



Pension Analyst

Important information

Legislation

March 2009

Worker, Retiree, and Employer Recovery Act provides relief for defined contribution plans

Who's affected

This new law applies to sponsors of and participants in qualified defined benefit and defined contribution plans, including multiemployer plans, governmental plans, and church plans that do not elect to be covered by ERISA ("non-electing church plans"). It also applies to ERISA and Non-ERISA 403(b) plans and governmental section 457(b) plans.

Background and summary

On December 23, 2008, President Bush signed into law the Worker, Retiree, and Employer Recovery Act of 2008 (WRERA). This law makes several technical corrections to the Pension Protection Act of 2006 (PPA) and provides limited relief from the current economic crisis for plan sponsors and certain plan participants.

This publication discusses the impact of WRERA on defined contribution plans, including required minimum distribution (RMD) relief for 2009, as well as PPA technical corrections addressing:

- The requirement that plans permit non-spouse beneficiaries to make direct rollovers;
- The elimination of the requirement that eligible automatic contribution arrangements (EACAs) comply with the Department of Labor's (DOL's) qualified default investment alternative (QDIA) rules;
- The clarification that permissible withdrawals are not taken into account in applying the elective deferral limit;
- The elimination of the gap period income requirement for excess elective deferrals;
- The clarification that rollovers from a Roth 401(k) or Roth 403(b) to a Roth IRA are not subject to income limitations;
- Clarification on the deduction limit when an employer sponsors both a defined contribution and defined benefit plan covering one or more of the same employees.

Separate publications discuss the impact of WRERA on single-employer, multiemployer, and governmental defined benefit plans.

Action and next steps

Plan sponsors should review the information contained in this publication, and identify the provisions that apply to their plans. Although plan sponsors will not immediately need to amend their plans for the 2009 RMD relief, plan sponsors will need to notify Prudential Retirement if they would like to allow their plan participants and beneficiaries to directly roll over amounts that would otherwise be RMDs for 2009.

In this issue

[Waiver of required minimum distributions \(RMDs\) for 2009](#)

[Rollovers of RMDs](#)

[Plan amendments](#)

[Open issues](#)

[Prudential's response](#)

[Non-spouse beneficiary direct rollovers](#)

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Eligible automatic contribution arrangements (EACAs) Elimination of gap period income requirement for excess deferrals Rollovers from designated Roth account to Roth IRA Combined plan deduction limit Next Steps
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Waiver of RMDs for 2009

Generally, RMDs must begin to be made from retirement plans by April 1 of the calendar year following the later of the calendar year in which participants reach age 70½ or retire. Due to the current economic downturn, WRERA provides 2009 RMD relief for participants and beneficiaries in individual retirement accounts or annuities (IRAs) and defined contribution plans (including 401(a) plans, 403(b) plans, and governmental section 457(b) plans). As a result, no RMDs are required for distribution calendar year 2009.

Participants with a required beginning date of April 1, 2010, are not required to take a 2009 RMD. Instead, the first RMD for those participants will be their 2010 RMD, which must be made by December 31, 2010. However, participants with a required beginning date of April 1, 2009, must still take their 2008 RMDs by April 1, 2009.

The 2009 RMD relief also applies to the five-year rule applicable to beneficiaries when a participant dies before his required beginning date and the death occurred before January 1, 2009. As a result, beneficiaries will receive an extra year to receive total payouts of their account balances if the payment deadline was December 31, 2009, or later. *For example, for an account of an individual who died in 2007, the five-year period ends in 2013 instead of 2012.*

The 2009 RMD relief does not apply to nongovernmental section 457(b) plans. Participants and beneficiaries in nongovernmental 457(b) plans must receive their 2009 RMD as scheduled.

Rollovers of RMDs

In addition, WRERA permits plans to allow participants and beneficiaries to make direct rollovers to other plans or IRAs of amounts that would have been 2009 RMDs. However, those distributions are not subject to the 402(f) notice requirements and will not be subject to the 20% mandatory federal income tax withholding. As a result, if the portion that would otherwise be the 2009 RMD is paid as a cash distribution, that portion is subject to 10% federal income tax withholding, unless the participant elects out of withholding.

If a plan does not allow participants and beneficiaries to make direct rollovers of amounts that would otherwise be RMDs for 2009, these individuals will still be able to indirectly roll over the portion that would be considered an RMD within 60 days after receipt of the payment.

Plan amendments

Generally, plan sponsors have until the last day of the plan year beginning on or after January 1, 2011, to amend their plans to reflect the 2009 RMD relief. Sponsors of governmental plans have until the last day of the plan year beginning on or after January 1, 2012, to amend their plans. We expect the IRS to provide further guidance regarding the type of plan amendments required for the RMD relief, along with guidance on other outstanding issues.

Although plan sponsors do not need to immediately amend their plan documents for the 2009 RMD relief, sponsors that want to allow their plan participants and beneficiaries to directly roll over the amounts that would otherwise be considered RMDs for 2009 will need to contact their Prudential Retirement representative. Participants and beneficiaries in plans that do not permit direct rollovers of those RMD amounts will still be able to indirectly roll their distributions to an IRA or another retirement plan within 60 days of receiving payment.

Open issues

While WRERA provided some welcome relief for many participants and beneficiaries with respect to RMD payments, it also leaves a number of open issues, including:

- The type of plan amendments required for the RMD relief;
- Whether participants and beneficiaries who receive 2009 RMD payments may elect to return them to the distributing plan, even if plan provisions currently wouldn't permit the acceptance of such payments; and
- Whether all amounts that would otherwise be 2009 RMDs are eligible for rollover, or only certain types of 2009 RMD

payments are eligible for rollover.

Several industry groups have already provided comments to the IRS and requested guidance with respect to these and other open issues. In addition, the IRS has been asked to consider a “good faith” compliance standard for plan sponsors and participants until further guidance is issued. We will keep you posted as additional guidance is issued.

Prudential’s response

To assist plan sponsors in complying with the change in the RMD rules, Prudential Retirement will send letters to affected participants and beneficiaries in 401(a) plans, 403(b) plans, and governmental section 457(b) plans to notify them of their ability to request or waive their 2009 RMD payments.

Non-spouse beneficiary direct rollovers

PPA allows non-spouse beneficiaries to make a direct rollover of a death benefit payment from a qualified defined benefit or defined contribution plan, section 403(b) plan, or governmental section 457(b) plan to an IRA. These direct rollovers are available for distributions made after December 31, 2006.

IRS Notice 2007-7 provided guidance that plans were permitted, but not required, to offer these direct rollovers to non-spouse beneficiaries. However, the technical corrections in WRERA clarify that, effective for plan years beginning after December 31, 2009, plans are required to provide a direct rollover option for non-spouse beneficiaries and must provide a 402(f) notice.

For plan years beginning on or after January 1, 2009, if you have already adopted a plan amendment to allow non-spouse beneficiaries to make direct rollovers to an IRA, Prudential Retirement will permit non-spouse beneficiaries to make direct rollovers to an IRA. If you have not adopted an amendment to allow non-spouse beneficiaries to make direct rollovers to an IRA during the 2009 plan year, Prudential Retirement will not permit non-spouse beneficiaries to make direct rollovers this year. However, for plan years beginning on or after January 1, 2010, as directed by WRERA, Prudential will allow non-spouse beneficiaries to make direct rollovers to an IRA.

Eligible automatic contribution arrangements (EACAs)

An EACA is an automatic enrollment arrangement that is exempt from some of the standard distribution restrictions that apply to 401(k) plans, 403(b) arrangements, and governmental section 457(b) plans. An [EACA](#) may distribute:

- Automatic contributions made to the plan within 90 days of the effective date of a participant’s first automatic contribution, regardless of the participant’s age or ability to take standard in-service distributions; and
- Excess contributions and excess aggregate contributions to correct failed ADP and ACP tests within 6 months of the end of the plan year without subjecting the employer to a 10% excise tax.

PPA required EACA plans to comply with the Department of Labor’s (DOL) rules for a qualified default investment alternative (QDIA) when establishing a default investment fund for automatic contributions. However, WRERA contains a technical correction that eliminates this QDIA requirement.

WRERA also clarifies that permissible withdrawals are not taken into account in applying the elective deferral limit (\$16,500 in 2009).

These changes apply retroactively to plan years beginning after December 31, 2007.

Elimination of gap period income requirement for excess deferrals

In its final rules relating to designated Roth accounts, the IRS required distributions of excess deferrals from 401(k) plans or 403(b) plans made for tax years beginning on or after January 1, 2007, to include gap period income. “Gap period income” is the earnings on the distribution amounts from the end of the calendar year in which the contributions were made through the date the distribution is made.

WRERA removes the requirement to distribute gap period income on excess deferrals, effective retroactively to excess deferrals for tax years beginning on or after January 1, 2007. This provision is consistent with the PPA provision that removed the gap period income requirements for ADP and ACP test corrective distributions.

For excess deferrals distributed after December 31, 2008, Prudential will pay gap period income if required by your plan document.

Rollovers from designated Roth account to Roth IRA

Beginning in 2008, PPA allows a participant to directly roll over his "eligible rollover distribution" from a qualified plan, 403(b) plan, or section 457(b) plan into a Roth IRA, as long as the participant's adjusted gross income (AGI) is \$100,000 or less. While this provision succeeded in removing many of the barriers for rolling dollars to a Roth IRA, PPA did not provide an exclusion from the AGI limitation for direct rollovers from Roth 401(k) or Roth 403(b) accounts. As a result, a participant was restricted from rolling over designated Roth 401(k) or Roth 403(b) contributions to a Roth IRA if his AGI exceeded \$100,000.

WRERA clarifies that direct rollovers from a Roth 401(k) or Roth 403(b) account to a Roth IRA are not subject to these income limitations.

Combined plan deduction limit

A special combined plan contribution deduction limit applies when an employer sponsors both a defined contribution plan and a defined benefit plan covering one or more of the same employees. This limit is the greater of: (1) 25% of compensation paid or accrued during the plan year, or (2) the contribution needed to meet minimum funding requirements.

Effective for contributions made for tax years beginning on or after January 1, 2006, PPA provided that this combined plan limit does not apply if the defined contribution plan contributions do not exceed 6% of compensation for beneficiaries under the plans. However, in 2007, the IRS [took the position](#) that even if defined contribution plan contributions do not exceed 6% of compensation, the combined plan limit would still apply to the defined benefit plan. WRERA clarifies that if contributions to a defined contribution plan are less than 6% of compensation, the defined benefit plan is not subject to the overall deduction limit. If contributions to a defined contribution plan exceed 6% of compensation, only contributions in excess of 6% are counted toward the combined limit. This provision is effective retroactively to contributions made for tax years beginning after December 31, 2005.

Next steps

In general, sponsors of defined contribution plans, including ERISA and non-ERISA 403(b) plans, have until the last day of the plan year beginning on or after January 1, 2011 to amend their plans for the 2009 RMD relief. Sponsors of governmental plans have until the last day of the plan year beginning on or after January 1, 2012 to make these amendments.

Plans that have not already adopted an amendment to allow non-spouse beneficiaries to make direct rollovers to an IRA should do so by the last day of the plan year beginning on or after January 1, 2010, unless a later deadline is provided by the IRS. Sponsors of governmental plans have until the last day of the plan year beginning on or after January 1, 2011 to make these amendments. The IRS may provide further clarifications in the future regarding these amendment deadlines.

If Prudential Retirement provides document services for your plan, we will work with you to ensure that your document complies with the applicable amendment deadlines.

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Pension Analyst by Prudential Retirement

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