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August 2007 Employee Benefits Update

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SELECT COMPLIANCE DEADLINES

Benefit Statements for Participant-Directed Plans Due August 15, 2007

The Pension Protection Act of 2006 (the "PPA") requires that participant-directed defined contribution plans provide benefit statements to participants on a quarterly basis. Pending the publication of final regulations, the Department of Labor ("DOL") issued a safe harbor of 45 days after the end of a quarter to provide the statement. Second quarter benefit statements for calendar year plans are due by August 15, 2007.

DOL Guidance on Benefit Statements Will Be Late

On July 12, 2007, DOL official Robert Doyle announced that the DOL would miss the August 17, 2007 deadline for publishing guidance on the form, content and timing requirements of the PPA's benefit statement requirement. Mr. Doyle also advised that the guidance previously published by the DOL for benefit statements was intended to be general, temporary guidance concerning "good faith compliance" only. This interim guidance, he noted, does not necessarily represent the approach that will be reflected in the proposed regulations.

As the DOL, Internal Revenue Service ("IRS") and Pension Benefit Guaranty Corporation (“PBGC”) continue to clarify the requirements for compliance under the PPA, we recommend that plan sponsors create a flexible PPA action plan to monitor both mandatory and optional changes included in the PPA.

Form 5500 Filing Deadline for Calendar Year Plans with Extensions

If a plan administrator filed a Form 5558 on or before July 31, 2007, the plan's Form 5500 filing deadline has been extended to October 15, 2007. Additionally, if the plan sponsor extended its corporate federal income tax return, the plan may be eligible for an automatic extension until September 15, 2007 if certain criteria are satisfied. Please note that Schedule P to Form 5500 has been eliminated.

When preparing Form 5500, plan sponsors may become aware of amendments that were not timely adopted. Certain late amendments can be adopted retroactively under the Voluntary Correction Program of the IRS's Employee Plans Compliance Resolution System. An abbreviated correction application permits

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certain plan sponsors to adopt certain late amendments for the nominal fee of $375 for each year in which failure to adopt occurs. The IRS recently published additional guidance regarding this abbreviated correction form, which clarified the content requirements for a complete submission.

Cycle B Determination Letter Filings Due January 31, 2008

Remedial Amendment Period Cycle B individually designed plans must be submitted for a favorable IRS determination letter no later than January 31, 2008 to rely on the extended period during which qualification amendments may be retroactively adopted. Cycle B plans include those sponsored by employers with tax identification numbers ("EINs") ending in a two or seven, as well as all multiple employer plans.

Medicare Part D Deadlines for Calendar Year Plans

All group health plans that offer prescription drug coverage to Medicare-eligible employees (under either an active plan or retiree plan) must provide the annual creditable coverage disclosure to Medicare-eligible participants and dependents no later than November 15, 2007. As we reported in our April 2007 Employee Benefits Update, CMS revised the model notices and creditable coverage guidance yet again, which means that plan sponsors should review their creditable coverage notices carefully before sending out the notices this fall. The revised guidance and model notices can be located at the CMS website.

Also, group health plan sponsors with a calendar year plan year must apply for the Medicare Part D retiree drug subsidy by October 2, 2007. A 30-day application extension is available if the extension request is filed by October 2, 2007. The subsidy application and extension should be submitted to the Centers for Medicare and Medicaid Services ("CMS") through the Retiree Drug Subsidy Center website.

Annual Multiemployer Funding Notice for Defined Benefit Plans Due September 30, 2007< for Calendar Year Plans/strong>

Plan administrators of multiemployer defined benefit plans must annually provide participants with a notice on the plan's basic financial information. Calendar year plans must furnish the notice by September 30, 2007, or within two months after the close of the plan's extension period for filing Form 5500 (if applicable). The PBGC has issued a model notice. Note that the Pension Protection Act of 2006 replaces this notice requirement with a new funding notice

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that will need to be provided within 120 days after the end of each plan year beginning with the 2008 plan year.

RETIREMENT PLAN DEVELOPMENTS

IRS Revises and Updates 403(b) Regulations

Almost three and a half years after publishing proposed regulations, the IRS published final regulations under Code section 403(b). The final regulations will likely require comprehensive changes to most 403(b) programs. Section 403(b) provides for retirement savings through tax-deferred annuity contracts or mutual fund custodial accounts for employees of public schools, tax-exempt organizations and churches. Although special or delayed effective dates apply to certain provisions of the final regulations, the regulations generally apply for tax years beginning on or after January 1, 2009.

The most significant change adopted by the final regulations is the requirement that all 403(b) programs must be maintained pursuant to a written plan document. While 403(b) programs that were subject to ERISA will likely have a written plan document, some 403(b) programs are not subject to ERISA and may not have a plan document. The final regulations mandate that the plan document satisfy the final regulations in form and operation. The written plan document, however, need not be a single document. Thus, the document may incorporate by reference the contracts under which benefits are provided to participants. Regardless of the number of documents that make up the plan document, the plan document(s) must set forth all material terms of the program and describe the allocation of program-related responsibilities among the employer, the issuer of the investment options and any other party involved.

Another significant change adopted by the final regulations is that plan sponsors may now terminate a 403(b) program, provided the termination and distribution of assets complies with the criteria established by the IRS. Upon distribution at termination, 403(b) program participants will be permitted to roll over any eligible rollover distribution to an eligible retirement plan, including an IRA.

All employers maintaining 403(b) programs must have a written plan document in place by January 1, 2009. If an employer fails to maintain a written plan document for a 403(b) program, the penalties are quite severe. Any contract or custodial account purchased by an employer that does not maintain a written plan document will not be treated as a 403(b) contract or account.

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DOL Publishes Guidance On Impact of 403(b) Regulations

In response to the IRS's final 403(b) regulations, the DOL published a Field Assistance Bulletin ("FAB") explaining the impact of the final regulations on the ERISA safe harbor for 403(b) programs. The ERISA safe harbor exempts a 403(b) program from the requirements of ERISA if the program is funded solely with employee contributions, participation is voluntary, all rights under the program are enforceable solely by the employee and the employer restricts its involvement to certain specified activities.

The DOL confirms in FAB 2007-2 that compliance with the final 403(b) regulations will not necessarily result in coverage of the program under ERISA. An employer's development and adoption of a single plan document to coordinate administration among contract or account issuers and to address applicable tax matters without reference to a particular contract or account will not cause the arrangement to fail to qualify for the safe harbor. The written plan should allocate all discretionary responsibilities to the insurance company, trustee or custodian because it would be inconsistent with the safe harbor for the employer to have responsibility for or make discretionary decisions in administering the program. Negotiation with a product provider to change the terms of its arrangement for other than tax compliance reasons would also violate the safe harbor.

Gap Period Income Required on Excess Deferrals

A recent addition to regulations under Code section 402(g) requires plans to distribute "gap period" income on distributions of deferrals in excess of the Code section 402(g) limit ("excess deferrals") for taxable years beginning on or after January 1, 2007. The "gap period" is the period beginning after the end of the taxable year in which the deferral was allocated and ending on the date of distribution. Plans must include gap period income to the extent gains or losses would be credited on the excess deferrals if the entire account was distributed. Prior regulations permitted, but did not require, plans to distribute gap period income.

The final regulations under Code sections 401(k) and 401(m) also require plans to distribute gap period income on distributions of excess contributions ("ADP") and excess aggregate contributions ("ACP") beginning with the 2006 plan year. (Prior to 2006, distribution of gap period income was discretionary.) Beginning in 2008, however, the PPA eliminated gap period income on excess contributions and excess aggregate contributions. Unfortunately, the PPA did not eliminate the gap

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period income requirement for excess deferrals.

The chart below summarizes the requirements regarding distribution of gap period income.

	Discretionary	Required	Eliminated
Excess Contributions (ADP)	Prior to 2006 Plan Year	2006 and 2007 Plan Years	Beginning with 2008 Plan Year
Excess Aggregate Contributions (ACP)	Prior to 2006 Plan Year	2006 and 2007 Plan Years	Beginning with 2008 Plan Year
Excess Deferrals ($15,500 for 2007)	Prior to 2007 Plan Year	Starting with 2007 Taxable Year	Not eliminated

Plan sponsors will need to amend their 401(k) plans to reflect these changes.

IRS Announces Anticipated Code Section 457(f) Guidance

In Notice 2007-62, the IRS announced its intent to issue guidance for "ineligible" nonqualified deferred compensation plans of state and local governments and tax-exempt entities under Code section 457, known as 457(f) plans. The anticipated guidance will define two key concepts: "bona fide severance pay plan" and "substantial risk of forfeiture." The IRS intends the guidance to be consistent with the recently-published final regulations under Code section 409A, which also applies to 457(f) plans.

A bona fide severance pay plan will have essentially the same definition as a severance pay plan under Code section 409A. Likewise, a substantial risk of forfeiture under Code section 457(f) will have the same definition as that term is defined for purposes of Code section 409A. These similarities are intended to eliminate difficult to administer differences between Code section 409A and Code section 457.

Taxpayers may rely on the anticipated guidance outlined in the Notice immediately. Because 457(f) plans must be amended to comply with Code section 409A by January 1, 2008, sponsors of these plans should consider consulting with legal counsel to determine whether the plan complies with the

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anticipated guidance and how to proceed if modifications are necessary.

Debt for Unpaid Plan Contributions Discharged in Bankruptcy

The Sixth Circuit recently held that an employer obligated to contribute to a trio of multiemployer benefit funds pursuant to a collective bargaining agreement can *discharge in bankruptcy a $99,000 debt for unpaid employer contributions owed to the funds. Board of Trustees of Ohio Carpenters Pension Fund v. Charles Bucci*, 2007 WL 1891736. Even if the employer held ERISA plan assets and could thus be considered an ERISA plan fiduciary because he failed to make the proper contributions, the court found that the employer was not considered a "fiduciary" for purposes of the Bankruptcy Code. Therefore, the employer's obligation to contribute was a contractual obligation only, which can be discharged in bankruptcy.

DOL Publishes Final LM-30 Regulations

The DOL published its final regulations revising the Form LM-30, which must be filed annually by union officials to report transactions with employers and businesses presenting conflicts of interest. The final regulations apply for fiscal years beginning on or after August 16, 2007. For most union officials, the revised Form LM-30 should be used for the 2008 fiscal year and would be due on or about March 31, 2009.

HEALTH AND WELFARE PLAN DEVELOPMENTS

EEOC Eliminates Reverse Discrimination Prohibition

The Equal Employment Opportunity Commission published a final rule updating its regulations under the Age Discrimination in Employment Act ("ADEA"), effective July 6, 2007. The DOL deleted from the prior regulations language that prohibited discrimination against relatively younger individuals, also known as reverse discrimination. Thus, the final regulations do not prohibit employers from favoring older individuals. However, the DOL clarified that the ADEA does not create an enforceable right for older individuals and does not require employers to prefer older individuals.

This amendment was prompted by the United States Supreme Court decision in *General Dynamics Land System, Inc. v. Cline*. 540 U.S. 581 (2004). In Cline, employees aged 40 to 49 sued their employer under the ADEA after the employer eliminated its obligation to pay for retiree health benefits in the future for any employee then under age 50. The Supreme Court rejected the employees' claim,

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holding that the ADEA does not prohibit an employer from taking actions that place older workers in a more favorable position.

Updated FMLA Regulations Unlikely Despite DOL Request for Comments

In December 2006, the DOL invited interested groups to comment on the Family and Medical Leave Act ("FMLA") and the regulations thereunder. At the end of June, the DOL published a report indicating that it had received more than 15,000 comments, many of which reflected disagreements over the application of the FMLA. The disagreements centered on several issues, including the definition of serious health condition, intermittent leave, notice, medical certification and the interaction between the FMLA and the Americans with Disabilities Act. Despite these disagreements, the DOL stated that it had no current plans to amend the regulations.

Tuition for College-Prep School for Handicapped Child Is Medical Expense

The IRS recently ruled that tuition for a school that assisted handicapped children with learning disabilities of a medical nature to complete college or vocational programs constituted a deductible medical care expense under Code section 213. Priv. Ltr. Rul. 200729019 (April 10, 2007). The taxpayers in this case were the parents of a severely medically handicapped child who had been diagnosed with severe developmental disorders. The child was referred to a school designed to provide her with the remedial training she required to take part in college-level or vocational programs.

Under Code section 213, ordinary education expenses are not deductible as medical care expenses. However, expenses for "special schools" can be deductible medical care expenses in certain circumstances. The IRS reasoned that the school at issue qualified as a special school because the program was designed to help the child overcome the disabilities caused by her medical condition.

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