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Know This Notice—PPA Participant Disclosures

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An underlying theme to the Pension Protection Act of 2006 (PPA) is enhancing disclosure requirements to participants. Under PPA, these new or revised disclosures cover the broad range of discussing the health of the plan, participant rights under the plan and the addition of new features to the plan.

Although the intent is to educate the participant, the numerous requirements regarding the form and timing of the disclosures may lead to administrative confusion. In an attempt to avoid this confusion, this article describes the contents, deadlines and other factors involved in PPA disclosure requirements to participants.

Automatic Enrollment Arrangements

Automatic enrollment arrangements received favorable treatment in PPA either through confirming state law preemption or through creating new arrangements. The alphabet soup of automatic enrollment arrangements (*i.e.*, ACAs, EACAs, QACAs) each require substantially the same information in the notice to participants, but there are a few subtle differences.

Automatic Contribution Arrangements (ACAs)

Under automatic contribution arrangements (ACAs), the notice to participants must contain:

- An explanation of the circumstances under which elective contributions will be made for the participant;
- The percentage of such contributions which will be made on the participant's behalf;
- The participant's right to elect to not have such contributions made or to elect to have such



contributions made at a different percentage or amount; and

- How contributions made under the arrangement will be invested in the absence of any investment election by the participant.

The notice must be provided to participants affected by the automatic enrollment within a reasonable period before the first elective contribution and within a reasonable period before each subsequent plan year. For example, if a plan administrator limits the ACA to newly enrolled participants, only those participants would be required to receive the notice. Generally, a reasonable period of time is considered at least 30 days, but not more than 90

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days, before the employee first becomes eligible and before each subsequent plan year.

Although not required to preempt state law, the plan administrator will most likely want to implement a qualified default investment alternative (QDIA) to obtain fiduciary relief. Therefore, the notice requirements discussed later in the QDIA section may be integrated into the ACA notice. Failure to provide the ACA notice subjects the plan administrator to a civil penalty of up to \$1,100 per day for each failure [payable to the Department of Labor (DOL)].

Eligible Automatic Contribution Arrangements (EACAs)

Building on the ACA notice, the notice for eligible automatic contribution arrangements (EACAs) must contain the same information as the ACA notice along with describing the participant's right to make a permissible withdrawal and the procedures to elect such a withdrawal. Furthermore, an EACA is required to use a QDIA and the QDIA notice requirements discussed later may be integrated into the EACA notice.

The proposed IRS regulations require the notice to be provided to every employee eligible under the cash or deferred arrangement, not just the participants affected by the automatic enrollment. Consequently, the notice must be provided to all participants regardless of whether the participant made an affirmative election. Similar to the ACA requirements, the notice must be given within a reasonable period before the first elective contribution and within a reasonable period before each subsequent plan year. The 30- to 90-day time period described above in the ACA section is most likely considered a reasonable period. Due to an EACA meeting the requirements of an ACA, failure to provide the EACA notice subjects the plan administrator to a civil penalty of up to \$1,100 per day for each failure (payable to the DOL).

Qualified Automatic Contribution Arrangements (QACAs)

Once again building on the ACA notice, the notice for qualified automatic contribution arrangements (QACAs) must contain the same information as the ACA notice along with the general requirements of a traditional 401(k) safe harbor notice. In contrast to an EACA, a QACA is not required to allow participants to make a permissible withdrawal. However, the plan administrator may decide to implement this feature into the QACA. If so, the EACA notice may be integrated with

the traditional 401(k) safe harbor requirements to form the QACA notice. Similar to the ACA and EACA time periods, the notice must be given within a reasonable period before the first elective contribution and within a reasonable period before each subsequent plan year. The 30- to 90-day time period described above in the ACA section is most likely considered a reasonable period. Failure to provide the notice results in the plan administrator being unable to rely on the relief provided by complying with the QACA requirements.

The IRS has provided a model notice for plans electing QACA or EACA arrangements at: www.irs.gov/pub/irs-tege/sample_notice.pdf.

Qualified Default Investment Alternatives (QDIAs)

Although normally discussed with the automatic enrollment arrangements, the qualified default investment alternative (QDIA) regulations may apply to any qualified plan allowing participant-directed investment elections. To obtain the fiduciary relief under the QDIA regulations, the notice must contain the following:

- Description of the circumstances upon which investment in the QDIA is made for the participant;
- Explanation of the participant's right to direct the investment of assets;
- Description of the QDIA, including description of investment objectives, risk and return characteristics and fees and expenses related to the QDIA;
- Description of the participant's right to transfer assets invested in the QDIA to other investment alternatives under the plan, including any restrictions, fees or expenses related to such transfer; and
- Explanation of how participants can obtain investment information concerning other investment alternatives under the plan.

Generally, notice must be furnished at least 30 days in advance of the date of first investment in QDIA or 30 days in advance of the plan eligibility date. For example, a plan with one year eligibility and semi-annual entry dates may provide the notice prior to December 1 for all participants entering the plan on the upcoming January 1. In addition, notice needs to be furnished 30 days in advance of each subsequent plan year.

An alternative is available for an immediate eligibility plan. This alternative is most relevant for a QDIA within an automatic enrollment arrangement. Obviously, it would be a challenge

to provide a newly hired employee 30 days advance notice when the intent is to have the employee become immediately eligible and contributions to begin on the next payroll. Therefore, the notice may be provided on the plan eligibility date (date of hire) provided the participant has an opportunity to make permissible withdrawals as required for an EACA. For example, an employee hired on November 15 and who immediately becomes a participant may receive the notice on this date. In addition, this employee would be receiving another copy of the notice around December 1 to fulfill the “each subsequent plan year” requirement. Fiduciary relief would be provided under the QDIA regulations as long as the participants may withdraw their contributions before 90 days.

The notice may be distributed by means traditionally approved by the IRS and DOL, including electronic media. Failure to provide the notice results in the plan administrator being unable to obtain the fiduciary relief under the QDIA regulations.

Plans Holding Publicly Traded Employer Stock

PPA also included a new code section providing diversification rights regarding publicly traded employer stock held by defined contribution plans. Although the initial notices were due in 2007, there may be a continuing obligation to provide notice to participants holding publicly traded employer stock. If a plan continues to restrict the diversification of stock until participants have reached three years of service, participants must be provided notice at least 30 days before the first date on which the participants are eligible to exercise their rights.

For example, an employee is hired on May 1, 2008 as a full-time employee. On July 1, 2009, the employee becomes a participant and all profit sharing contributions are automatically invested in employer stock. If the plan uses the hours of service method, the participant would be able to diversify his or her profit sharing account starting January 1, 2011, and notice would need to be provided prior to December 1, 2010. If the plan uses the elapsed time method, the participant would be able to diversify his or her profit sharing account on May 1, 2011, and notice would need to be provided prior to April 1, 2011.

The IRS has provided a model notice in Notice 2006-107 which may be viewed at: www.irs.gov/irb/2006-51_IRB/ar09.html.

Failure to provide the notice subjects the plan administrator to a penalty of up to \$110 per day for each failure (payable to the participant).

Defined Benefit Funding Notice

The good news ... PPA repealed the plan funding notice requirement under ERISA §4011 and removed the Summary Annual Report (SAR) requirement under ERISA §104(b)(3) for plan years beginning after December 31, 2007. The bad news ... PPA replaced the SAR requirement with a new funding notice for single employer defined benefit plans for plan years beginning after December 31, 2007. Although changes were also made for multiemployer plans, this article focuses solely on requirements for single employer plans. The notice is required to provide the following:

- Certain identifying plan information;
- A statement regarding the plan’s funding target attainment percentage for the current plan year and the two preceding plan years (actual percentage unless in excess of 100%);
- A statement of the total assets and liabilities of the plan for the current plan year and the two preceding plan years;
- A statement of the number of plan participants;
- A description of the funding policy and the asset allocation of investments under the plan;
- Explanation of any amendment, schedule increase or decrease, or event that has a material effect on the plan’s liabilities or assets for the applicable year;
- A summary of the rules governing the termination of single employer plans;
- A general description of plan benefits guaranteed by the PBGC;
- A statement that a participant may obtain an electronic copy of the annual report; and
- A statement that the plan is required to provide information under ERISA §4010.

The notice must be provided no later than 120 days after the end of the plan year relating to such notice. However, for small plans (generally 100 or fewer participants), the plan administrator is provided additional time. The notice for small plans may be provided by the filing deadline for the Form 5500. Failure to provide the

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Benefit Limits Imposed on Underfunded Plans

PPA added a new code section that placed funding-based limitations on certain benefits in single employer defined benefit plans. If the adjusted funding target attainment percentage falls below a certain amount for a given plan year, the plan may be required to limit unpredictable contingent benefits, limit increasing benefit liabilities, prohibit accelerated benefit payments and/or freeze accruals. If these restrictions are placed on the plan, written notice must be provided to all plan participants.

For example, written notice must be provided within 30 days of the plan being subject to the restrictions pertaining to limiting unpredictable contingent benefits and prohibiting accelerated benefit payments. In addition, written notice must be provided within 30 days after the valuation date for a plan year in which accruals are frozen. The notice must disclose how the participants are affected by the particular restrictions. To illustrate, if the plan prohibits accelerated benefit payments, the notice must define a prohibited payment and describe any options available to the participant.

Failure to provide the notice subjects the plan administrator to a civil penalty of up to \$1,100 per day for each failure (payable to the DOL).

Conclusion

The PPA participant disclosure rules are not that simple. Be on the lookout for the IRS and DOL to continue providing guidance regarding the PPA participant disclosures. In addition, ASPPA will continue to monitor the released guidance and provide insight whenever possible. ↗



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