3 of the new guidance describes the relevant changes. Most notably, the guidance states that IRS will not address Pension Protection Act (PPA) amendments in determination letter requests for individually designed plans based on its 2006 and 2007 cumulative lists of required plan documents. However, preapproved (prototype and volume submitter) defined benefit plans must be amended for certain provisions of PPA, and will be included in the IRS review.

IRS Clarifies "Covered Employee" Definition under Section 162(m)

The IRS officially issued Notice 2007-49, which clarifies that the definition of a "covered employee" under the IRC as it relates to the disclosure of executive compensation differs from the term as provided in the most recent disclosure rules under the SEC.

Currently, Code Section 162(m)(1) limits the deduction a corporation is allowed to take for certain covered employee compensation that exceeds $1 million per taxable year. Subsequently, the final SEC regulations governing executive compensation disclosure pronounced "named executive officers" to be the determining factor, and thereafter the Treasury Department (Treasury) and IRS followed suit by using this definition for determinations under Section 162(m).

Notice 2007-49 alters the Treasury/IRS approach, stating that "the amended [SEC] disclosure rules increase the number of executives who are named executive officers by virtue of their position from one to two, and reduces the number of executives who are named executive officers based on their compensation level from four to three. Thus, while the amended disclosure rules continue to require disclosure for five executive officers, two executives are now covered by the rules based on their positions, and three are covered by the rules based on their level of compensation. In contrast, a covered

employee for purposes of Section 162(m)(3) consists of only one executive officer based on his or her position and four officers based on their level of compensation."

Since Code Section 162(m)(3) has not been amended since the SEC disclosure rules were finalized, the IRS announced that the agency will define "covered employee" under Section 162(m) as:

- any employee, who as of the close of the taxable year either is the principal executive officer of the taxpayer, or is serving as the acting principal executive officer; or

- any employee whose total compensation for a taxable year is required to be reported to shareholders under the Securities and Exchange Act for being among the three highest compensated officers.

Individuals will be excluded if the disclosure of their compensation is required under the Securities and Exchange Act because the individual is the taxpayer's principal financial officer or is serving as the acting principal financial officer. The IRS has since clarified that this was intended to include a company's chief financial officer.

Treasury Department Issues Proposed Guidance on Comparable Contributions to HSAs, Accelerated Employer Contributions

Treasury recently issued proposed regulations on comparability rules for employer contributions when an employee has not established a health savings account (HSA) by December 31 of any year. This was an issue that the Treasury "reserved" for a later rulemaking when it issued its July 31, 2006, final regulations, clarifying and expanding upon guidance regarding the comparability rules. Under federal tax law, an employer who fails to make comparable contributions to the HSAs of its employees during a calendar year is subject to an excise tax equal to 35 percent of the aggregate amount contributed by the employer to the HSAs of its employees for that year.

The proposed regulations provide a means by which employers can comply with the comparability requirements for employees who delay establishing an HSA until after December 31 or who establish an HSA but do not notify the employer of that fact. To be in compliance, the employer must satisfy specific notice and contribution requirements: the written notice must be provided by January 15 of the following year and explain that if the employee establishes the HSA by the last day of February and notifies the employer of such establishment, the employee will receive a comparable contribution to the HSA. For employees who satisfy these requirements, the employer's comparable contribution, plus reasonable interest, must be made to the HSA by April 15. The proposed regulation includes sample notice language.

The proposed regulations also address a second issue in which an employer accelerates part or all of its contribution for the entire year to HSAs of employees who have incurred qualified medical expenses (during the calendar year) that exceed the employer's cumulative HSA contributions at that time. According to the proposed regulations, if an employer accelerates contributions for this reason, these contributions must be available on an equal and uniform basis to all eligible employees throughout the calendar year and employers must establish reasonable uniform methods and requirements for acceleration of contributions and the determination of medical expenses.

The regulations will apply to employer contributions made on or after the date final regulations are published in the Federal Register, although taxpayers may rely on the proposed regulations for guidance pending the issuance of final regulations. The notice also states that, alternatively, until publication of final regulations, an employer may continue to rely on previously proposed comparability regulations published in the Federal Register on August 26, 2005, (Q&A 6(a) of Section 54.4980G-4) which provide that an employer is not required to make comparable contributions for a calendar year to an employee's HSA if the employee has not established an HSA by December 31st of the calendar year.

The comment deadline for the proposed regulations is August 30, 2007. A public hearing on the proposed regulations is scheduled for September 28, 2007.

IRS Clarifies 401(k) Safe Harbor under Mid-Year Addition of Roth Contribution Program

The IRS recently released Announcement 2007-59, which states that a plan will not fail to be a 401(k) safe harbor plan merely because the plan is amended mid-year to add a qualified Roth feature and/or the expanded hardship withdrawals made possible by the Pension Protection Act of 2006 (PPA). Although not expressly addressed in the announcement, presumably the guidance also applies to 401(m) safe harbor plans.

The announcement also asks whether additional guidance is needed with respect to mid-year changes to safe harbor plans. Comments to the IRS are requested in writing by September 17, 2007.

IRS Releases Revenue Procedure for Substitute Mortality Table Requests

The Treasury and the IRS published proposed regulations on the mortality assumptions that a defined benefit plan must use in funding calculations for plan years beginning on or after January 1, 2008 in accordance with the PPA.

These regulations also provide the framework for the development and use of a substitute mortality table based on the plan's own mortality experience. The IRS has now issued Revenue Procedure 2007-37, which describes the process for requesting rulings on the acceptability of substitute mortality tables under the IRC and ERISA.

RECENT JUDICIAL ACTIVITY

District Court Dismisses 401(k) Fee Suit Against Employer

The U.S. District Court for the Western District of Wisconsin has granted a motion to dismiss 401(k) plan fee litigation in *Hecker et al v. Deere & Company/Fidelity*. The class-action suit was one of several regarding fee arrangements in 401(k) plans, generally targeting revenue sharing arrangements. The plaintiffs alleged fiduciary duty violations stemming from the defendants' (i) selection of investment options with "excessive and unreasonable fees and costs," and (ii) failure to disclose to plan participants appropriate information regarding such fees and costs, including failure to disclose revenue sharing payments between the service providers.

With respect to the allegation that the "defendants breached their fiduciary obligations by selecting and offering investment options with unreasonably high fees," the court ruled that the company would be protected by the ERISA Section 404(c) safe harbor because

the plan permitted the participants to choose among a broad array of investment options. The court went on to state that even if 404(c) did not apply, the breadth of the investment options available to participants, which was over 2500 funds, when taking into account the directed brokerage window, made "untenable" the plaintiffs' claims that every investment option was "burdened with excessive expenses."

The issue of 401(k) plan fees continues to attract attention in the House of Representatives. The House Ways and Means Oversight Subcommittee intends to hold as many as two hearings in the fall. Meanwhile, House Education and Labor Committee has already introduced legislation to require expanded disclosure of 401(k) fees and is conducting a series of hearings on the topic.

Third Circuit Rules for EEOC in Retiree Health Case

The U. S. Court of Appeals for the Third Circuit recently unanimously held in *AARP v. Equal Employment Opportunity Commission (EEOC)* that the EEOC reasonably exercised its exemption authority under the ADEA when the agency proposed regulations permitting the coordination of retiree health care benefits with Medicare eligibility. The appeals court decision affirms a lower court decision, but relies on different reasoning.

The EEOC proposed the regulation in 2003 to exempt from the ADEA the practice of altering, reducing or eliminating employer-sponsored retiree health benefits when retirees become eligible for Medicare or a state-sponsored retiree health benefits program. The regulation was proposed in response to *Erie County Retirees Ass'n v. County of Erie*, in which the Third Circuit held that, since Medicare eligibility is age dependent, the ADEA did not permit reduction or termination of retiree health benefits upon Medicare eligibility unless the employer met the "equal benefit or equal cost" test. Publication of the final regulation was blocked when the AARP successfully challenged the EEOC's authority to issue the exemption.

In the decision, the Third Circuit held that Section 9 of the ADEA clearly and unambiguously grants to the EEOC the authority to provide narrow exemptions from the ADEA. According to the court, "because the language of section expressly grants the EEOC the power to implement such exemptions, there is no question that a limited exemption shown by the agency to be reasonable, necessary and proper falls within the agency's authority under the statute." The court further held that the EEOC had satisfied that standard when it set forth its reasons in the proposed regulation and indicated that the regulation is intended to respond to the unintended negative effects of its prior approach, "namely that employers have chosen to terminate retiree benefits rather than adhere to a standard that has proven to be costly to sustain."

The appeals decision made specific reference to an *amicus brief* filed by the Equal Employment Advisory Council, the HR Policy Association, America's Health Insurance Plans, the American Benefits Council, the ERISA Industry Committee, the National Rural Electric Cooperative Association, the Society for Human Resource Management, WorldatWork, the College and University Professional Association for Human Resources, and the American Council on Education in support of the EEOC, and noted the broad support among labor groups and employers for the proposed regulation. The decision lifts the injunction of the implementation of the proposed EEOC regulation, clearing the way for publication of a final regulation. It is not yet known whether AARP will appeal the decision to the U.S. Supreme Court.