EMPLOYEE BENEFIT
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Corporate Accounting Reform and Retirement Plans

This past fall the U.S. Department of Labor issued interim final regulations on blackout notices to be provided to retirement plan participants and beneficiaries under the Sarbanes-Oxley Act of 2002.* Essentially, the regulations follow the rules laid out in the Act. Since most of the provisions affecting plans and their administration take effect in January 2003, plan sponsors should be familiar with them and their impact.

BLACKOUT NOTICES

Administrators of individual account plans, such as 401(k) plans and other participant-directed defined contribution plans, must provide all affected plan participants and beneficiaries with 30-days' notice of any "blackout period." A blackout period, for purposes of the notice requirements, is a period of more than three consecutive business days during which the normal rights of plan participants and beneficiaries to direct or diversify the assets in their accounts (or obtain plan loans or distributions) are limited or restricted.

The blackout notice must:

- Be provided in writing, but may be sent electronically as long as the notice is "reasonably accessible" to the recipient.
- State the reason for the blackout.
- List the name, address, and telephone number of the plan administrator or another person who can answer questions concerning the blackout period.
- Identify the investments affected.
- Include an expected beginning and ending date of the blackout.

The notice also must advise plan participants to evaluate the appropriateness of their current investment decisions in light of their inability to direct or diversify assets in their accounts during the blackout and to make any appropriate changes prior to the blackout beginning date.

Failure to provide participants with proper notice subjects a plan administrator — *not* the plan — to a civil penalty of up to $100 a day per participant.

EXCEPTIONS

A regularly scheduled suspension or limit that is disclosed to participants and beneficiaries through a summary plan description, summary of material modifications, or in materials describing investment alternatives under the plan is *not* considered a blackout period. Other exceptions include limitations or restrictions imposed by the application of securities laws or pursuant to a qualified domestic relations order (QDRO).

If a plan administrator cannot meet the 30-day advance notice requirement due to unforeseeable events or circumstances beyond the administrator's control or if delaying the blackout would violate fiduciary standards, the plan administrator must provide the notice as soon as reasonably possible, unless it is completely impossible, in which case notice is not required. This exception also applies if the blackout is due solely to a merger, acquisition, divestiture, or similar transaction involving the plan or plan sponsor under which affected persons become or cease to be participants or beneficiaries under the plan. An explanation of why the plan could not meet the 30-day requirement must be provided to participants and beneficiaries in writing to avoid the civil penalties.

CRIMINAL PENALTIES

The new law significantly increases the criminal penalties for *willful* violations of any of the reporting and disclosure requirements of the pension law (ERISA). The maximum

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penalty for an individual has increased from $5,000 to $100,000 and the maximum prison term from one to ten years. For corporations, partnerships, and other entities that are not individuals, the maximum penalties have increased from $100,000 to $500,000. These penalties are in addition to any civil penalties assessed.

TRADING RESTRICTIONS

The new law also prohibits directors and executive officers of an employer from trading or transferring employer securities they own outside of the company retirement plan during any blackout period that restricts plan trading of employer securities. These restrictions apply only to employer securities acquired in connection with the directors' or officers' service or employment. If officers or directors become subject to restrictions, the issuer of the employer securities must timely notify the Securities and Exchange Commission (SEC) of the blackout period.

For purposes of the insider trading restriction, a blackout period is defined as three or more consecutive business days during which at least 50% of all plan participants are unable to buy or sell employer stock held in the plan. One-participant retirement plans are excluded, as are regularly scheduled trading suspensions and limits and blackouts due to corporate mergers, acquisitions, and divestitures.

SEC REPORTING

Stock transactions by directors, officers, and 10% or more beneficial owners of a publicly traded company (as defined by the Securities Exchange Commission Act), including transactions conducted within a retirement plan, must be reported to the SEC within two business days. This provision was effective August 29, 2002. Beginning no later than July 30, 2003, the SEC will post the reported transactions on a public Internet site within one day of filing. The company issuing the stock will be required to post transaction statements on its corporate website (if the company has one) not later than the end of the business day following the filing.

EFFECTIVE DATES

Penalty and reporting provisions are already in effect. The notice requirements are effective January 26, 2003. A sample notice is included in the regulations. The regulations also provide a transition rule for the initial 30 days after the effective date. For blackouts occurring beginning between January 26, and February 25, 2003, the blackout notice must be provided "as soon as possible."

Where a plan amendment is needed to implement the new rules, that amendment does not have to be made until the first plan year beginning on or after January 26, 2003, provided the amendment is retroactive to the effective date and the plan operates in compliance with the rules in the interim. The insider trading restrictions also are effective January 26, 2003.

*P.L. 107-204 and Federal Register 10/21/2002

Plan Sponsor Priorities

The *2002 Annual Defined Contribution Survey*, conducted by CRA RogersCasey/IOMA asked employers what their priorities were for their retirement plans over the next three years.

Source: CRA RogersCasey/IOMA, June 2002

RECENT developments

DOL

The U.S. Department of Labor's Pension and Welfare Benefits Administration (PWBA) and the IRS have announced a joint project to ensure compliance with annual return/report (Form 5500) filing obligations. In December 2002, the agencies began mailing letters of inquiry to plans identified as potential nonfilers. Plan administrators who want to avoid the potential $1,100 a day penalty for failure to file *and* additional IRS penalties can take advantage of the Delinquent Filer Voluntary Compliance (DFVC) Program to file overdue reports by paying reduced penalties. Administrators who have been notified by the PWBA about a delinquent filing are not eligible to participate in the program. For more information on the joint project, contact the PWBA at 202-693-8360 or call the IRS customer service number toll-free at 877-829-5500. Information about the DFVC Program is available online at *www.dol.gov/pwba* or by calling the PWBA number above.

GAO

The General Accounting Office has published a primer on the private pension plan system and plan operation and administration. *Answers to Key Questions about Private Pension Plans* examines private pensions and public policy, types of plans employers may offer, the role of ERISA, tax code provisions on plan coverage and benefits, and government insurance protection of pension benefits. A copy is available online at *www.gao.gov/* (GAO-02-745SP).

IRS

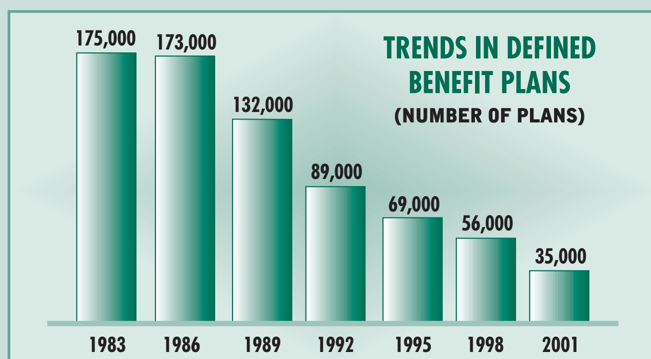
The IRS is looking into phased retirement as a possible option for private sector employers who may be facing worker shortages as increasing numbers of baby boomers reach retirement age. With a phased retirement program, older employees work full- or part-time while receiving retirement benefits. Among the issues the IRS is considering are the relevance of whether an employee has reached a plan's early retirement age and the extent to which that person has reduced his or her workload. The Service also is reviewing input from employers on guidance related to Section 415 compliance and how reductions in compensation under a phased retirement arrangement could be handled.

The IRS has published proposed regulations clarifying the requirement that defined benefit and other plans must disclose the relative value of optional forms of benefit available under the plan in lieu of a qualified joint and survivor annuity (QJSA). In essence, the proposed regulations require the optional benefit to be presented to the plan participant in the same form as the QJSA. For example, the disclosure can show the actuarial present value of an optional benefit form as a percentage of the actuarial present value of the QJSA or state the present values of the QJSA and the optional benefit. The proposed regulations also include several examples plan sponsors will find helpful in understanding the disclosure requirements (67 FR 62417).

STATS

From the Profit Sharing/401(k) Council of America's *45th Annual Survey of Profit Sharing and 401(k) Plans*: Overall, 401(k) plan participation dropped slightly in 2001 from 80.2% of eligible employees to 78%. However, the average deferral rates for plan participants remained steady at 5.3% for lower paid employees and 6.4% for higher paid employees. On average, plan participants contributed $3,514 each in 2001. Copies of the new survey can be obtained by calling 312-441-8550 or online at *www.psca.org.*

Despite a resurgence of employee interest in traditional defined benefit retirement plans, these plans continue to lose ground to 401(k) plans and other defined contribution plans, according to new research from the Employee Benefit Research Institute. From an all-time high of more than 175,000 in 1983, the number of defined benefit plans has dropped to about 35,000 in 2001. In another trend away from the traditional, more defined benefit plans are offering lump-sum distributions upon termination of employment as an alternative to monthly annuity payments.



Source: Employee Benefit Research Institute, *An Evolving Pension System: Trends in Defined Benefit and Defined Contribution Plans*, September 2002

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Recent Developments (continued from previous page)

THE COURTS

The second circuit federal Court of Appeals has joined the third and tenth circuits in ruling that qualified domestic relations orders (QDRO) rules apply to both pension and welfare plans. As part of a divorce decree, an employee agreed to name his daughters as the beneficiaries of his employer-sponsored retirement plan benefits and life insurance provided by the employer. However, he actually named his father as beneficiary of both. After the employee died, his daughters and father filed claims for the benefits. The appeals court upheld a lower court's decision that the divorce settlement was a QDRO and awarded the retirement and insurance benefits to the daughters (*Metropolitan Life Ins. Co. v. Bigelow,* CA-2, 2002).

Two participants brought successful suits against an employer's defined benefit plan because of the plan administrators' incorrect calculation of lump-sum benefits and failure to notify participants that they would forfeit benefits if they worked after retirement age. The employer maintained that the amounts awarded by the court to the participants should be paid by the plan's liability insurer under a policy which covered breaches of fiduciary responsibilities by the retirement plan and its administrator. However, the policy specifically excluded from coverage liability for any benefits due under the plan's terms. The employer argued that the exception to the coverage did not apply because the basis of the participants' claims was *not* language in the plan, but ERISA and DOL regulations under ERISA. It maintained that actions for benefits include only suits to recover *contractual* claims for benefits. A federal appeals court disagreed, stating that the claims were for plan benefits because they were based on questions about the method used to calculate the benefits. ERISA governs qualified retirement plans, but it is not the source of plan benefits. The plan is. Thus, the claims for correct pension amounts were claims for plan benefits (*The May Department Stores Company v. Federal Insurance Company,* CA-7, 2002).

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