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Articles in this Edition

RECENT LEGISLATIVE ACTIVITY 2

Health Information Privacy Bill Introduced in House 2
GAO Issues Report on Hedge Funds, Including Appendix on Retirement Investments 2
White House Introduces Medicare Funding Legislation 3
House Leaders Thanked for Rejection of Medicare ESRD Expansion 3
Senate HELP Committee Holds Hearing on Ledbetter Pay Discrimination Issue 4

RECENT REGULATORY ACTIVITY 4

DOL Unveils Retirement Planning Resource 4
IRS Private Letter Ruling Addresses and IRS Provides Further Guidance on Performance-Based Compensation under Tax Code Section 162(m) 4
PBGC Proposes Regulations with New Information Reporting Requirements........ 5
PBGC Implements Diversified Investment Policy 6
Congressmen Submit Comments to DOL on Proposed 401(k) Plan Disclosure Rules 6
IRS Ruling Addresses Use of Qualified Plan Assets for Purchasing Long-Term Care Insurance 7
DOL Outlines Fiduciary Responsibility for Collection of Delinquent Contributions 7
Treasury, IRS Release Guidance on Hybrid Plan Backloading Rules 7
IRS Affirms: Effective Date Interpretation Applies to Earlier Proposed Regulations 8

RECENT JUDICIAL ACTIVITY 8

U.S. Supreme Court Reverses Decision in LaRue 401(k) Case 8

RECENT LEGISLATIVE ACTIVITY

Health Information Privacy Bill Introduced in House

Representatives Edward Markey (D-MA) and Rahm Emanuel (D-IL) recently introduced the Technologies for Restoring Users' Security and Trust (TRUST) in Health Information Act (H.R. 5442), a bill to increase individuals' access to their own health information while still preserving the personal privacy, security, and confidentiality of that information. The legislation is designed to coincide with the creation of a nationwide interoperable health information system.

According to a news release accompanying the bill's introduction, H.R. 5442 would:

- enable patients to keep their medical records out of health information technology (IT) systems unless they provide consent;
- require patients to be notified if systems containing their health information are breached and their records are exposed;
- mandate the use of data security safeguards such as encryption and other technologies to protect sensitive information;
- authorize grant funding to enable the purchase and enhance the use of qualified health IT systems; and
- establish a public-private partnership to make recommendations concerning health IT standards, criteria for the electronic exchange of personal health information and the creation of a nationwide interoperable health information technology infrastructure.

Mr. Markey is a member of the House Energy and Commerce Committee, which shares jurisdiction over health care legislation. Additional legislation is expected to be introduced in the coming weeks.

GAO Issues Report on Hedge Funds, Including Appendix on Retirement Investments

The U.S. Government Accountability Office (GAO) recently issued the report HEDGE FUNDS: Regulators and Market Participants Are Taking Steps to Strengthen Market Discipline, but Continued Attention Is Needed. The report was inspired by the recent surge of hedge funds (pooled investment vehicles that are privately managed and often engage in active trading of various types of securities and commodity futures and options) and increasing questions about their potential risks. The report is based on review of policy documents, industry reports and interviews with regulatory and industry officials, and:

- describes how federal financial regulators oversee hedge fund-related activities under their existing authorities;
- examines what measures investors, creditors, and other parties have taken to impose market discipline on hedge funds; and
- explores the potential for systemic risk from hedge fund-related activities and describes actions regulators have taken to address this risk.

The report ultimately finds that hedge fund advisers have improved disclosures and transparency about their operations since the near collapse of the large hedge fund Long-Term Capital Management, but financial regulators and industry participants remain concerned about the adequacy of risk management at major financial institutions because it is a key factor in controlling the potential for hedge funds to become a source of systemic risk.

The report includes "Appendix II: Pension Plan Investments in Hedge Funds Have Increased but Are Still a Small Percentage of Plans' Total Assets". The appendix presents summary information about the potential impact that pension law reform may have on the ability of hedge funds to attract pension plan investments and statistics on the extent of pension plan investments in hedge funds in recent years. A forthcoming GAO report (expected to be issued in the summer of 2008) will provide more detailed information about various aspects of pension plan investments in hedge funds.

Congress continues to show interest in the potential risks associated with hedge funds and their taxation.

White House Introduces Medicare Funding Legislation

The Bush Administration recently submitted the Medicare Funding Warning Response Act, a measure designed to reduce overall spending in the Medicare program. Under the Medicare Modernization Act of 2003 (MMA), the President is required to submit such a legislative proposal if it is determined that more than 45 percent of total Medicare spending will be derived from general revenues (rather than trust funds) within the current or following six years. (This determination was confirmed in April 2007.)

The Bush Administration's proposal calls attention to the excess cost growth plaguing Medicare and the health care system overall, and emphasizes a shift from traditional fee-for-service arrangements to modern designs that offer greater choice and price accountability to individual consumers.

To arrive at this goal, the proposal sets forth three specific courses of action:

- implement the principles of value-based health care (as embodied by the U.S. Health and Human Services Department's ongoing campaign);
- address the burdens of liability on health care and insurance providers; and
- increase individual awareness and responsibility of health care costs.

An official summary of the measure is available. This bill may be a vehicle for legislation promoting medical liability reform and health information technology (part of the value-driven health care platform). However, it is still unclear whether Congress will seriously consider the proposal.

House Leaders Thanked for Rejection of Medicare ESRD Expansion

Thirty three employer organizations signed a group letter to Representatives Charles Rangel (D-NY) and Jim McCrery (R-LA) (the chairman and ranking member, respectively, of the House of Representatives Ways and Means Committee) and Representatives John Dingell (D-MI) and Joe Barton (R-TX) (the chairman and ranking member, respectively, of the House Energy and Commerce Committee), thanking them for their roles in rejecting an extension of the Medicare Secondary Payer (MSP) period for end-stage renal disease (ESRD) in the Medicare, Medicaid and SCHIP Extensions Act of 2007. The letter also urges the congressmen to reject the provision if it arises again as part of a legislative proposal. President Bush has included the provision as part of his Fiscal Year 2009 budget proposal.

As contained in the 2007 bill, the provision would require employers with 100 or more workers to be the primary payers for coverage for individuals with end-stage renal disease (ESRD) for up to 42 months. Currently, employer plans are required to cover individuals with ESRD for an initial 3 month waiting period after a patient is diagnosed with this condition, plus an additional 30 months after the waiting period. After the initial 33-month period, Medicare becomes the primary payer for individuals with end-stage renal disease. ESRD is the only disease which

Medicare covers for individuals regardless of their age. The provision is estimated to save Medicare $1.2 billion over a ten year period, but would likely cost employer-sponsored health plans considerably more – between $3 and 4 billion – than the amount Medicare would save because commercial payment rates for this service are often two to three times higher than the rate Medicare sets for itself for payment for ESRD treatment.

Senate HELP Committee Holds Hearing on Ledbetter Pay Discrimination Issue

The Senate Health, Education, Labor and Pensions (HELP) Committee recently held a hearing on S. 1843, The Fair Pay Restoration Act: Ensuring Reasonable Rules in Pay Discrimination Cases. The legislation, sponsored by HELP Committee Chairman Edward Kennedy (D-MA) is a response to the decision of the Supreme Court in *Ledbetter v. Goodyear*, which held that employees must sue for pay discrimination within a specific statutory period of time (180 days of the date of the alleged discriminatory act). The plaintiff in the case had failed to file suit within that time frame.

S. 1843 would allow the statute of limitations to begin again each time a payment of wages or benefits (including pensions) was made. There are currently 32 Senate cosponsors of S. 1843. A similar bill, the Lilly Ledbetter Fair Pay Act (H.R. 2831) passed the House of Representatives on July 31, 2007. The sponsors of S. 1843 and H.R. 2831 included in the "findings" sections of the bills a provision saying that it was not intended to change any retirement plans. This intention was not reflected in the body of the bill.

During the Senate HELP hearing, both the plaintiff in the original *Ledbetter* case and other witnesses mentioned the effect that discrimination had on retirement benefits. This would indicate that the Senate intends to open retirement plans to liability in pay discrimination cases.

RECENT REGULATORY ACTIVITY

DOL Unveils Retirement Planning Resource

The U.S. Department of Labor (DOL) Employee Benefits Security Administration has unveiled an online publication, Taking the Mystery out Of Retirement Planning, designed to help individuals calculate their financial needs for retirement. The resource includes interactive worksheets and a narrative with illustrations, principles and "clues" to help people through the process. According to a recent news release, "using the worksheets, individuals who are 10 to 15 years from retirement can calculate their income and savings as well as their projected expenses in retirement."

Plan sponsors may find this publication a potentially valuable resource for older workers and recent retirees, consistent with the "increasing financial literacy" goal of Safe and Sound, a long-term strategic plan for improving personal financial security. Employers may want to consider sharing this resource with their employees.

IRS Private Letter Ruling Addresses and IRS Provides Further Guidance on Performance-Based Compensation under Tax Code Section 162(m)

The Internal Revenue Service (IRS) recently issued Revenue Ruling 2008-13, providing guidance on performance-based compensation under Internal Revenue Code (Code) Section 162(m), which limits the amount of compensation paid to certain key employees (other than performance-based compensation) that can be deducted by an employer.

Section 162(m) had been the subject of IRS Private Letter Ruling (PLR) 200804004, which states that performance-based compensation plans will not qualify for the performance-based compensation exception under Code Section 162(m) if they provide amounts payable without

regard to whether performance goals are met upon an executive's involuntary termination or resignation for good reason.

Revenue Ruling 2008-13 expands the interpretation of the PLR, disqualifying performance-based compensation plans from the exception if they provide amounts payable without regard to whether performance goals are met if the covered employee's employment is involuntarily terminated by the corporation without cause or the covered employee terminates his or her employment for good reason, or *if the covered employee retires*.

The revenue ruling does provide relief for existing plans, as it will not be applied to compensation plans if *either*:

- the performance period for such compensation begins on or before January 1, 2009, or
- the compensation is paid pursuant to the terms of an employment contract as in effect (without respect to future renewals or extensions, including renewals or extensions that occur automatically absent further action of one or more of the parties to the contract) on February 21, 2008.

While the expansion of the PLR's approach is not ideal, and the guidance does not allow for a notice and comment period, the relief provided by the IRS provides some security for existing performance-based compensation plans.

PBGC Proposes Regulations with New Information Reporting Requirements

The Pension Benefit Guaranty Corporation (PBGC), the governmental agency that insures defined benefit pension plans, has issued proposed regulations providing guidance on determining whether defined benefit pension plans must report certain financial and actuarial information with the PBGC. Modification of these filing requirements, found in ERISA Section 4010, was required by the Pension Protection Act of 2006.

The proposed regulations, released in late February and applicable to information years beginning after 2007, provide guidance for plan sponsors on the circumstances under which they must disclose to PBGC financial statements or other information for determining plan assets and liabilities. The regulations also:

- waive information reporting in certain cases for controlled groups with aggregate underfunding of $15 million or less;
- modify the standards for determining which plans are exempt from reporting actuarial information; and
- revise the actuarial information requirements to conform to other PPA changes and provide other clarifications.

The first reports under the new rules would generally be due by April 15, 2009. The PBGC previously issued Technical Update 07-2 on November 28, 2007, providing guidance on annual financial and actuarial reporting requirements under the Pension Protection Act of 2006 (PPA). Under this update, for purposes of the annual employer reporting and reportable events regulations, a plan’s unfunded vested benefits and vested benefits amounts are determined as of the relevant year-end “testing date” using the rules for determining the variable rate premium under the law in effect before the enactment of the PPA. The guidance in this Technical Update generally applies (1) under the annual employer reporting regulation, to information years that begin before 2008 and (2) under the reportable events regulation, to event years that begin in 2008.

Public comments on the proposed regulations are due by April 21, 2008.

PBGC Implements Diversified Investment Policy
The PBGC has adopted a new investment policy that calls for increased diversification of its invested assets (approximately $55 billion). PBGC Director Charles E.F. Millard asserted in a February 18 statement that "Although [the new policy] should generate higher returns, it also offers lower risk through broader diversification. This strategy gives the [PBGC] a 57 percent likelihood of full funding within ten years, compared to 19 percent under the previous policy."

The PBGC intends to allocate 45 percent of its assets to a diversified set of fixed-income investments, 45 percent to diversified equity investments and 10 percent to alternative investment classes. The agency's previous policy set an equity investment target of 15-25 percent, although the actual level of equity investments was 28 percent at the end of FY 2007.

The investment strategy and calculation assumptions of the PBGC have often been questioned, and it has been recommended that the agency employ an investment strategy with more equities for long-term growth. More reasonable assumptions in determining assets and liabilities would more accurately reflect the actual level of the PBGC's balance sheet. The PBGC reported in its Fiscal Year 2007 Annual Management Report that the agency's deficit for 2007 has fallen to $13.1 billion, an improvement over the $18.1 billion deficit in 2006. The agency previously reported deficits of $22.8 million deficit reported in 2005 and the $23.3 billion deficit reported in 2004.

Congressmen Submit Comments to DOL on Proposed 401(k) Plan Disclosure Rules
Key Democrats from the House of Representatives Education, HELP Committee and the Senate Aging committee have submitted comments to the U.S. Department of Labor (DOL) on its proposed fee disclosure guidance under ERISA Section 408(b)(2).

The DOL proposed regulations and proposed class exemption require that contracts and arrangements between employee benefit plans and service providers include provisions that will ensure the disclosure of information to assist plan fiduciaries in assessing the reasonableness of compensation or fees paid by the plan, as well as the potential for conflicts of interest. (An official DOL fact sheet is available.)

The Democrats' comment letter urges the DOL "to act promptly to more seriously monitor 401(k) plan operations," with the following four key points of emphasis:

- "The [DOL] needs to more fully consider the unique nature of participant-directed plans and focus its regulations on protecting participants who are neither informed nor protected by employer decision-making."
- "The [DOL] must more fully exercise its authority to monitor pension plan operations and make that information widely available so that policymakers can monitor the adequacy of existing policies and practices."
- "The [DOL] needs to more actively work with other federal and state agencies to monitor investment products that are marketed and sold to pension plans."
- "The [DOL] should regularly review the documents that are being provided to pension plans and participants to ensure that financial service firms are providing needed information in understandable terms."

The letter also focuses on specific elements of the proposed regulations, such as class exemptions, bundled services, information disclosure and termination penalties.

It is expected that Representative George Miller (D-CA), chairman of the House Education and Labor Committee and one of the letter's signers, will introduce a revised version of his Fair Disclosure for Retirement Security Act (H.R. 3185) in the coming weeks. The revised bill is expected to receive consideration by his committee and the full House of Representatives in the next few months.

IRS Ruling Addresses Use of Qualified Plan Assets for Purchasing Long-Term Care Insurance

A recently published IRS private letter ruling (PLR), originally dated November 15, 2007, addresses the use of qualified plan assets to purchase qualified long-term care insurance. The PLR reaffirms the proposed regulations on accident or health insurance under a qualified plan (issued August 20, 2007), in which IRS states its position that "the payment of premiums from a qualified trust for accident or health insurance, including a qualified long-term care insurance contract under section 7702B, constitutes a distribution under section 402(a) to the participant against whose benefit the premium is charged."

DOL Outlines Fiduciary Responsibility for Collection of Delinquent Contributions

The DOL recently issued Field Assistance Bulletin (FAB) 2008-01, outlining the responsibilities of named fiduciaries and trustees of ERISA-covered plans for the collection of delinquent employer and employee contributions. The FAB is intended to address situations in which pension plan agreements relieve the financial institutions serving as plan trustees of any responsibility to monitor and collect delinquent contributions. In some of these cases, no other trust agreement or plan document assigns those obligations to another trustee or imposes the obligations on a named fiduciary with the authority to direct a trustee. In other cases, the plan documents and trust agreements are silent or ambiguous on the matter.

The FAB makes clear that "the responsibility for collecting contributions is a trustee responsibility." It further states that "if a plan has two or more trustees, the duty may be allocated to a single trustee. A plan may also provide that a named fiduciary may direct a trustee as to this responsibility or may appoint an investment manager to take on this duty. To the extent the nature and scope of the trustee's responsibilities are specifically limited in the plan documents or trust agreement, it is generally the responsibility of the named fiduciary with the authority to hire and monitor trustees to assure that all trustee responsibilities with respect to the management and control of the plan's assets (including collecting delinquent contributions) have been properly assigned to a trustee or investment manager."

Treasury, IRS Release Guidance on Hybrid Plan Backloading Rules

The U.S. Treasury Department (Treasury) and the IRS recently issued Revenue Ruling 2008-7, formally addressing the application of the accrual rules for pension plans under Internal Revenue Code Section 411(b)(1) (commonly referred to as the "backloading" rules).

In short, the ruling articulates in detail how the backloading rules work; in this regard, the IRS generally reiterates its recent unfavorable views. The ruling also states that under certain conditions (discussed below), it will provide relief through the end of the 2008 plan year to plans using a "greater of" formula. In general, plans that have been faced with the "greater of" issue will be able to satisfy the conditions. However, the relief only applies for tax purposes; the IRS' unfavorable position would apply for ERISA purposes. In a separate news release, the Treasury announced that the backloading regulations will be revised effective for the 2009 plan year to solve the "greater of" problem. Therefore, from the tax perspective, the IRS' objective is to solve this problem by giving relief for the past and changing the regulations for the future.

In order to qualify for the relief, a plan must:

- as of 2/19/08, have a favorable IRS determination letter covering its greater of formula;

- as of 2/19/08, be within its remedial amendment period (i.e., generally, the period during which curative amendments can still be made to fix a plan qualification problem) with respect to the plan amendment creating the greater of formula, or

- be one of the plans caught by the hybrid plan determination letter moratorium.

In addition, each of the plan's formulas must, tested separately, satisfy the backloading rules. If one of the formulas, tested separately, would not satisfy the backloading rules, it may be amended retroactively to fix that problem and thereby qualify for the relief.

The ruling contains some implicit guidance with respect to the views of the IRS on other hybrid plan issues, but the core of the ruling is summarized above. The ruling also demonstrates how a plan that provides a temporary greater of formula can satisfy the backloading rules, under certain very specific circumstances, through the use of more than one of the applicable backloading rules. There are, however, many situations where this creative solution to the backloading problem would not work, including many plans with permanent greater of formulas. However, the combination of the relief and the prospective regulatory changes will make the details of the current backloading rules less significant, at least for tax purposes.

IRS Affirms: Effective Date Interpretation Applies to Earlier Proposed Regulations

In addition, the IRS recently released Notice 2008-21, formally confirming that the agency's application of the 2009 plan year effective date for previously released regulations (for hybrid plans and defined benefit plan funding requirements, both on December 28) will similarly apply to the proposed regulations for employer-specific mortality tables (issued in May 2007) and benefit restrictions (issued in August 2007). The change in effective date had been informally announced in an IRS news release regarding the proposed funding regulations on December 28, 2007.

The notice affirmed that a reasonable interpretation of the statutory requirements (new Code Sections 430 and 436 on plan funding and benefit restrictions) would generally suffice for 2008 plan years, but included specific requirements for a reasonable interpretation, including required use of asset "smoothing" instead of "averaging". The notice also includes some special rules to provide relief to small plans.

RECENT JUDICIAL ACTIVITY

U.S. Supreme Court Reverses Decision in LaRue 401(k) Case

In late February, the U.S. Supreme Court unanimously reversed a lower court ruling in the case of *LaRue v. DeWolff,* et al., involving a 401(k) participant's right to sue the plan administrator for breach of fiduciary duty under ERISA. Under the facts of the case, the plaintiff sought to recover losses for his own individual account (rather than losses on behalf of the entire plan) when the administrator failed to carry out the plaintiff's investment directions. Also at issue was whether the reimbursement of such a claim represents "appropriate equitable relief" under ERISA.

The U.S. Court of Appeals for the Fourth Circuit had ruled in favor of the plan administrator, noting that Section 502(a)(2) of ERISA provides monetary recoveries for "the benefit of the plan as a whole, not to particular persons with rights under the plan," and further ruled that the plaintiff's claim did not qualify as equitable relief based on the premise that monetary relief against a non-fiduciary to make a participant whole does not constitute equitable relief.

The Supreme Court decision overturns the ruling of the Fourth Circuit, finding that "although §502(a)(2) does not provide a remedy for individual injuries distinct from plan injuries, that provision does authorize recovery for fiduciary breaches that impair the value of plan assets in a participant's individual account." A key element of the court's ruling was their determination that

defined contribution plans dominate the current retirement plan environment while ERISA and most precedent primarily address defined benefit plans. The Court declined to address the equitable relief theory.

This case has implications not only for defined contribution plans but for broader benefits plan administration as well.

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