VEDDERPRICE®

March 2, 2009

Employee Benefits Briefing

IMPORTANT DEVELOPMENTS (OTHER THAN COBRA)

Despite the economic slowdown, this has been a busy time for benefits administrators. Year-end is always hectic, and was more so in 2008, with the need to finalize all nonqualified plans and to cope with increased pension funding requirements. 2009 appears to offer no respite, as employers continue to respond to depressed conditions with reductions in force and suspensions of 401(k) plan matching contributions. In addition to these concerns, administrators need to be aware of several recent legislative and judicial developments that will impact benefit plan administration. The following is a summary of some of the more important developments. The COBRA subsidy provisions in the economic stimulus legislation were discussed in a separate Employee Benefits Briefing, dated February 17, 2009.

I. LEGISLATIVE AND REGULATORY DEVELOPMENTS

WRERA and Defined Contribution Plans

The Worker, Retiree and Employer Recovery Act of 2008 (WRERA), signed by President Bush on December 23, 2008, includes a number of provisions relating to retirement plans. This article focuses on the changes for defined contribution plans.

Suspension of Minimum Required Distributions

Under current law, participants who are 70 ½ or older are required to take "minimum required distributions" from their defined contribution plan accounts. Minimum required distributions generally must begin by April 1 of the calendar year following the year in which the participant attains age 70 ½ and must continue to be made by the end of each year thereafter.

To provide additional time for participant account balances to recover from the recent stock market losses, WRERA permits the suspension of minimum required distributions from defined contribution plans for 2009. WRERA does not suspend the required minimum distribution rules for defined benefit plans.

WRERA does not, however, provide relief for participants who attained age 70 ½ in 2008 and elected to postpone their first minimum required distribution until April 1, 2009. For such a participant, the first minimum required distribution that is paid in 2009 is actually for 2008, and thus is not suspended under WRERA. The participant's second required minimum distribution (i.e., the minimum required distribution due by December 31, 2009) is the 2009 distribution that would be suspended. Similarly, for a participant who attains age 70 ½ in 2009, the first minimum required distribution (for 2009), is suspended even though it could be paid as late as April 1, 2010.

Required minimum distributions being made to a deceased participant's beneficiary may also be suspended for 2009. For example, if the account balance of the participant is being distributed to the beneficiary over the five years following the participant's death, the five-year period will be calculated without including 2009. Accordingly, if a participant died in 2007, and the five-year payment period previously ran from 2008 through 2012, the five-year payment period now runs from 2008 through 2013 (without a payment in 2009).

Although the concept of suspending minimum required distributions for 2009 is relatively straightforward, implementing that suspension can be more complicated. For example, it will be important to review whether participants who have begun receiving minimum required distributions or installment payments can normally suspend them, and whether (assuming distributions are suspended) an affirmative election will be required by the participant to continue receiving payments or to restart future installment or minimum required distributions. In addition, if the plan sponsor elects to suspend distributions for 2009, the plan will need to be amended to reflect this suspension, although the amendment will not be required to be made until the end of the first plan year beginning on or after January 1, 2011.

Regardless of whether a plan sponsor suspends distributions for 2009, any distributions that are made will not be considered required minimum distributions under Section 401(a)(9) of the Internal Revenue Code, and thus may be eligible to be rolled over to an IRA or another qualified plan. The fact that distributions may be eligible to be rolled over will need to be explained to participants, but the plan administrator is not obligated to allow for direct rollover.

Nonspouse Beneficiary Rollovers

The Pension Protection Act of 2006 (PPA) permitted plans to allow nonspouse beneficiaries of deceased participants to roll over their balances directly to an "inherited IRA," but did not require plans to offer this option. WRERA makes nonspouse beneficiary rollovers mandatory for plan years beginning after December 31, 2009. This change applies to both defined contribution and defined benefit plans.

Elimination of Gap Period Income

WRERA removes the requirement that refunds of excess deferrals under defined contribution plans include "gap period" income. Excess deferrals are participant pre-tax deferrals above the Internal Revenue Code Section 402(g) limit (currently $16,500). Gap period income is the earnings on the refunded amounts from the end of the calendar year in which the deferrals were made through the date the refund is made. The change is effective for excess deferrals made in 2008 (and distributed in 2009) and subsequent years.

Children's Health Insurance Program Expansion

President Obama signed the Children's Health Insurance Reauthorization Act of 2009 (the "Act") into law on February 4, 2009. The Act expands the Children's Health Insurance Program (CHIP) and, among other items, authorizes states to provide premium subsidies for group health plan coverage for eligible individuals (generally low-income children and families). The premium assistance program imposes new special enrollment, notice and disclosure obligations on employer group health plans.

Premium Assistance Program

Effective April 1, 2009, states may provide premium subsidies for "qualified employer coverage" in lieu of providing health coverage through the CHIP program.

Qualified employer coverage is:

- coverage for which at least 40% of the cost is paid by the employer;
- "creditable coverage" as defined under the HIPAA; and
- available to a reasonable classification of employees (as determined in accordance with IRS rules).

High-deductible health plans and flexible spending accounts (FSAs) are not qualified employer coverage.

Subsidies may be provided as reimbursements to the employee or through direct payments to the employer, though employers may opt out of receiving direct payments.

Special Enrollment

The Act creates new special enrollment rights for employees and dependents who are eligible but not enrolled in an employer group health plan. Group health plans must permit enrollment upon: (1) termination of Medicaid or CHIP coverage due to loss of eligibility; or (2) becoming eligible for premium assistance through CHIP for the employer's group health plan. Employees must request special enrollment within 60 days of the occurrence of one of these events. Plan administrators should note that this 60-day enrollment period is a departure from the existing special enrollment rules for loss of other coverage or acquisition of a dependent, under which employees have only 30 days to request special enrollment.

The new special enrollment rights are effective as of April 1, 2009. Plan documents and SPDs that describe special enrollment rights may need to be updated to reflect these new rights.

Notice Requirement

Employers in states that have adopted premium assistance programs must provide written notice of the program to their employees. This notice may be included in the summary plan description or in other plan information, such as enrollment materials. The Act directs the Departments of Labor (DOL) and Health and Human Services (HHS) to develop a model notice by February 4, 2010. Employers are not required to furnish this notice until after the model notice is issued.

Disclosure Requirement

Plan administrators whose plans cover Medicaid or CHIP eligible individuals will be required to disclose to the state, upon request, information about the plan, including details about benefits, premiums and cost-sharing. The disclosures are intended to assist the state in planning the premium assistance program and in determining whether the plan coverage constitutes qualified employer coverage. The Act directs HHS and DOL to develop a model disclosure form within eighteen months. States may not request this disclosure until the first plan year that begins after the model disclosure form is issued.

Penalties for Noncompliance

The Act provides civil penalties of up to $100 a day for failure to comply with the new notice and disclosure requirements.

Defined Benefit Plan Annual Funding Notice

The Department of Labor recently published, in Field Assistance Bulletin 2009-01, new guidance on the annual funding notice required for defined benefit plans.

The annual funding notice, introduced by PPA, replaces the summary annual report for defined benefit plans (defined contribution plans must still prepare a summary annual report). The FAB details the information that must be included in the notice, and provides model notices for both single employer and multi-employer defined benefit plans. Among other items, the notice must include the plan's funding percentage, a statement of the value of the plan's assets and liabilities, a description of how the plan's assets are invested as of certain dates, and a description of the benefits under the plan that are eligible to be guaranteed by the Pension Benefit Guaranty Corporation (PBGC).

Unfortunately, the model notice is up to six pages long and likely to be confusing to participants. Although the FAB provides that use of the model is not mandatory, it is anticipated that most actuarial consultants will use the model as a starting point to assure compliance with the revised disclosure requirements.

Plans must furnish the annual funding notice within 120 days of the end of the plan year. For calendar year plans, this means the notice must be provided no later than April 30, 2009. Small plans, generally those with no more than 100 participants, may delay distributions of the notice until the earlier of the due date or the actual filing date for the plan's Form 5500. The notice generally must be provided to each plan participant and beneficiary, the PBGC (if liabilities exceed assets by more than $50 million), each labor organization representing plan participants, and, for multiemployer plans, each employer obligated to contribute to the plan.

II. LITIGATION DEVELOPMENTS

Seventh Circuit Rules in "Excessive Fees" Case

On February 12, in a decision that could affect the tide of recent ERISA "excessive fee" cases, the Seventh Circuit Court of Appeals affirmed the U.S. District Court's dismissal of all claims in *Hecker v. Deere & Company* (7th Cir., Feb. 12, 2009). *Deere* is the first excessive fee case to reach a federal appeals court, and the Department of Labor filed an amicus brief in support of the plaintiffs arguing that the Court should deny Deere's motion to dismiss.

The suit involved two 401(k) plans sponsored by Deere. The Company appointed Fidelity Trust to serve as trustee to the plans. The plans offered 23

Fidelity mutual funds, two Fidelity investment funds, a Deere stock fund, and a "BrokerageLink" option that gave participants access to 2,500 additional non-Fidelity funds. Each plan participant directed the investment of his or her plan account among these funds.

Fidelity Management & Research Company ("Fidelity Research") served as investment advisor for the mutual funds offered as investment options under the plans. Each mutual fund charged a fee, calculated as a percentage of assets. Fidelity Research shared its revenue from these fees with Fidelity Trust.

The Seventh Circuit framed the plaintiffs' allegations against Deere as follows: first, that Deere breached its fiduciary duty by not informing the participants that Fidelity Trust received money from the fees collected by Fidelity Research, and second, that Deere imprudently agreed to limit the investment options to Fidelity Research funds and therefore offered only investment options with excessively high fees.

With respect to the first claim, the Seventh Circuit held that ERISA does not require the disclosure of revenue sharing arrangements. Deere disclosed to the participants the total fees for the funds and directed participants to the fund prospectuses for information about fund-level expenses. The Court concluded that this was sufficient disclosure under ERISA. The later distribution of the fees from Fidelity Research to Fidelity Trust was not material information the participants needed to know to keep from acting to their detriment. Accordingly, the omission of details of the revenue sharing arrangement was not a breach of Deere's fiduciary duty. (The opinion notes, however, that the Department of Labor has recently issued proposed regulations which would require the disclosure of revenue sharing arrangements.)

With respect to the second claim, the Seventh Circuit held that the mix of investments and fees under the plans was sufficient. The expense ratios among the Fidelity mutual funds and the funds available through BrokerageLink ranged from 0.7% to 1% of the assets under management. In addition, all of the funds were offered to investors in the general public at the same rates. That it was possible for other funds to have lower expense ratios was viewed by the Court as irrelevant: ERISA does not require "every fiduciary to scour the market to find and offer the cheapest possible fund (which might, of course, be plagued by other problems)."

In addition, the Court noted that it was not improper for Deere to limit the investment options under the plans to Fidelity mutual funds. Again, neither ERISA nor its regulations prohibit a fiduciary from selecting funds from one management company. ERISA requires that a fiduciary behave like a prudent investor under similar circumstances and, the Seventh Circuit noted, prudent investors may limit themselves to funds offered by one company and then diversify within those funds.

Finally, the Seventh Circuit concluded that, even if Deere had breached its fiduciary duties with respect to the disclosure of fees and the selection of funds, an alternate ground for dismissal was available through the "safe harbor" defense under ERISA § 404(c). Under ERISA § 404(c), plan fiduciaries are not liable for losses which result from participant directed investments if: (1) participants have the right to direct the investment of their accounts; (2) the plan offers a broad range of investment options; and (3) participants are given sufficient information to make informed decisions with regard to the investment alternatives under the plan. Because the Court concluded that Deere satisfied these requirements, the safe harbor served as a defense to the fiduciary breach claims.

The case is significant in that the Seventh Circuit dismissed the case in its entirety at the early motion to dismiss stage. The decision should provide welcome reassurance to plans sponsors of large self-directed 401(k) plans that have been a target of excessive fee complaints.

Supreme Court Upholds Plan's Distribution to Ex-Wife Where Waiver Did Not Comply With Plan Documents

In *Kennedy v. DuPont Savings & Inv. Plan* (Sup. Ct., Jan. 26, 2009), a unanimous Supreme Court held that a plan must distribute benefits to a participant's ex-wife who was the named beneficiary at the time of the participant's death, notwithstanding the ex-wife's waiver of those benefits as part of a divorce settlement.

The participant filed a beneficiary designation naming his wife as the sole beneficiary under the plan. When the participant and his wife later divorced, she relinquished all rights to any employee benefit plan accounts as part of the divorce settlement. However, the participant did not remove his ex-wife as a beneficiary under his Company's 401(k) plan, though he did execute a new beneficiary form naming his daughter as the beneficiary under the Company's defined benefit plan. When the participant died, his daughter became the executrix of his estate and asked DuPont to distribute his $400,000 account to the estate. The plan refused, and paid the account balance to his ex-wife in accordance with the beneficiary designation on file. The participant's daughter sued the administrator and DuPont, arguing that the divorce settlement amounted to a waiver of benefits and that the plan violated ERISA by paying benefits to the participant's ex-wife.

The Supreme Court held that a beneficiary can disclaim benefits through a waiver that does not qualify as a QDRO without running afoul of ERISA's anti-alienation provision. However, the Court also held that any waiver must be in accordance with the plan's waiver procedures to be effective. In this regard, the Court found that the participant had more than enough time to change his beneficiary designation and that the administrator properly considered the valid beneficiary designation and disregarded his ex-wife's disclaimer of benefits that did not comply with the plan's procedures.

Kennedy gives plan administrators the opportunity to:

- review their plan documents and summary plan descriptions ("SPDs") to determine whether they should adopt specific procedures for waiver of benefits. If plan documents and SPDs already contain a waiver procedure, plan administrators and benefits personnel should review these procedures to ensure that they are properly communicated to plan participants seeking information following a divorce. If the plan does not include a provision for a waiver of benefits, the administrator may wish to consider adding a formal waiver procedure; and
- review current procedures and forms regarding beneficiary designations. Some plans provide for automatic revocation of a spousal beneficiary designation after a divorce. Others provide that the beneficiary designation remains valid until properly revoked or changed by the participant. Administrators should be familiar with these provisions and should review beneficiary forms to see that the rules are clearly communicated.

If you have any questions about the matters discussed in these articles, please contact Paul Russell, Patrick Spangler or Jessica Winski, or any other Vedder Price attorney with whom you currently work.

FEDERAL TAX NOTICE: Treasury Regulations require us to inform you that any federal tax advice contained herein is not intended or written to be used, and cannot be used by any person or entity, for the purpose of avoiding penalties that may be imposed under the Internal Revenue Code.

VEDDERPRICE®

222 NORTH LASALLE STREET
CHICAGO, ILLINOIS 60601
312-609-7500 FAX: 312-609-5005

1633 BROADWAY, 47th FLOOR
NEW YORK, NEW YORK 10019
212-407-7700 FAX: 212-407-7799

875 15th STREET NW, SUITE 725
WASHINGTON, D.C. 20005
202-312-3320 FAX: 202-312-3322

www.vedderprice.com

The Employee Benefits Group

Vedder Price has one of the nation's largest employee benefits practices, with ongoing responsibility for the design, administration and legal compliance of pension, profit sharing and welfare benefit plans with aggregate assets of several billion dollars. Our employee benefits lawyers also have been involved in major litigation on behalf of benefit plans and their sponsors. Our clients include large national corporations, smaller professional and business corporations, multi-employer trust funds, investment managers and other plan fiduciaries.

Employee Benefits Group Members

Mark I. Bogart	312-609-7878
Sara Stewart Champion	212-407-7785
Michael G. Cleveland	312-609-7860
Christopher T. Collins	312-609-7706
Megan J. Crowhurst	312-609-7622
Thomas P. Desmond	312-609-7647
John H. Eickemeyer	212-407-7760
Thomas G. Hancuch	312-609-7824
Jonathan E. Hyun	312-609-7791
John J. Jacobsen, Jr.	312-609-7680
Michael C. Joyce	312-609-7627
Neal I. Korval	212-407-7780
Philip L. Mowery *(Practice Leader)*	312-609-7642
Stewart Reifler	212-407-7742
Paul F. Russell	312-609-7740
Robert F. Simon	312-609-7550
Patrick W. Spangler	312-609-7797
Kelly A. Starr	312-609-7768
Lawrence L. Summers	312-609-7750
Jessica L. Winski	312-609-7678
Charles B. Wolf	312-609-7888

About Vedder Price

Vedder Price P.C. is a national, business-oriented law firm with over 260 attorneys in Chicago, New York and Washington, D.C. The firm combines broad, diversified legal experience with particular strengths in labor and employment law, employee benefits, executive compensation, corporate finance and transactions and commercial litigation.

Employee Benefits Briefing is published by the law firm of Vedder Price P.C. It is intended to keep our clients and other interested parties generally informed of legal developments in employee benefits. It is not a substitute for professional advice. For purposes of the New York State Bar Rules, this bulletin may be considered ATTORNEY ADVERTISING. Prior results do not guarantee a similar outcome.