retirement
plan news

JANUARY/FEBRUARY 2008

QDIA Final Regulations

The Pension Protection Act of 2006 (PPA) created the qualified default investment alternative (QDIA) largely to promote the offering of automatic enrollment arrangements for 401(k) plans, including the qualified automatic contribution arrangement (QACA).

The QDIA provides a safe harbor from fiduciary risk when employers choose investments for automatically enrolled and other participants who do not make their own investment decisions. Employers who follow the QDIA regulations will have no legal liability for market fluctuations or investment outcomes when they provide a QDIA for employees who fail to direct their own investments.

The Department of Labor issued the highly anticipated QDIA regulations in late October and set an effective date of December 24, 2007 — just in time for 2008 and the debut of the qualified automatic contribution arrangement.

Qualified Default Investment Alternative. PPA's goal is for the QDIA to meet workers' long-term retirement savings needs and not just preserve capital. Rather than specify certain investment products, the final regulations spell out "mechanisms" for investing participant contributions. QDIA investment categories include:

- A product with a mix of investments that takes into account the individual's age, retirement date, or life expectancy (for example, a lifecycle or targeted retirement date fund);
- A product with a mix of investments that takes into account the characteristics of the group of employees as a whole, rather than each individual (for example, a balanced fund);
- An investment service that allocates contributions among existing plan options to provide an asset mix that takes into account the individual's age or retirement date (for example, a professionally managed account); and
- A capital preservation product, but only for the first 120 days of participation. After 120 days, the plan fiduciary must redirect the participant's investment into one of the other QDIA categories (unless the participant has withdrawn or redirected his or her investments before the 120-day period is up).

Variable Annuity and Other Pooled Investments. The QDIA categories may be offered through variable annuity contracts or through pooled investment funds, provided the QDIA regulations are satisfied.

Existing Stable Value Funds. Some plans have been using stable value products as a default investment. The final regulations "grandfather" these arrangements by providing relief for contributions invested in stable value products prior to the effective date of the final rule (December 24, 2007). No fiduciary relief is provided for future contributions to stable value products.

ERISA Supersedes State Law. The PPA and the final QDIA rule provide that ERISA supersedes any state law that would prohibit or restrict automatic contribution arrangements, regardless of

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whether such arrangements qualify for the safe harbor.

Additional QDIA Requirements. The following list includes brief summaries of other key requirements.

- Generally, a QDIA may not be invested in employer securities.
- A plan may not restrict participants from transferring the funds in a QDIA to any other investment alternative available under the plan. The transfer must be permitted with the same frequency that applies to other plan investments, but not less than quarterly.
- A QDIA must be managed by either an investment manager, plan trustee, or plan sponsor who is a named fiduciary, or by an investment company registered under the Investment Company Act of 1940.

Conditions for Fiduciary Relief. For the safe harbor protection to apply, employers must satisfy the following conditions.

- Assets must be invested in one of the QDIA investment categories.
- Participants must have had the opportunity to direct their investments but failed to do so. If an investment directive is filed later, then the investment direction from the participant will supersede the QDIA. A notice must generally be provided at least 30 days in advance of either an employee's eligibility or his or her first investment in a QDIA. A notice must also be filed 30 days in advance of each subsequent plan year.

- Investment materials for the QDIA (i.e., prospectuses, account statements, etc.) that are provided to the plan must also be furnished to participants invested in the QDIA.
- Participants must be able to direct investments out of a QDIA as frequently as they can switch out of other plan investments — but at least quarterly. During the first 90 days after the first automatic enrollment deferral is withheld and invested in a QDIA, no surrender charge, liquidation or exchange fee, redemption fee, or similar expense will be charged. However, ongoing fees related to the operation of the investment *may* be charged. After the 90-day period, the restrictions, fees, and expenses of the plan will apply to a QDIA.
- The plan must offer a "broad range of investment alternatives" as defined in the regulations in ERISA Section 404(c).

Keep in mind that investment funds, model portfolios, and investment management services must be prudently selected and monitored by plan fiduciaries (i.e., the employers). ❖

IRS and Social Security Cost-of-Living Adjustments

IRS LIMITS	2008	2007
Defined Contribution Plan Limit on Annual Additions	$46,000	$45,000
Defined Benefit Plan Limit on Annual Benefits	$185,000	$180,000
Maximum Compensation for Allocation and Accrual Purposes	$230,000	$225,000
401(k), SARSEP, 403(b), and 457 Plan Deferrals/Catch-up	$15,500/$5,000	$15,500/$5,000
SIMPLE Deferrals/Catch-up	$10,500/$2,500	$10,500/$2,500
IRA Contributions/Catch-up	$5,000/$1,000	$4,000/$1,000
Compensation Defining Highly Compensated Employee (2008 amount for use in 2009 plan year tests)	$105,000	$100,000
Compensation Defining Key Employee/Officer	$150,000	$145,000
Social Security Taxable Wage Base (SSTWB)	$102,000	$97,500

The landscape of the retirement plan industry is constantly changing. And 2008 promises more of the same. There are plan document changes in store, and the Pension Protection Act of 2006 (PPA) calls for a number of changes to defined contribution retirement plans. This article reviews the current list of 2008 changes. Of course, legislative and/or regulatory actions could create additional changes. Stay tuned.

Restatement of Preapproved Defined Contribution Plans. By April of 2008, the IRS will announce the release of opinion and advisory letters for preapproved defined contribution plan sponsors (i.e., master and prototype plans and volume submitter EGTRRA plans). The IRS will also announce the deadline by which all employers using such plans must amend and restate onto the approved EGTRRA plan documents. (The period is expected to be about two years.)

Final Section 415 Regulations Plan Amendment. The deadline for adopting the final 415 regulations is the end of the first plan year starting on or after July 1, 2007. Calendar-year plans generally must adopt this amendment by December 31, 2008. Included in these regulations are the new post-severance compensation rules.

PPA Changes. These are the major changes affecting defined contribution plans for the 2008 plan year.

Direct Rollover to a Roth IRA. Under PPA, funds from a qualified plan, such as a 401(k), may be directly rolled over to a Roth IRA. Prior to this change, the rollover went to a traditional IRA, which could then be converted to a Roth IRA. We await guidance from the IRS on the taxation and reporting of this new transaction.

Nonspouse Beneficiary. The IRS has changed this from an optional plan provision to one that is required. Thus, all qualified plans will operate under this PPA provision in 2008. The plan document amendment for PPA provisions is not required until 2009.

Bonding Increase. For non-ESOP defined contribution plans with employer securities, the bond is 10% of plan assets up to a maximum of $1,000,000 (increased from $500,000).

Automatic Enrollment Plan Testing Change. For any automatic enrollment plan subject to ADP/ACP testing, the time frame for making a refund for a failed ADP/ACP test without a 10% penalty has been extended to the end of the sixth month after the end of the plan year being tested (i.e., June 30 for a calendar-year plan).

Automatic Enrollment 90-day Revocation Period. An automatically enrolled employee in an eligible automatic contribution arrangement may opt out of deferring and request a withdrawal of all deferrals within 90 days of the first payroll from which deferrals were taken. In such a case, the plan is to return all deferrals made during that time frame (adjusted for gains or losses) to the employee, and there is no IRS penalty. We await IRS guidance to clarify operational details.

Qualified Automatic Contribution Arrangement (QACA). This new automatic enrollment plan option is generating a great deal of buzz and may become quite popular.

Qualified Joint and Survivor Annuity (QJSA) Option. New *optional survivor annuity* provisions must be made available under certain qualified plans. The new rule applies only to plans subject to QJSA rules, such as defined benefit and money purchase pension plans. If the plan's normal QJSA survivor annuity payable to the spouse after the participant's death is less than 75% of the annuity payable while both spouses are alive, the plan must allow the participant to elect an optional survivor annuity with an applicable percentage of 75%. Similarly, if the plan's normal QJSA survivor annuity is greater than or equal to 75% of the annuity payable while both spouses are alive, the plan must allow the participant to elect an optional survivor annuity with an applicable percentage of 50%. ❖

recent developments

IRS Creates New Designation. The enrolled retirement plan agent (ERPA) is a new IRS designation. ERPAs will be able to practice before the IRS regarding issues involving the Employee Plans Determination Letter program, the Employee Plans Compliance Resolution System (EPCRS), and the Employee Plans Master and Prototype and Volume Submitter program. ERPAs will also generally be permitted to represent taxpayers with respect to IRS forms under the 5300 and 5500 series but not with respect to actuarial forms or schedules. To qualify, individuals will have to pass an as yet undetermined program of IRS examinations. The IRS estimates that the earliest ERPA enrollments are 18 to 24 months away.

Form 5500 Changes. Form 5500 has been issued for the 2007 plan year. Changes include the voluntary alternative reporting option and financial schedules created by the Pension Protection Act (PPA). Certain plans having fewer than 25 participants as of January 1 of the plan year being filed may be able to take advantage of these shorter reporting requirements.

Form 5500-EZ Filing Threshold Changed. Form 5500-EZ is for plans benefiting only sole proprietors (and, if applicable, their spouses) or plans benefiting only partners (and their spouses). The filing threshold had been $100,000 in assets. Effective with plan year 2007, PPA increased the filing threshold to $250,000 in assets on the last day of the 2007 plan year. After the 2006 plan year, plans with total assets between $100,000 and $250,000 may stop filing a Form 5500-EZ until their asset base exceeds $250,000. If the employer sponsors more than one plan, the asset total is based on all the plans, not each plan separately. A Form 5500-EZ should be filed for the final plan year *regardless* of whether the plan was required to file a Form 5500-EZ for any prior year.

DFVCP Calculator. The DOL's delinquent filer voluntary compliance program (DFVCP) is for employers who fail to file a Form 5500. It encourages employers to voluntarily bring their plans into compliance by reducing the penalties that are due. If a missing Form 5500 is discovered during an audit, the penalty can be extremely high. The DOL has created a calculator on its website to allow employers to calculate the reduced penalty — *www.dol.gov/ebsa/calculator/dfvcpmain.html*. ❖

The general information in this publication is not intended to be nor should it be treated as tax, legal, or accounting advice. Additional issues could exist that would affect the tax treatment of a specific transaction and, therefore, taxpayers should seek advice from an independent tax advisor based on their particular circumstances before acting on any information presented. This information is not intended to be nor can it be used by any taxpayer for the purpose of avoiding tax penalties.

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