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Internal Revenue Service

Treasury Secretary Timothy Geithner Announces Retirement Security Initiatives for American Families

On September 5, 2009, Treasury Secretary Timothy Geithner announced four new regulatory initiatives to help families save for retirement and reviewed two legislative proposals that were previously released. The new initiatives are explained, along with the report *Retirement Security for American Families*, on a new IRS web page - <http://www.irs.gov/retirement/article/0,,id=212061,00.html>.

The new regulatory initiatives, which will be described in more detail in articles below, will:

- expand opportunities for improving participation through automatic enrollment in 401(k) and SIMPLE IRA retirement plans,
- make it easier to save tax refunds by converting income tax refunds into I Savings Bonds,
- show how employees can save payments they would receive for unused vacation or other similar leave in their retirement plan at termination of employment as well as annually during employment, and
- help employers understand retirement plan design options and employees understand their tax-favored rollover and other savings options through revised notices to be provided upon eligibility for distribution from their retirement plans.

Included as legislative initiatives in President Obama's budget and subject to passage by Congress are the following:

- Creation of Automatic IRAs: Unless workers choose to opt out, workers without workplace retirement plans would be enrolled in IRAs through payroll deposit contributions at work. Such voluntary contributions would be matched by the Savers Tax Credit for eligible families.
- Reform and Expansion of Savers Tax Credit: The Saver's Tax Credit, which would be available to low- and middle-income working families, include those earning too little to owe income taxes, would match one half of families' savings up to \$500 per individual each year.

Automatic Enrollment Guidance Released

The IRS issued guidance to facilitate automatic enrollment in 401(k) and SIMPLE IRA plans to increase retirement savings. As part of the retirement and savings initiatives, the following was released:

- [Revenue Ruling 2009-30](#) demonstrates ways a 401(k) plan sponsor can include automatic contribution increases in its plan. This guidance enhances prior guidance released by describing two scenarios. The conclusions, based on the specific fact situations outlined in the revenue ruling, are as follows:
 - The qualified percentage requirement (including uniformity and minimum percentage requirements) pertaining to a qualified automatic contribution arrangement (QACA) or the uniformity requirement relating to an eligible automatic contribution arrangement (EACA) may be satisfied even though default contributions for all employees increase on a date other than the first day of a plan year.

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The revenue ruling states that the increases are eligible for an exception to the uniformity requirement because they apply in the same manner to all eligible employees for whom the same number of years or portions of years have elapsed since the default contributions were first made for them under the automatic contribution arrangement. In addition, the timing of the minimum percentage requirements are satisfied under the facts described because the increase default contribution applies earlier than it would otherwise be required.

- An eligible employee's default contribution percentage can automatically increase in plan years after the first plan year based, in part, on increases in the eligible employee's plan compensation as provided by the plan document. Even though this results in the nonuniformity of default contribution percentages, this is permissible since the automatic contribution arrangement is not intended to be an EACA or a QACA.
- [Notice 2009-65](#) provides automatic enrollment plan language in two sample amendments that a 401(k) plan sponsor can adopt with automatic IRS approval. The notice states that since the amendments are samples, plan sponsors are not required to adopt either amendment verbatim. Rather, the IRS encourages plan sponsors to review the plan's terms and administrative protocols and make appropriate modifications.
- [Notice 2009-66](#) includes questions and answers to help small employers add automatic enrollment to their SIMPLE IRA plans. The Department of Labor has advised the IRS that the qualified default investment alternatives under ERISA apply to the investment of contributions, including default salary reduction contributions, under a SIMPLE IRA plan. In addition, the IRS has requested comments about the necessity of issuing additional guidance on automatic contribution arrangements and SIMPLE IRAs.
- [Notice 2009-67](#) provides sample automatic contribution language that a SIMPLE IRA plan sponsor can adopt with automatic IRS approval. The IRS states that they expect to issue a revised Form 5305-SIMPLE, *Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) – for Use With a Designated Financial Institution*, that includes an automatic contribution arrangement.

More Savings Options for Tax Refunds

Currently a taxpayer can have their refund directly deposited to a traditional IRA, Roth IRA, or SEP-IRA, but not a SIMPLE IRA. Starting with the 2010 filing season, taxpayers will be able to convert their income tax refunds into I Savings Bonds.

http://www.treasurydirect.gov/indiv/products/prod_ibonds_glance.htm In future years, taxpayers will be able to purchase I Bonds for their children or grandchildren. The IRS has released questions and answers to explain this savings initiative.

http://www.irs.gov/pub/irs-tege/ibond_questions_answers.pdf

Unused Vacation or Other Similar Leave May Be Contributed to Retirement Plan

To further increase retirement savings, the IRS has issued guidance on saving payments an employee or former employee would receive for unused vacation or other similar leave in their 401(a) and 401(k) plans. This guidance does not pertain to 403(b) or 457 plans. Recognizing that many employees receive substantial cash payments for unused vacation or other similar leave at termination of employment or even annually during employment, a 401(a) plan, including a 401(k) plan, may choose to amend their plan to offer contributions in lieu of leave.

- [Revenue Ruling 2009-31](#) addresses annual contributions of payments employees would receive for unused vacation or other similar leaves to an ongoing defined contribution plan, whether as employer contributions or elective 401(k) contributions. Qualified plans may be amended to permit certain annual contributions of the dollar equivalent of an employee's unused paid time off. An employee is not required to recognize these contributions as gross income until distributed from the plan.

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- [Revenue Ruling 2009-32](#) addresses similar contributions at termination of employment. This revenue ruling states that a qualified plan may, under certain circumstances, allow employees upon termination of employment to contribute the dollar equivalent of unused paid time off to the plan. However, these contributions, taking into account any other contributions, prior deferrals and prior annual additions, cannot violate the nondiscrimination requirements of §401(k), the annual addition limits under §415(c) or the annual elective deferral limits under §401(a)(30). These contributions are not includible in the participant's gross income until distributed from the plan.

IRS Releases Guidance on Minimum Distribution Rules

The IRS recently released final regulations involving minimum distribution requirements for governmental plans, and Notice 2009-82. <http://www.irs.gov/pub/irs-drop/n-09-82.pdf> Notice 2009-82 provides guidance relating to the ability for certain plan participants to skip their required minimum distributions (RMD) for 2009 without penalty. This provision was enacted under 401(a)(9) for the 2009 distribution year from certain plans under the Worker, Retiree, and Employer Recovery Act of 2008 (WRERA). The waiver applies to the following defined contribution plans as well as IRAs: 401(a), 401(k), 403(a), 403(b), governmental 457(b) plans and IRAs. The waiver does not apply to tax exempt 457(b) plans.

Due to the waiver of 2009 RMDs, distributees may roll over any amount they received from a defined contribution plan that would have been an RMD for 2009, except for the skipped RMD permitted under WRERA, and that otherwise meets the definition of an eligible rollover distribution. Note that the skipped RMD distribution is *not* treated as an eligible rollover distribution for purposes of the following:

- requiring the plan to offer a direct rollover of that amount,
- mandatory 20% withholding, or
- providing an eligible rollover distribution notice to the distributee.

Specifically, the notice provides transition relief through November 30, 2009 for a plan being operated inconsistent with its terms and rollover relief, as well as questions and answers and sample amendments. An excellent summary of Notice 2009-82 can be found in the September 25, 2009 Special Edition of *Employee Plan News*. <http://www.irs.gov/pub/irs-tege/se092509.pdf>

- *Governmental Plans* – On September 8, 2009 the IRS published final regulations under 401(a)(9) to treat a governmental plan, within the meaning of section 414(d), as having complied with the rules of section 401(a)(9) if the governmental plan applies a reasonable and good faith interpretation of 401(a)(9). <http://www.thefederalregister.com/d/p/2009-09-08-E9-21453> This rule applies to an eligible governmental 457(b) plan as well as to a section 403(b) contract that is part of a governmental plan. Further, the regulations under section 403(b) are also amended. The effective date of the final regulations is September 8, 2009.
- *Transition Relief for Inconsistent Plan Operation* – Recognizing that many plan administrators were unable to change their 2009 RMD procedures with the enactment of WRERA in late December 2008, the notice states that a plan will not be treated as failing to satisfy the requirement that it be operated in accordance with its terms merely because, during the period beginning on January 1, 2009, and ending on November 30, 2009:
 1. distributions that equal the 2009 RMDs or that are one or more payments in a series of substantially equal distributions (that include the 2009 RMDs) made at least annually and expected to last for the life (or life expectancy) of the participant, the joint lives (or joint life expectancy) of the participant and the participant's designated beneficiary, or for a period of at least 10 years were or were not paid,
 2. participants and beneficiaries were not given the option of receiving or not receiving distributions that include 2009 RMDs, or
 3. a direct rollover option was or was not offered for 2009 RMDs or for other amounts that can be rolled over.
- *Rollover Relief for Plans* – 2009 payments to a plan participant will not be treated as ineligible for rollover if the payments equal the 2009 RMDs or are one or more payments in a series of substantially equal distributions (that include the 2009 RMDs) made at least annually and expected to last for the life (or life expectancy) of the participant, the joint lives (or joint life expectancy) of the participant and the participant's designated beneficiary, or for a period of at least 10 years. As a

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result, such payments can be rolled over, provided the other rules are satisfied. If plan participants have already received distributions in 2009 but may have been unsure of which amounts could be rolled over, the IRS has extended the 60-day rollover period for any 2009 RMD and for any additional payments that are part of a series described above, so that it ends no earlier than November 30, 2009.

- *Rollover Relief for IRAs* – The IRS is extending the 60-day rollover period for IRA owners who have already received distributions of 2009 RMDs in 2009 so that it ends no earlier than November 30, 2009. It is important to note that no more than one distribution from an IRA in 2009 will be eligible for this rollover relief.
- *Sample Amendments* – Under WRERA, a plan or contract amendment can be delayed until the last day of the first plan year beginning in 2011 (2012 in the case of a governmental plan), provided the plan or contract operates as if the amendment were in effect from its effective date.

The first sample amendment provides that the plan default that applies in the absence of a participant's or beneficiary's election will be to pay out distributions that include 2009 RMDs, and the second sample amendment provides that the plan default that applies in the absence of a participant's or beneficiary's election will be to *not* pay out distributions that include 2009 RMDs. In addition, the sample amendments provide choices regarding additional direct rollover opportunities under the plan.

- *Frequently Asked Questions* – Topics covered include timing, rollovers by nonspousal beneficiaries, the need for spousal consent, and withholding.

Long Awaited Guidance on Rollover Safe Harbor Explanations and Other Rollover Information Released

To help recipients of retirement plan distributions better understand their tax-favored rollover and other retirement savings options, the IRS has revised safe harbor explanations to be provided to those eligible for rollover distributions. According to the IRS, a key risk to lifetime savings is when employees spend their lump sum payment, instead of electing to roll over the payment to an IRA or other retirement plan. The IRS has also revised the rollover chart that provides information on where distributions from various retirement plans may be rolled. http://www.irs.gov/pub/irs-tege/rollover_chart.pdf Finally, the IRS has released guidance on rollovers from employer plans to Roth IRAs.

Revised Safe Harbor Explanations

The IRS has released Notice 2009-68, which contains two safe harbor explanations that satisfy the 402(f) requirement. <http://www.irs.gov/pub/irs-drop/n-09-68.pdf> Recipients of eligible rollover distributions are required to receive information about:

- direct rollover rules,
- the mandatory income tax withholding rules for distributions not directly rolled over,
- the tax treatment of distributions not rolled over, and
- when distributions may be subject to different restrictions and tax consequences after being rolled over.

The first safe harbor explanation applies to a distribution *not* from a designated Roth account. The second safe harbor explanation applies to a distribution from a designated Roth account. Statutory and regulatory changes are included in the model notices, which may be tailored to conform to written plan documents and administrative protocols. Model notices may be used immediately. The IRS has included a transition until the end of 2009 for prior notices that satisfied Notice 2002-3, as long as they have been modified to reflect statutory changes since Notice 2002-3 was published.

The IRS cautions that if current law changes after September 28, 2009, any provision described in a safe harbor explanation must be modified if it is not longer accurate. Finally, the IRS expects to publish a Spanish translation of these safe harbor explanations.

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Rollovers from Employer Plans to Roth IRAs

Notice 2009-75, which was released on September 8, 2009, describes the tax consequences of rolling over an eligible rollover distribution from a 401(a), 401(k), 403(a), 403(b), or governmental 457(b) plan to a Roth IRA. http://www.irs.gov/pub/irs-drop/notice_2009-75.pdf An individual must include in gross income amounts, other than after-tax contributions, that are part of the eligible rollover distribution rolled over to a Roth IRA. If an individual rolls over an eligible retirement distribution from a designated Roth account, regardless of whether it is a qualified distribution, the rollover is not includible in gross income.

Prior to January 1, 2010, only individuals meeting the income and filing status eligibility requirements may roll over an eligible retirement distribution from an eligible employer plan (other than from a designated Roth account) to a Roth IRA. According to the notice, individuals who do not meet the eligibility requirements may roll over the eligible retirement distribution into a non-Roth IRA. The non-Roth IRA can then be converted to a Roth IRA in 2010, when the income and filing status eligibility requirements will be eliminated.

Additional News from the Internal Revenue Service

The IRS has launched a web site for employers to encourage small business owners to establish retirement plans for their workers called *IRS Retirement Plans Navigator*. <http://www.retirementplans.irs.gov> When announcing the new web site, the IRS noted that it is seeking to promote compliance with tax law by providing information and resources on maintaining plans and correcting plan errors. Plan sponsors are also referred to other useful links such as the Retirement Plans Frequently Asked Questions (FAQs) and the Employer Plan Customer Account Services on www.irs.gov.

The IRS has also published a Special Edition of *Retirement News for Employers* in September 2009 to explain the *Retirement & Savings Initiatives: Helping Americans Save for the Future* discussed above. http://www.irs.gov/pub/irs-tege/rne_se0909.pdf

In addition, the IRS released the Fall Edition of *Employee Plan News*, which also covers the Retirement and Savings Initiatives. <http://www.irs.gov/pub/irs-tege/fall09.pdf> Articles on loans and hardships as well as the coordination of retirement plan limits are also included.

Department of Labor

Guidance Released on Summary Prospectus

On September 8, 2009, the Department of Labor's Employee Benefits Security Administration (EBSA) released Field Assistance Bulletin 2009-03 that describes the circumstances under which a participant-directed individual account plan may satisfy the prospectus delivery requirements of ERISA section 404(c) by furnishing a "Summary Prospectus" in accordance with requirements established by the Securities and Exchange Commission (SEC). <http://www.dol.gov/ebsa/regs/fab2009-3.html>

The new SEC rules, which are aimed at improving investor disclosure materials, provide a short form prospectus that is written in plain English with a user-friendly format. The Summary Prospectus includes key information that allows participants and beneficiaries to compare and contrast their plan investment options. If a participant or beneficiary wants additional information, the Summary Prospectus includes an Internet address to access a broader statutory prospectus along with a toll-free telephone number and e-mail address to get a paper copy at no cost.

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