EMPLOYEE BENEFITS DEVELOPMENTS MARCH 2007

Hodgson Russ Newsletter
March 16, 2007

Practices & Industries

Employee Benefits

RULINGS, OPINIONS, ETC.

Electronic PBGC premium filings now required for all plans beginning in 2007
In 2006, the Pension Benefit Guaranty Corporation (PBGC) published a rule requiring sponsors of insured defined benefit pension plans to submit their premium information filings to the PBGC electronically. Effective July 1, 2006, the new rule required sponsors of plans with 500 or more participants to electronically file premium information for plan years beginning after 2005. That new electronic filing requirement, however, now extends to all plans beginning in 2007. In other words, plans with fewer than 500 participants also must begin to comply with the electronic filing requirement for plan years beginning after 2006. The rule does not require electronic payment, only electronic filing of premium information. The electronic filing requirement also does not apply to information sponsors must file to comply with a PBGC request for information in connection with a premium compliance review. Plans may apply for exemptions on a case-by-case basis—exemptions for good cause will be granted in appropriate circumstances. Filings may be submitted through the PBGC's on-line e-filing application ("My Plan Administration Account," or "My PAA"), which is available at www.pbgc.gov. (71 Fed. Reg. 31077)

New guidance on post-PPA distribution rules
In January, the Internal Revenue Service (IRS) published Notice 2007-7, which provides guidance on a number of the qualified plan distribution provisions of the Pension Protection Act of 2006 (PPA), including the following:

Hardship distributions for medical, tuition, or funeral expenses of beneficiaries. The notice clarifies that IRC §§ 401(k) and 403(b) plans may (but are not required to) allow hardship distributions for a primary beneficiary's medical, tuition, or funeral expenses. For this purpose, a "primary beneficiary" is an individual named as a beneficiary under the plan who has an unconditional right to all or a portion of the participant's account if the participant dies.

Direct rollovers to IRAs for nonspouse beneficiaries. The notice makes it clear that qualified retirement plans, as well as IRC § 403(b) and governmental IRC § 457 plans, may (but are not required to) offer a tax-free direct rollover of a distribution to a nonspouse beneficiary's IRA—a cash distribution followed by a traditional rollover within 60 days will not work for a nonspouse beneficiary. If direct rollovers are offered to nonspouse beneficiaries, they must be offered on a nondiscriminatory basis. If a nonspouse beneficiary makes a direct rollover, the IRA will be treated as an inherited IRA and must be distributed in accordance with the minimum distribution rules applicable to inherited IRAs.

Vesting of nonelective contributions to defined contribution plans. The notice makes it clear that a plan is permitted (but is not required) to have one vesting schedule for nonelective contributions made for plan years beginning after 2006, and another vesting schedule for other nonelective contributions (i.e., pre-2007 plan year contributions) under the plan. A contribution relates to a plan year that begins before 2007 if it is allocated under the terms of the plan as of a date in that plan year and is not subject to any conditions that have not been satisfied by the end of the plan year.

Notice and consent period for qualified plan distributions. Following PPA's enactment, certain distribution notices (i.e., the special tax notice, the early distribution consent notice, and the qualified joint and survivor annuity notice) may be provided as many as 180 days before the annuity starting date. The notice clarifies that the new timing rules for these notices apply only to notices issued or distributed in a plan year beginning after 2006.

Early distribution consent notice—new content requirements. The PPA requires plan administrators to revise the early distribution consent notices that generally must be provided to participants whose vested accrued benefit exceeds $5,000 and who have not reached normal retirement age. For plan years beginning after 2006, the early distribution consent notice must now describe the consequences of failing to defer the receipt of the distribution. However, for early distribution consent notices provided prior to the 90th day after the issuance of regulations on the new notice rules, a plan administrator will be in compliance if it makes a reasonable attempt to comply with the new content requirements. Notice 2007-7 includes guidance as to what constitutes a reasonable attempt to comply with those new content requirements. For defined benefit plans, the notice should include a description of how much larger benefits will be if the commencement of distributions is deferred. For defined contribution plans, the notice should include a description indicating the investment options available under the plan (including fees) that will be available if distributions are deferred. All notices must reference the portion of the plan's summary plan description containing any special rules that might materially affect a participant's decision to defer.

CASES

Third Circuit joins Seventh Circuit in finding cash balance plans not discriminatory
Two federal district courts in the Third Circuit have found the basic design of cash balance plans not to be age discriminatory.

The first decision by the United States District Court of New Jersey involved the defined benefit plan sponsored by Dun & Bradstreet Corp., which was converted to a cash balance plan design. Judge Stanley Chesler followed and expanded on the decision of the Seventh Circuit involving the IBM personal pension plan (See *Employee Benefits Developments*, September 2006), which found that the time value of money is not sufficient to find age discrimination within a cash balance plan design. Judge Chesler deemed other cases that have found cash balance plans to be discriminatory incorrect based on their treatment of the term "accrual," a verb, as equivalent to the term "accrued," a noun. Judge Chesler stated that "… finding 'benefit accrual' to be the same as 'accrued benefit' is tantamount to equating a past process with the present result of it. It violates both language and logic…." (*Finley v. Dun & Bradstreet Corp*., D. NJ 2007)

Only four days later, the Third Circuit announced its decision involving the PNC Financial Services Group Inc. pension plan. The federal district court acknowledged there was a split of decisions within the district courts of the Second Circuit (See *Employee Benefits Developments*, January 2007) that would need to be resolved by the Second Circuit. The Third Circuit chose to follow an analysis similar to that in the Seventh Circuit decision involving the IBM personal pension plan. The federal district court also noted Congress addressed in the PPA, on a prospective basis, the age discrimination issues involving cash balance plans. While the PPA's provisions do not apply to conversions occurring before June 29, 2005, the Third Circuit found Congress could not have intended for cash balance plans to be considered discriminatory. (*Register v. PNC Financial Services Group Inc*., 3d Cir. 2007)

In a further development regarding the IBM personal pension plan case, the United States Supreme Court announced it will not review the Seventh Circuit's decision upholding the cash balance plan design. Stay tuned for further developments. (*Cooper v. IBM Personal Pension Plan*, S. Ct., cert. denied 2007)

The "shield" of ERISA

Here's a small case with an interesting lesson. An executive at Hartford Financial Services was terminated from her position. Her claim for severance benefits and other damages might have been brought as a claim for benefits under a welfare plan, but the Employee Reitirement Income Security Act (ERISA) doesn't allow for tortious damage claims. A tactic to avoid the ERISA limits on damage claims is to file a lawsuit in state court alleging breach of contract, tortious interference, intentional infliction of emotional distress, negligent misrepresentation, unjust enrichment, or other tort claims. In this case, the plaintiff used this tactic, and the employer immediately removed the case to federal district court. Finding the removal proper, the United States District Court for Connecticut rejected the plaintiff's claim that she was not suing for benefits under an ERISA plan. The plaintiff attempted to characterize the failure to pay severance benefits as an act that unjustly enriched the company and claimed that the amount of the claimed severance benefit was simply a measure of the damages resulting from this unjust enrichment. While it can be uncertain whether a severance plan is subject to regulation as an ERISA welfare plan, an employer can design a severance plan to assure ERISA coverage and shield itself from tort claims and liabilities that are precluded by ERISA. In this case, the federal district court concluded the plaintiff's claims arose under an ERISA plan and the interpretation of any rights granted under it and rejected the attempt to remand the case to state court. While a trial may still occur in this matter, the rules and procedures of ERISA may protect the employer from tort claims that could far exceed claimed benefits in an employee benefit plan. (*Curcio v. Hartford Financial Services Group, et al*., D. Conn. 2007)

Court orders employer to retroactively enroll employee in LTD plan

The United States District Court for Utah ruled an employer must retroactively enroll an employee in its long term disability (LTD) plan because the employer failed to ensure that the employee had properly enrolled when he was hired. When the employee was hired, the employer provided him with an incomplete set of enrollment materials. In addition, the employer did not notice, or help the employee correct, mistakes the employee made in filling out the enrollment forms. Later, when the employee suffered an injury and applied for LTD benefits, the LTD insurer denied the employee's application on the basis that he never properly enrolled in the plan.

The court noted the employer, which also acted as plan administrator, owed a fiduciary duty to its employee. This duty extended beyond “simply complying with the specific duties imposed by the plan documents or statutory regime; it also includes the activities that are ‘ordinary and natural means’ of achieving the ‘objective’ of the plan.” This case highlights the need for plan administrators to provide clear enrollment information to participants, to carefully review submitted enrollment forms, and to promptly address any confusing or ambiguous responses. (*Atwood v. Swire Coca-Cola USA*, D. Utah, 2007)