Plan Sponsor

Outlook

A Current Issues Resource for Plan Sponsors and Administrators 4th Quarter 2007

PPA Requires Changes for 2008 Plan Year

The Pension Protection Act of 2006 (PPA) continues to have a significant impact on defined contribution plans. For the 2008 plan year, sponsors will face some required, automatic and optional actions resulting from the PPA.

Electronic filing is required

For plan years beginning on or after January 1, 2008, sponsors must electronically file the Form 5500 with the Department of Labor (DOL). The DOL is required to post this information on its Web site within 90 days of receipt, and sponsors must display it on any intranet Web site.

A calendar year plan using the maximum Form 5500 filing extension would have to electronically file by October 15, 2009. DOL and sponsor intranet postings would be due by January 31, 2010.

Recent indications from the DOL are that the electronic filing requirement will be delayed by one year to plan years beginning on or after January 1, 2009.

Maximum bond increases for some

The maximum bond requirement under ERISA has been an amount equal to at least 10% of plan assets as of the end of the previous plan year, but not greater than $500,000.

For plans holding employer securities, the maximum bond rises to $1,000,000 for plan years beginning on or after January 1, 2008.

Rollovers to Roth IRA permitted

Effective on January 1, 2008, participants in qualified plans may roll over an eligible rollover distribution to a Roth IRA, as long as his or her adjusted gross income is $100,000 or less.

Automatic enrollment safe harbor available

For plan years beginning on or after January 1, 2008, the PPA makes available an optional safe harbor for avoiding ADP, ACP and top-heavy testing. The requirements to satisfy the safe harbor include an automatic deferral percentage of at least 3% in the first year, 4% in the second, 5% in the third and 6% (but not more than 10%) thereafter.

Also required is either an employer match of at least 10% of the first 1% and 50% of the next 5% of employee contributions, or an employer contribution of at least 3% of compensation.

Vesting must occur after no more than two years, and a notice to participants is to be distributed before the beginning of the plan year.

Contributions may be withdrawn

After the commencement of automatic enrollment contributions, auto enrollment plans may distribute these contributions if the participant requests a refund within 90 days of when the first automatic contribution was made.

Distributions would consist of the automatic contributions and related earnings, and would be included in the participant's income in the year the distribution is made. The 10% penalty tax on early withdrawals would not apply. Any employer matching contributions are forfeited.

This provision is optional. It may be applied in plan years beginning on or after January 1, 2008.

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Pension Plan Limitations for 2008

401(k) Maximum Participant Deferral *(*$20,500 for those age 50 or over, if plan permits)*	$15,500*
Defined Contribution Maximum Annual Addition	$46,000
Highly Compensated Employee Threshold	$105,000
Annual Compensation Limit	$230,000

PPA Changes for 2008

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New deadline for return of contributions

Also effective for plan years starting on or after January 1, 2008, corrective distributions of excess contributions from failed 401(k) plan ADP tests may be made within six months following the end of the plan year. These distributions are taxable in the year received, and are exempt from the 10% early distribution penalty tax.

Previously, these corrective distributions had to be made within 2½ months of the end of the plan year for the sponsor to avoid a 10% excise tax.

Section 404(c) relief extended

ERISA Section 404(c) provides relief to plan fiduciaries for investment losses incurred when a participant or beneficiary exercises control over the investment of his or her individual account. The PPA added a provision for relief in situations involving "fund mapping."

When investment choices are changed by the plan sponsor (for example, when a sponsor changes service providers), participants have an opportunity to choose from among new options. Old investment options are often "mapped" to new, comparable choices. Default arrangements are created for cases in which participants do not make new elections.

Fund mapping qualifies for 404(c) protection if:

- written notice of the changes and the default procedure is distributed to participants and beneficiaries at least 30 days but not more than 60 days before the effective date of the changes;
- the participant does not make an affirmative election before the effective date of the change; and,
- the participant's account was invested in accordance with his or her elections immediately before the changes are effective.

This is optional, and is available in plan years beginning on or after January 1, 2008.

Plan sponsors are encouraged to consult their plan's legal counsel for guidance on these PPA provisions.

By the Numbers...

How Does Your Plan Compare?

Data compiled from the retirement plan activities of 3 million participants in 1,800 plans in 2006 indicate little change in a number of benchmarks in recent years.

The average participation rate was 64%, essentially unchanged since 2000. As expected, older and higher-paid employees continued to be more likely than younger or lower-paid workers to participate. Women were more likely than men to enroll, across all income levels.

Participants contributed an average of 7.3% of their pay, also unchanged since 2000. One-fourth of participants contributed 10% or more and another quarter saved 4% or less. Only 10% saved the maximum permitted by law. About 14% used the catch-up contribution feature.

Half of the employees had immediate eligibility for elective contributions. The eligibility period for employer contributions was typically one year.

Automatic savings design was popular

About 12% of plans had adopted an automatic enrollment feature, and nearly all of those offered a balanced fund as the default investment option. Six out of ten of these plans had a fully automated design, consisting of automatic enrollment, automatic contribution increases and a balanced or lifecycle fund as the default.

Investment options increased

In 2000, the average number of investment options was 13. By 2006, that average had risen to 20. Most of the increase was due to the addition of lifecycle funds.

About 75% of plans offered lifecycle funds in 2006 and 28% of participants invested in them.

Other findings include:

- Only 14% of participants requested an exchange between funds in 2006.
- 69% of all transactions were conducted by participants via the Internet.
- On average, participants with loans borrowed a modest 12% of their account balances.
- Upon termination or retirement, half of the participants left their assets in their employer's plan.

The full report can be viewed at http://tinyurl.com/ywtcqa.

Plan Sponsors Ask…

Q: We're planning ahead for the Form 5500 filing process and think we qualify for the small plan audit waiver. What are the requirements?

A: For small plans (generally those with fewer than 100 participants at the beginning of the plan year), the Form 5500 audit requirement is waived if the plan's assets are "qualifying plan assets" and additional participant disclosures are made in the Summary Annual Report (SAR).

Additional required disclosures include:

- the name of each "regulated financial institution" holding qualifying plan assets,
- the name of the surety company issuing the plan's fidelity bond (does not apply if 95% or more of the plan's assets are qualifying assets),
- a notice stating that participants and beneficiaries may examine statements from the financial institutions that describe the assets held, and
- contact information for the Employee Benefits Security Administration.

Note also that the plan's ERISA bond requirement may be higher than usually required if less than 95% of the plan's assets are qualifying plan assets at the start of the plan year.

For more information, such as definitions of qualifying plan assets and regulated financial institutions, see the Department of Labor's Frequently Asked Questions on this topic at http://tinyurl.com/239jev.

Q: Is there survey information available about what asset classes are popular with new 401(k) plan enrollees?

A: Yes. The Employee Benefit Research Institute's (EBRI) "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2006" report indicates that more new hires are investing in balanced funds, including lifestyle or lifecycle funds.

On average, nearly 25% of the account balances of new hires were invested in balanced funds at the end of 2006, up from 19% in 2005 and about 7% in 1998.

For perspective, the report noted that about half of all participants' account balances were in equity funds at year-end 2006. About 36% of participants had no equity funds, while 21% had more than 80% of their balances in equities.

Surprisingly, 47% of participants in their 20s had no equity funds. About 31% of those in their 40s and 42% of participants in their 60s held no equity funds.

A great deal of additional information is available in EBRI's *Issue Brief No. 308*, which is available at http://tinyurl.com/2a8a35.

Q: Does an employer match have an effect on retention of participants in automatic enrollment plans?

A: New research from the National Bureau of Economic Research suggests that plan sponsors shouldn't rely much on the match's impact on reducing participant opt-outs.

In "The Impact of Employer Matching on Savings Plan Participation Under Automatic Enrollment," the Yale University and Harvard University researchers concluded that while auto enrollment successfully raises participation rates, and those rates are related to the generosity of the match, the overall effect is "modest."

They found that decreasing the match by 1% of pay was related to a roughly 3% decline in the participation rate at six months of eligibility. They also estimated that removing a match entirely under auto enrollment would, at six months of eligibility, reduce participation by 5 to 11 percentage points.

An abstract of the study and ordering information are at http://tinyurl.com/37wulh.

401(k) Stats at a Glance

Want a quick overview of key 401(k) plan statistics? Try the Investment Company Institute's FAQs at http://tinyurl.com/bfsq6. And for a comprehensive one-page summary, see the American Benefits Council's *"401(k) fast facts"* at http://tinyurl.com/yq5vsb.

Web Resources for Plan Sponsors

Internal Revenue Service, Employee Plans
www.irs.gov/ep

Department of Labor, Employee Benefits Security Administration
www.dol.gov/ebsa

401(k) Help Center
www.401khelpcenter.com

BenefitsLink
www.benefitslink.com

BenefitNews
www.benefitnews.com

Profit Sharing/401(k) Council of America
www.psca.org

Employee Benefits Institute of America, Inc.
www.ebia.com

Employee Benefit Research Institute
www.ebri.org

Savings Progress Varies by Generation

A new study of 10 million participants in 13,000 plans demonstrates clearly how retirement savings efforts and their results differ among generations.

Plan participation rates at the end of 2006 were 67% for Baby Boomers (born 1946-1964), 58% for Gen Xers (1965-1978) and 28% for Gen Yers (1979-1991). Deferral rates for these three groups were 7.7%, 6.2% and 4.6%, respectively.

Average account balances ranged from $89,000 for Baby Boomers, $34,000 for Gen Xers and $6,000 for Gen Yers.

Broadly speaking, of greater concern were the findings that 13% of participants held no equity funds at all, 19% had their savings in just one non-diversified investment option, and 85% did not perform a portfolio rebalance in 2006.

A wide array of data on auto enrollment, average participation rates and other topics is available in the study's Highlights of Findings, at http://tinyurl.com/39411c.

Plan Sponsor's Quarterly Calendar

Consult your plan's counsel or tax advisor regarding these and other items that may apply to your plan.

JANUARY

- Send payroll and employee census data to the plan's record-keeper for plan-year-end compliance testing (calendar year plans).
- Audit fourth quarter payroll and plan deposit dates to ensure compliance with the Department of Labor's rule regarding timely deposit of participant contributions and loan repayments.
- Verify that employees who became eligible for the plan between October 1st and December 31st received and returned an enrollment form. Follow up on forms that were not returned.

FEBRUARY

- Update the plan's ERISA fidelity bond coverage according to the plan's December 31st total assets (calendar year plans). If the plan holds employer stock, the Pension Protection Act of 2006 requires increased bond coverage, up to $1,000,000, for plan years beginning January 1, 2008.
- Review and revise the roster of all plan fiduciaries, and confirm each individual's specific responsibilities and duties in writing.
- Issue a reminder memo or e-mail to participants to encourage them to review and update, if necessary, their beneficiary designations for all benefit plans.

MARCH

- Begin planning for timely completion and submission of the plan's Form 5500 and, if required, a plan audit (calendar year plans). Consider the Department of Labor's small plan audit waiver requirements.
- Review all outstanding participant plan loans to determine if there are any delinquent payments. Confirm that each loan's repayment period and amount borrowed do not violate legal limits.
- Check bulletin boards and display racks to make sure that posters and other plan materials are conspicuously posted and readily available to employees, and that the information is current.

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