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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 Christopher M. Smith, Employee Benefits attorney and Principal of Flexible Benefits Systems, Inc., csmith@fbsi.com.

Articles in this Edition

RECENT LEGISLATIVE ACTIVITY

PLEASE NOTE: Health Care Reform is updated through February 22, 2010, but may have been subsequently changed or updated as a result of ongoing congressional action. The WEB Benefits Insider will follow up on these issues and provide any updates in the March Issue.

Health Care Reform Update: President Obama Unveils Proposal

On February 22, President Obama released a summary of his health care reform proposal, intended to bridge the gap between the measures already passed by the Senate and the House of Representatives. (The proposal is also available on the White House Web site.) The Democrats' recent loss of the 60-vote "supermajority" in the Senate has yielded a stalemate and Democratic leaders are now working on compromise language and a procedural strategy that will garner enough votes for passage in both chambers.

Obama's proposal, estimated by White House officials as covering an additional 31 million people and costing approximately $950 billion over 10 years, was discussed at a public, bipartisan health care summit on February 25.

The White House released the details of the proposal in summary form. It is not yet known if legislative text will be prepared or introduced. Based on the summary, it appears to resemble more closely the Senate-passed Patient Protection and Affordable Care Act (H.R. 3590). The summary includes the following changes relevant to employer plan sponsors:

- The proposal includes the excise tax on "high-cost" insurance coverage, with thresholds raised from $8,500 for singles to $10,200 and from $23,000 for families to $27,500. These amounts would be indexed for subsequent years at general inflation plus 1 percent. Included is an adjustment for firms whose health costs are higher due to the age or gender of their workers. Unlike the Senate bill, this tax no longer counts dental and vision benefits as potentially taxable benefits.
- The high-cost plan tax (and the tax thresholds) would begin in 2018.
- The proposal closely follows the Senate bill's "employer responsibility" provisions, requiring employers (with more than 50 employees) that do not offer coverage (where at least one full-time employee obtains a tax credit for coverage in an insurance exchange) to pay a per-employee assessment. Under the Obama proposal, this amount is increased from $750 per full-time employee to $2,000. (The first 30 employers would be subtracted from the calculation of the payment amount.)
- In accordance with the employer responsibility requirement, the proposal fully eliminates the assessment for workers in a waiting period, while maintaining the 90-day limit on the length of any waiting period beginning in 2014.
- The flat-fee assessments for individuals not complying with the mandate to purchase health insurance are revised from $495 to $325 in 2015 and $750 to $695 in 2016, indexed for inflation thereafter. The proposal also raises the percent of income that is an alternative payment amount from 0.5 to 1.0 percent in 2014, 1.0 to 2.0 percent in 2015, and 2.0 to 2.5 percent for 2016 and subsequent years.
- The proposal levies annual assessments on health insurers totaling $67 billion over 10 years, beginning in 2014.
- A tax on retiree drug subsidies received by employers for providing drug benefits to retirees that are at least equal in value to those available under the Medicare Part D program would be effective in 2012.

- The proposal does not include the House bill provision adding an income surtax for individuals earning more than $1 million. Instead, the proposal includes the Senate provision implementing a FICA payroll tax of 0.9 percent on taxpayers with earned income above $200,000 ($250,000 for couples) as well as a 2.9 percent assessment on unearned income such as dividends and interest.
- A new provision would give the federal government the authority to review and possibly deny premium rate increases by health insurers. The Department of Health and Human Services (HHS) would design a process to evaluate rate hikes and require insurers to justify them. If those rates are not sufficiently justified, the HHS secretary or state insurance commissioner could deny the rate increase or require rebates to be issued. The HHS secretary would also create a Health Insurance Rate Authority to make rate review recommendations to the secretary and issue an annual report on insurance market trends.

President Obama Administration Proposes Retirement Savings Initiatives

On January 25, the Obama Administration released an official fact sheet on "Supporting Middle Class Families," an economic relief initiative addressing family caregiving, college affordability and retirement security issues. These proposals are the product of Vice President Joe Biden's Middle Class Task Force, comprised of top-level administration policymakers and charged with "raising the living standards of middle-class, working families in America." The task force met on January 25 to discuss the inclusion of these proposals in the president's State of the Union Address on January 27.

The specific retirement savings recommendations offered by the Administration appear to be either proposals already included in last year's 2010 budget submission or descriptions of regulatory efforts that are already underway:

Establishing Automatic IRAs: The proposal would require employers who do not currently offer a retirement plan to enroll their employees in a direct-deposit individual retirement account (IRA) unless the employee opts out. The contributions would be voluntary and matched by the Savers Tax Credit for eligible families. According to the fact sheet, the Administration is also streamlining the process for employers to automatically enroll workers in 401(k) plans. New tax credits would help pay employer administrative costs and the smallest firms would be exempt.

The fact sheet does not provide further detail, but the automatic IRA element appears similar to Obama's 2010 budget proposal, in which any company in business for at least two years that has 10 or more employees and does not sponsor a qualified plan would be required to implement automatic payroll deduction IRAs.

Simplifying and Expanding the Saver's Credit: The proposal would convert the "Saver's Credit" into a governmental matching contribution. The current law Saver's Credit allows low- and moderate-income individuals to take a tax credit of up to $1,000 (up to $2,000 if filing jointly), adjusted for inflation and phased out between $30,000 to $50,000, on voluntary contributions to an employer-sponsored retirement plan or an individual retirement arrangement. The administration's proposal would simplify the Saver's Credit to match 50 percent of the first $1,000 of contributions by families earning up to $65,000 and providing a partial credit to families earning up to $85,000. The Administration would also make this tax credit refundable.

This recommendation was also embodied in the President's 2010 budget proposal and is similar to the Savings for American Families' Future Act (H.R. 1961), sponsored by Representative Earl Pomeroy (D-ND).

Updating 401(k) Regulations: The proposal includes much of the work currently being undertaken by the U.S. Department of Labor (DOL), including regulations on 401(k) plan fee disclosure and investment advice for defined contribution plan participants, in addition to further study on the availability of annuities and other forms of guaranteed lifetime income and the rules surrounding target-date funds.

According to the Semi-Annual Regulatory Agenda released by the DOL Employee Benefits Security Administration (EBSA) in the fall of 2009, proposed investment advice regulations are expected to be issued by the end of February. The agency recently withdrew its final regulations interpreting the investment advice provisions of the Pension Protection Act of 2006 (PPA) and the accompanying administrative class exemption. It appears the re-proposed rule will not include an administrative class exemption.) Similarly, service provider defined contribution plan fee disclosure regulations are expected to be issued in final form in May 2010, while the participant fee disclosure regulations are expected to be issued in final form in September 2010. Various legislative proposals on plan fee disclosure are still pending in Congress and could be considered as part of defined benefit plan funding relief legislation.

DOL also announced on December 7 that the agency will make it a top priority to encourage the annuitization of defined contribution plan benefits. DOL Secretary Hilda Solis said in a video webcast that her department is working with the U.S. Treasury Department "to determine how best to enhance retirement security by facilitating access to a lifetime stream of income at retirement." An official request for information on this topic is currently in development.

Pension Reform Update: Group Letter Sent to Congress

On January 19, more than 240 pension funds, companies, charitable organizations, trade associations, and unions in sending a letter urging all members of Congress to support funding relief for defined benefit pension plan sponsors. Specifically, the letter urges Congress to adopt temporary provisions that will ease cash flow constraints and make contributions more predictable and manageable.

The accelerated funding requirements included in the Pension Protection Act and the market-driven declines in pension asset values have resulted in extreme and unanticipated jumps in upcoming pension obligations for 2009 plan years and beyond. Benefit organizations have repeatedly and consistently expressed concern to congressional representatives and their staffs about potential job loss resulting from a lack of defined benefit plan funding relief.

It now appears that both chambers of Congress are moving toward action on relief legislation.

In the House of Representatives, Ways and Means Committee members have taken the lead, in concert with the Education and Labor Committee, in crafting a measure that would likely permit greater amortization of plan losses, based on provisions in the Preserve Benefits and Jobs Act of 2009 (H.R. 3936) (sponsored by Ways and Means Committee member Earl Pomeroy (D-ND)) and the 401(k) Fair Disclosure and Pension Security Act (H.R. 2989) (sponsored by Education and Labor Committee Chairman George Miller (D-CA)).

Though lawmakers have made no final commitments, the reform measure would likely allow an extended period for single-employer defined benefit plans to amortize funding shortfalls over nine years, delaying the seven amortization payments for two years with employers making interest payments in the first two years (the so-called "2+7 rule"). An alternative provision could allow the funding of plan losses over a 15-year amortization period – though this 15-year relief would likely be limited to "ongoing plans" in which accruals are still taking place. Companies would be able to take advantage of this relief for funding obligations arising in two out of three years: 2009, 2010 and/or 2011.

Relief is also expected to require limitations on executive compensation and could also include elements of 401(k) plan fee disclosure legislation. Some modified provisions from Ways and Means Committee member Lloyd Doggett's (D-TX) Retirement Fairness Act (H.R. 4126), addressing the nondiscrimination rules of qualified retirement plans, could also be attached.

Similar efforts are also afoot in the Senate, where lawmakers have expressed interest in attaching defined benefit relief language to the first available legislative vehicle. This could include the Obama Administration's jobs package, expected to take shape soon. Senate Health, Education, Labor and Pensions (HELP) Committee Chairman Tom Harkin (D-IA) and Senate Special Aging Committee Chairman Herbert Kohl (D-WI) have also introduced 401(k) plan fee disclosure legislation that could be attached to a funding relief measure.

Despite this short time frame, additional open issues are still being debated, including the level and applicability of executive compensation limitations.

Senator Nelson to Introduce Executive Compensation Legislation

Senator Bill Nelson (D-FL) has announced his intention to introduce legislation that would address financial regulatory reform, predicating a bank's eligibility for tax deductions on compliance with new requirements governing compensation and risky practices.

Nelson's proposal would amend Internal Revenue Code Section 162(m) to provide that compensation over $1 million would be nondeductible unless it is performance-based and at least half of performance-based compensation must vest over a period of five years or more. It would also require that performance-based compensation for executives at public companies be awarded in employer stock and that compensation must include "clawback" arrangements for return of the money if misconduct surfaces. In addition, employees must end the use of personal hedging strategies, such as compensation insurance. These requirements would apply to the 25 highest-paid executives and other employees whose actions affect the risk exposure of "systemically significant" financial institutions.

While President Obama has already announced a new fee on banks to recover taxpayer money that went to rescue struggling financial institutions in 2009, the president has reportedly ruled out levies on executive compensation.

As Congress begins to consider wide-ranging financial regulatory reform proposals, the treatment of nonqualified deferred compensation is likely to be a source of both controversy and federal revenue.

RECENT REGULATORY ACTIVITY

Mental Health Parity Interim Final Regulations Formally Released

On February 2, the U.S. Departments of Labor, Health and Human Services and Treasury formally released interim final regulations, implementing the Paul Wellstone and Pete Domenici Mental Health Parity and Addiction Equity Act (MHPAEA) of 2008.

These regulations impose significant restrictions on how a plan may define its benefits, compare benefits for purposes of applying parity and utilize medical management practices. There are also several aspects of the regulations that appear to go well beyond the statutory parameters.

The regulations are applicable for plan years beginning on or after July 1, 2010, and a special effective date is provided for collectively bargained plans. However, the preamble states that the agencies will take into account good-faith efforts to comply with a reasonable interpretation of the statutory MHPAEA requirements with respect to a violation that occurs before the regulations' applicability date, though this does not prevent participants or beneficiaries from bringing a private action.

The MHPAEA, enacted October 3, 2008, expanded the requirements of the Mental Health Parity Act of 1996 (which required parity in aggregate lifetime and annual dollar limits for mental health benefits and medical surgical benefits) to include parity in financial requirements and treatment limitations. The MHPAEA also extended parity requirements to substance use disorder treatment.

BNA: IRS to Survey 401(k) Plans

The Bureau of National Affairs (BNA) is reporting that the Internal Revenue Service (IRS) plans to send a questionnaire to selected 401(k) plan sponsors "in an effort to gauge compliance and to see what compliance issues need to be addressed." BNA cites Monika A. Templeman, director of Employee Plans Examinations, who spoke before a conference on January 22. The questionnaires are expected to be sent to a cross-section of 401(k) plan sponsors before March.

The information will be used to compile a report on plan compliance trends and develop strategies to address them.

IRS Releases HEART Act Guidance

On January 10, the Internal Revenue Service released Notice 2010-15, providing guidance on the some provisions of the Heroes Earnings Assistance and Relief Tax (HEART) Act, a military tax relief bill enacted in 2008. HEART Act provides tax and savings assistance for military veterans and their families and includes a number of other provisions affecting employer-sponsored benefit plans.

This guidance addresses, in question-and-answer format:

- Section 104 of the act, relating to survivor and disability payments with respect to qualified military service;
- Section 105, relating to treatment of differential military pay as wages;
- Section 107, relating to distributions from retirement plans to individuals called to active duty;

- Section 109, relating to contributions of military death gratuities to Roth IRAs and Coverdell education savings accounts; and
- Section 111, relating to an employer credit for differential wage payments to employees who are active duty members of the uniformed services.

The IRS has already provided guidance on the tax treatment of expatriates and guidance on flexible spending accounts under the HEART Act.

The notice states that the IRS is considering issuing additional guidance related to the HEART Act and requests comments on such possible guidance. Written comments should be submitted by April 9, 2010.

DOL Finalizes Safe Harbor for Small Plan Assets Only

On January 13, the U.S. Department of Labor (DOL) Employee Benefits Security Administration (EBSA) released final regulations establishing a seven-business-day safe harbor period for small retirement plans, during which plan contributions and participant loan repayments would not be considered plan assets. The regulations are effective as of January 14, 2010.

The final regulations create a new small plan safe harbor but do not change the general current law requirement that participant contributions to pension plans must "become plan assets" as soon as they can reasonably be separated from the employer's general assets but in no event later than the 15th business day of the month following the month in which they are either received by the employer to be deposited into the plan or would otherwise have been paid in cash to the participant as regular compensation. When the contributions become plan assets is important because it would be a breach of fiduciary duty for plan assets to not be deposited in the plan. Losses and interest on late contributions or payments must be calculated from the date on which such contributions could reasonably have been segregated from the employer's general assets, not the end of the safe harbor period.

The final rule also clarifies that participant contributions are considered deposited when placed in an account of the plan, without regard to whether the contributed amounts have been allocated to specific participants or participants' selected investments.

EBSA states that the new safe harbor for small plans "will enhance the clarity and certainty for many employers as to when participant contributions will be treated as contributed in a timely manner to employee benefit plans." The final regulations, like the proposed regulations, are applicable to participant contributions to both retirement and health and welfare benefit plans. The regulations also make clear that Technical Release 92-01 (which provides an exception to the normal requirement that participant contributions be held in trust for cafeteria plans) will remain in effect until further notice.

These regulations finalize the proposed rules issued in February 2008. At that time, DOL also requested feedback about whether the safe harbor should be extended to large plans as well. However, DOL declined to extend the safe harbor to these large plans, arguing that "the agency does not believe that it has a sufficient record on which to evaluate current practices and assess the costs, benefits, risks to participants associated with extending the safe harbor or any variation thereof to large plans at this time." Officials had earlier argued that smaller employers typically need more time to complete these transactions than larger employers.

DOL Issues Outreach Information on ARRA COBRA Premium Subsidy Extension

On January 11, the Department of Labor (DOL) released various outreach materials related to the extension of the American Recovery and Reinvestment Act of 2009 (ARRA) COBRA premium subsidy assistance included in the Department of Defense Appropriations Act of 2010 (DOD Act), signed by President Obama on December 19, 2009.

The DOD Act amended ARRA to extend the COBRA premium reduction eligibility period for two months (until February 28, 2010) and increased the maximum period for receiving the subsidy from nine to 15 months.

The materials posted on the DOL Employee Benefits Security Administration's COBRA Web site include:

- An updated fact sheet
- A frequently asked questions (FAQ) document for employees (Questions 13-15 address the notices plan administrators must provide under the ARRA amendments)
- A job loss poster
- A program flyer for employees
- A program flyer for employers
- A flyer on applications for review

DOL is expected to issue updated model notices shortly to help plans comply with the new extension requirements.

DOL Announces Operation of EFAST2, New Form 5500 Documents

The Department of Labor (DOL) Employee Benefits Security Administration recently announced the operation of the EFAST2 online filing system, including the availability of the 2009 and 2010 Form 5500, and a new video on the changes to the 2009 Form and electronic filing. EFAST is designed to simplify and expedite the receipt and processing of the Form 5500 for satisfying the annual reporting requirements under ERISA and the Internal Revenue Code.

The following resources are now available:

- Official DOL/EBSA press release
- 2009 and 2010 Form 5500s
- Instructional video

IRS Issues Guidance on NQDC Plan Document Corrections

On January 5, the Internal Revenue Service (IRS) issued Notice 2010-06, providing methods for employers to voluntarily correct failures to comply with the document requirements under 409A of the Internal Revenue Code, which addresses nonqualified deferred compensation (NQDC) plans. Under 409A(a), amounts deferred under a NQDC plan are includible in income unless statutory requirements, generally relating to the time and form of payment of amounts deferred under the plan, are met both in form and operation. By making corrections, employers can avoid or reduce the current income inclusion and additional taxes applicable under the section.

Specifically, this notice provides:

- Clarification that certain language commonly included in plan documents will not cause a document failure;
- Relief permitting correction of certain document failures without incurring the income inclusion or additional taxes, provided, in certain circumstances, that the corrected plan provision does not affect the operation of the plan within one year following the date of correction;
- Relief limiting the amount currently includible in income and additional taxes for certain document failures if correction of the failure affects the operation of the plan within one year following the date of correction;
- Relief permitting correction of certain document failures without current income inclusion or additional taxes if the plan is the employer's first plan of that type (disregarding any plans not subject to § 409A or any plans under which all deferred amounts have previously been paid or forfeited) and the failure is corrected within a limited period following adoption of the plan;
- Transition relief permitting corrections of certain document failures without current income inclusion or additional taxes, if the document failure is corrected by December 31, 2010, and any operational failures resulting from the document failure are also corrected in accordance with Notice 2008-113 by December 31, 2010.

Notice 2008-113 provided guidance for corrections of certain Section 409A violations that would allow taxpayers (participants) to obtain relief from the full application of the income inclusion and additional taxes. Notice 2010-06 clarifies certain aspects of this earlier guidance, such as:

- The application of the "subsequent year correction method" to late payments of amounts deferred;
- The calculation of the amount that must be paid to the service provider (employee) as a correction of a late payment of an amount deferred under a plan if the payment would have been made in property, such as shares of stock; and
- The calculation of the amount that must be repaid by the service provider (employee) as a correction of an early payment of an amount deferred under a plan if the early payment was made in property, such as shares of stock.

IRS Provides Automatic Approval for Defined Benefit Funding Method Changes Resulting from Change in Software or Enrolled Actuary

The Internal Revenue Service (IRS) released Announcement 2010-3, providing for automatic approval of certain changes in a defined benefit plan sponsor's funding method resulting from a change in either the valuation software or the enrolled actuary.

The announcement sets forth, for plan years beginning on or after January 1, 2009, conditions for automatic approval of certain changes in the funding method for single-employer defined benefit plans that result either from a change in the valuation software used to determine the liabilities for such plans or from a change in the enrolled actuary and the business organization providing actuarial services to the plan. The guidance is being provided in response to numerous requests from actuaries and plan sponsors, many of whom are continuing to modify their valuation software in order to implement the changes to the funding rules made by the Pension Protection Act of 2006 (PPA), the Worker, Retiree, and Employer Recovery Act of 2008 (WRERA).

RECENT JUDICIAL ACTIVITY

District Court Throws Out 401(k) Fee Suit

On January 28, the U.S. District Court for the Northern District of Illinois dismissed a lawsuit filed against a plan sponsor for "excessive recordkeeping fees." The case, *George, et al. v. Kraft Foods Global*, was dismissed by U.S. Magistrate Judge Sidney I. Schenkier.

The initial complaint alleged that the defendants failed to account for revenue-sharing payments when negotiating fees with plan service providers or disclosing the fees paid by the plan, violating ERISA-imposed fiduciary obligations, and allowed an excessive amount of cash to be held by the company stock fund investment option and allowed investment management fees to be charged to the fund. The plaintiffs also argued that the fiduciary liability protection contained in ERISA Section 404(c) is not applicable because the defendants failed to disclose revenue-sharing payments to participants, making it difficult for participants to determine the actual amount of fees paid by the plan.

In dismissing the case, the court found that:

- the recordkeeping fees were in line with industry standards and were properly disclosed to participants, particularly through messages encouraging participants to consider the fees when making investment decisions;
- plan fiduciaries regularly assessed their relationship with their recordkeepers; and
- the plan's decision to unitize the company stock funds was typical to other 401(k) plans and not improper.

Congress is likely to consider legislation in 2010 regarding defined contribution plan fees and the U.S. Department of Labor is preparing final and proposed regulations on the issue.

U.S. Supreme Court Declines to Hear 401(k) Case

On January 19, the U.S. Supreme Court declined to hear the case of *Hecker et al v. Deere & Company/Fidelity*, regarding 401(k) plan fees. The U.S. Court of Appeals for the Seventh Circuit had previously denied an appeal for rehearing earlier in the year, affirming both the Seventh Circuit Court ruling for the defendant in the case and the earlier district court decision that the plaintiffs (participants in the Deere & Company 401(k) plans) failed to state a claim against the defendants. The U.S. Supreme Court did not comment on their decision.

The original class-action suit sought to address fee arrangements in 401(k) plans, generally targeting revenue sharing arrangements. The plaintiffs alleged fiduciary duty violations stemming from the defendants' selection of investment options with "excessive and unreasonable fees and costs," and failure to disclose to plan participants appropriate information regarding such fees and costs, including failure to disclose revenue sharing payments between the service providers.

An amicus brief was filed with the Seventh Circuit Court prior to its initial ruling, supporting the district court's earlier finding and also arguing that the case should not be allowed to proceed on procedural grounds, stating that declaring open season for baseless claims against 401(k) plan fiduciaries would harm the interests of plan participants seeking to save for retirement.