

401(k) Supreme Court Case

Until recently, federal courts had consistently maintained that ERISA, the federal law that governs qualified retirement plans, provides remedies for losses resulting from a fiduciary breach only on behalf of entire plans rather than on behalf of individual participants. Thus, plan participants could only sue for “recovery on behalf of the plan, as a whole.”

The court decisions generally relied on a Supreme Court ruling in *Massachusetts Mutual Life Ins. Co. v. Russell* (473 U.S. 134 (1985)). But the recent Supreme Court decision in *LaRue v. DeWolff* (No. 06-856, February 20, 2008) had a different outcome.

Supreme Court Decision. In a 9-0 decision, the Supreme Court ruled that ERISA allows a participant in a defined contribution plan to sue for reimbursement of investment losses. The losses suffered by the participant’s individual account in the case (which occurred during a market downturn in the early 2000s) resulted from a failure of the plan fiduciaries to follow investment directions. Prior to the downturn, the participant instructed the employer to make changes to his investment allocations. However, these instructions were not executed. As a result, the participant’s account lost \$150,000 before either party realized what had occurred.

In *LaRue*, a plan participant sought to make his individual account whole. The employer argued that this was not what was meant by recovery on behalf of the plan. The trial and federal appeals courts ruled in favor of the employer based on *Russell*. However, the Supreme Court disagreed.

The Supreme Court found that while ERISA does not provide a remedy for individual injuries as distinct from plan injuries, it does authorize recovery for fiduciary breaches that impair the value of plan assets. In the defined contribution context, this means restoring the losses in a particular participant’s individual account. The court unanimously agreed that if an employer fails to follow a participant’s investment direction and the participant’s retirement benefit is reduced as a result, then, as fiduciary, the employer is responsible. Thus, the Supreme Court’s decision abides by the principle of making the plan and, thus, the participant “whole.”

The Majority Opinion. Justice Stevens cited fiduciary responsibility in accordance with ERISA Section 409(a):

“Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this title shall be personally liable to



make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary. A fiduciary may also be removed for a violation of section 411 of this Act.”

(Continued on page 2)

CONTENTS

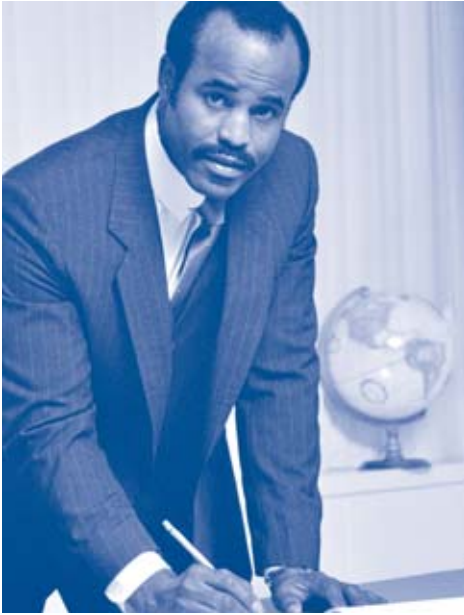
[401\(k\) Supreme Court Case](#)

[EGTRRA Opinion Letters](#)

[Deadline for Depositing Deferrals](#)

[Recent Developments](#)

401(k) Supreme Court Case (Continued from page 1)



Justice Stevens stated that a “defined contribution plan” promises the participant the value of an individual account at retirement. The balance in that

account is a function of how much the participant contributes and the investment performance of those contributions. In *LaRue*, the employer’s failure to execute the participant’s investment directions resulted in the reduction of the participant’s retirement account balance. Thus, the employer’s conduct constituted a breach of fiduciary duty for which the employer could 1) be held responsible and 2) be required to make the participant whole under ERISA. Therefore, whether such a fiduciary breach affects all participants or only one, it creates the type of harm that is an issue under ERISA Section 409(a).

Fiduciary Responsibility Unchanged.

The fact that this case may open up the employer (as plan fiduciary) to lawsuits cannot be dismissed. However, the fiduciary requirements have not changed.

Employers as fiduciaries must continue to comply with the fiduciary responsibilities inherent in a qualified plan and act diligently to protect the assets of the plan. Responsibilities include:

- Using plan assets solely for the benefit of the participants and beneficiaries (the exclusive benefit rule),
- Exercising prudence in investment choices and diligence and care on behalf of the participant (the prudent person rule), and
- Creating an investment policy statement and reviewing it periodically.

For more information on fiduciary responsibilities, the Department of Labor has compiled a booklet entitled “Meeting Your Fiduciary Responsibilities.” It can be found at: www.dol.gov/ebsa/pdf/fiduciaryresponsibility.pdf. ❖

EGTRRA Opinion Letters

On March 31, 2008, the IRS began issuing EGTRRA Opinion Letters for prototype and volume submitter defined contribution plans and announced that employers using these plans have until April 30, 2010, to adopt them.

Six-year Cycle. The EGTRRA document is the first to be approved under the IRS’s new six-year restatement cycle for preapproved plans, which started in 2005. It calls for plans to be restated every six years, submitted to the IRS for a new Opinion or Advisory Letter, and, once approved, adopted by employers.

As part of the cyclical process, the IRS issues an annual list of items that must be incorporated into plans that are being submitted for approval the following year. The EGTRRA document just approved contains the required changes from the 2004 IRS Cumulative List (issued as IRS Notice 2004-84), including EGTRRA changes, the final required minimum distribution rules, the final 401(k) and (m) regulations, and more.

Incorporating Changes. Changes that have occurred since Notice 2004-84 was issued are not included in the document.

Those — and any subsequent changes — will be included in the next six-year restatement cycle. However, the IRS requires that changes between restatements be incorporated into the plan document as “snap-on” *interim* amendments. For example, the final 415 regulations (issued in 2007) will be a required snap-on amendment that will apply to limitation years beginning on or after July 1, 2007. In addition, there will be a snap-on amendment for the Pension Protection Act of 2006 (PPA).

Note: Plans must operate in accordance with PPA provisions, even though documents will not be amended until sometime in 2009. ❖

Deadline for Depositing Deferrals


Every year, the Department of Labor (DOL) devotes significant resources to investigating cases involving the delinquent deposit of employee contributions. As a matter of fact, close to 90% of the applications under the DOL's Voluntary Fiduciary Correction Program involve deposit deadline violations. This past February, the DOL took steps to resolve the problem by providing long-awaited guidance in the form of proposed regulations that clarify the deposit deadline.

The Basic Rule Is Unchanged. The general rule for depositing plan deferrals has not changed. Amounts withheld by an employer must become plan assets “as soon as possible,” which technically means on the earliest date on which the amounts can reasonably be segregated from the employer's general assets. But it's difficult to know exactly when a deposit is late under this as-soon-as-possible requirement. Advisors as well as plan sponsors have been uncertain about how to satisfy this requirement. And employers were often unaware that they potentially engaged in a prohibited transaction if they took even one day longer than normal to make a deposit.

New Clarification. The proposed regulations offer a “seven-business-day safe harbor” for employers with small plans (less than 100 participants as of the first day of the plan year) to make deposits to their plans. The actual deadline would be the seventh business day following the day that amounts would have been payable to the participant in cash *or* received by the employer to repay a participant loan. The funds do not have to be allocated to participant accounts within the seven-day time frame or even invested: They need only be deposited in a plan account.

The DOL's new guidance is extremely helpful. It provides a much higher degree of certainty with respect to the timeliness of deferral (and loan repayment) deposits. Before deciding on the proposed time frame, the DOL performed a number of studies and considered five- and 10-day deadlines. The seven-day rule seemed easiest to implement.

Example: Acme Enterprises sponsors a 401(k) plan. There are 30 participants in the 401(k) plan. **Acme** has one payroll

A hand is shown dropping a coin into a stack of five coins. The coins are stacked vertically, and the hand is positioned above the top coin, with the coin being released. The background is a light blue gradient.

period for its employees and uses an outside payroll processing service to pay employee wages and process deductions. **Acme** has established a system under which the payroll processing service provides payroll deduction information to **Acme** within one business day after paychecks have been issued. **Acme** checks this information for accuracy within five business days and then forwards the withheld employee contributions to the plan. The total amount of the withheld employee contributions is deposited with the trust maintained under the plan on the seventh business day following the date on which the employees are paid. Under the DOL's proposed safe harbor, when participant contributions are deposited with the plan by the seventh business day following a pay date, the contributions are deemed to be contributed to the plan on the earliest possible date on which such contributions can reasonably be segregated from **Acme's** general assets.

Note: According to reports, DOL auditors are interpreting the rules as follows: If a plan complies with the seven-day period, fine. If not, penalties apply starting after three or five days — not seven — from when deferrals were withheld.

Effective Date. The new rules will go into effect when the final regulations are published in the Federal Register. *Nonetheless, small plans may begin taking advantage of the seven-business-day safe harbor period provided in this proposal right away.* ❖

recent developments

■ **Qualified Optional Survivor Annuity (QOSA).** Effective for plan years starting on January 1, 2008, and thereafter, the Pension Protection Act of 2006 (PPA) has amended the qualified joint and survivor annuity (QJSA) rules. Plans subject to these annuity requirements must now offer participants a qualified optional survivor annuity (QOSA) and a written explanation of the terms and conditions of the QOSA.

What this generally means is that a plan that is subject to the QJSA requirements must now provide participants with additional options regarding the spouse's survivor annuity. Under the new QOSA provisions, if a plan normally provides a survivor annuity that is equal to or greater than 75% of the annuity amount payable during the joint lives of the participant

and his or her spouse, then the participant must be given the option to elect a survivor annuity of 50%. Similarly, if the normal amount of the survivor annuity is 50%, the participant must be given the option to choose a 75% annuity. The QOSA must be at least actuarially equivalent to a single life annuity payable at the same time as the QOSA. It is important to note that the QOSA does not have to be actuarially equivalent to the plan's QJSA.

In general, the QOSA requirement applies to distributions with annuity starting dates in plan years beginning after December 31, 2007. (There is a special rule for collectively bargained plans.) Plans must operate under this PPA provision but do not have to be amended until 2009. Plans, including many prototype plans, that have a QJSA with a 50% survivor annuity

and provide an option for 75% do not need to be amended because the QOSA requirements are already satisfied.

■ **IRS Videos Available Online.** The IRS has made a number of video clips available online via the Retirement Plans Community web page at www.irs.gov/ep. These short videos provide useful information on a number of topics of interest to both employers and participants. Videos of interest to employers include *Maintaining Your Plan* (which provides tips on what employers/sponsors can do to keep their retirement plan healthy), *IRS Enforcement Priorities*, *Stopping Abuses in Retirement Plans*, *Self-Correcting Plan Mistakes* (a discussion of self-correction for common plan mistakes), and *Fixing Plan Mistakes Found During an IRS Audit*. *Increasing Your Retirement Savings* and *Managing Your IRA* may be of interest to participants. ❖

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