

# TRISTAR PENSION CONSULTING

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Participants are on a Need to Know  
Basis...and They Need to Know

- Introduction
- Notices Required for all DC Plans
  - Summary Plan Description (SPD) and Summary of Material Modification (SMM)
  - Summary Annual Report (SAR)
  - Participant Benefit Statement
  - Beneficiary Designation Forms
  - Fee Disclosure
- Provision-Specific Notices
  - Automatic Enrollment Notice
  - Safe Harbor Notice
- Investment Disclosures
  - Qualified Default Investment Alternative (QDIA) Notice
  - Diversification of Employer Securities
  - 404(c) Disclosure
- Event-Driven Notices
  - Distribution Notices
  - Participant Loans
  - Blackout Notice
- It's Not Easy Being Green
- Conclusion

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It seems that every time you turn around, you are required to provide yet another notice to the participants in your company's retirement plan. While plan-related notices are not a new phenomenon, the Pension Protection Act (PPA) took the concept to a different level by mandating a host of new notices.

Sponsors of 401(k) plans face the task of providing as many as 40 or more different notices. Some apply to all defined contribution (DC) plans and others are plan-design or event driven. While opinions differ on the most effective method to help employees understand this deluge of information, the focus of this article is how to satisfy the regulatory notice requirements to keep your plan in compliance.

## **NOTICES REQUIRED FOR ALL DC PLANS**

All ERISA-covered, DC plans must provide certain notices regardless of the provisions they contain.

### **SUMMARY PLAN DESCRIPTION (SPD) AND SUMMARY OF MATERIAL MODIFICATION (SMM)**

The SPD is a "plain English" summary of a plan's provisions. All SPDs must describe the following:

Eligibility;

Contributions;

Vesting;

Distributions; and

Plan contact information.

The SPD must be distributed within:

90 days of initial eligibility;

120 days of the plan becoming subject to ERISA; and

30 days of receipt of a written request.

Sponsors must generally update their SPDs at least once every five years. For amendments between updates, participants must receive an SMM describing the change. Although the deadline for the SMM is the 210th day of the year following the year the amendment is adopted, it is a best practice to notify participants of the change as soon as possible.

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The Department of Labor (DOL) can assess a sponsor penalty of up to \$1,100 per day if an SPD/SMM is late to a single participant. Failure to provide an SPD/SMM within 30 days of a participant's written request may entitle the participant to up to \$110 per day.

### **SUMMARY ANNUAL REPORT (SAR)**

The SAR provides a snapshot of the financial schedules attached to Form 5500. The SAR advises participants of their rights to additional related information and how to contact DOL if they have further questions. The deadline to distribute the SAR is two months following the due date (with extensions) for filing Form 5500.

### **PARTICIPANT BENEFIT STATEMENT**

The participant benefit statement summarizes activity in a participant's account for a given time period. Generally, each statement must include the following information:

Beginning account balance;

Contributions and/or distributions;

Investment gain or loss;

Ending account balance;

Vesting;

Statement regarding importance of diversification;

Description of each asset in which funds are invested; and

DOL website for more information.

Plans that allocate profit sharing contributions using permitted disparity must include a detailed description of the allocation method.

A plan's investment arrangement dictates the frequency with which statements must be provided. If any portion of the plan has participant-directed investments, statements must be provided within 45 days of the close of each quarter. For trustee-directed plans, the statement is due annually by the deadline for filing Form 5500. The penalty for late statements is \$100 per day per participant.

Some participant-directed plans are valued only once each year. Such plans are still required to provide quarterly statements based on the most recently available information. That may result in participants receiving the exact same statement four times throughout the year.

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## **BENEFICIARY DESIGNATION FORMS**

While not official notices, beneficiary designation forms are extremely important plan documents. A number of beneficiary disputes are litigated each year in the federal Circuit Courts of Appeals. To lessen the chance of this type of litigation, sponsors should ensure all participants complete beneficiary designation forms and update them any time they experience a "life event" such as a marriage, divorce, etc.

## **FEE DISCLOSURE**

Congress and DOL have recently focused attention on fee transparency in retirement plans. While there is no formal requirement at this time, it is anticipated that in the near future, plans will be required to distribute notices describing the fees allocated to each participant's account each quarter.

## **PROVISION-SPECIFIC NOTICES**

A plan can include provisions that subject it to additional notice requirements. For example, 401(k) plans must provide information related to salary deferrals while non-401(k) plans do not.

## **AUTOMATIC ENROLLMENT NOTICE**

Plans that include automatic enrollment must notify participants of:

The default deferral rate;

Their right to defer a different amount or not at all; and

The default investment to be used if they do not make an investment election.

The notice is due 30 to 90 days prior to initial coverage by the automatic enrollment feature and 30 to 90 days before the start of each subsequent plan year. Plans that provide eligibility on date of hire or very shortly thereafter can provide the notice on an employee's hire date.

## **SAFE HARBOR NOTICE**

There are four types of safe harbor 401(k) plans and all are required to notify participants 30 to 90 days prior to the start of each plan year. The notice must describe the plan's contribution, distribution and vesting provisions. Failure to timely provide the safe harbor notice is an operational failure that can subject the plan to disqualification.

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## **INVESTMENT DISCLOSURES**

Defined contribution plans allowing participants to direct the investment of some or all of their accounts must provide notices that inform and educate participants on the options available to them.

### **QUALIFIED DEFAULT INVESTMENT ALTERNATIVE (QDIA) NOTICE**

Participant-directed plans must specify the investment option to be used as the default when a participant does not make an election. Plan sponsors selecting a QDIA as their default must inform participants of the fund selected and notify them of their right to select a different option. The notice must be provided at least 30 days before the initial default investment and 30 days prior to the start of each subsequent year.

### **DIVERSIFICATION OF EMPLOYER SECURITIES**

Certain publicly traded companies that include employer stock as an investment option must notify participants of their right to diversify their accounts and the importance of maintaining a well-diversified portfolio. This notice is due 30 days before a participant becomes eligible to diversify. Delinquent notices are subject to a penalty of \$100 per day per participant.

### **404(C) DISCLOSURES**

Fiduciaries that seek to avail themselves of the ERISA 404(c) safe harbor must provide additional participant disclosures including:

List of investment options including general description of risk/return characteristics;

List of investment managers;

Description of fees;

Limitations on the exercise of voting rights; and

Contact information for a responsible plan fiduciary.

## **EVENT-DRIVEN NOTICES**

Some notices are required on the occurrence of certain events or transactions.

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## **DISTRIBUTION NOTICES**

When participants request distributions, there are several documents that must be provided before and after the date of distribution.

Rollover Notice and Special Tax Notice: describes participants' rights and the tax implications of electing a rollover in lieu of cash. Due 30 to 180 days prior to the date of actual distribution.

Form 1099-R: Due by January 31st of the year following the year of distribution.

Although the IRS recently updated its sample Special Tax Notice, it does not include the rollover notice. Plan sponsors should either incorporate the mandatory rollover language or provide a separate notice to satisfy this requirement.

The pre-distribution paperwork for plans providing automatic IRA rollover of vested balances under \$5,000 must notify employees of the financial institution and investment option to be used as well as any associated fees.

## **PARTICIPANT LOANS**

In order to qualify for the prohibited transaction exemption for participant loans, the plan must provide the following items when a participant requests a loan:

Participant loan program (if not included in the SPD);

Loan application;

Promissory note;

Amortization schedule;

Irrevocable pledge; and

Truth-in-lending disclosure (not required for loans issued after July 1, 2010).

## **BLACKOUT NOTICE**

A blackout period occurs when participants' access to their accounts is restricted for more than three consecutive business days. In response to several corporate scandals involving 401(k) plans, a notice is now required at least 30 days prior to the start of the blackout. The notice must identify the beginning and ending week, explain rights and investments affected and advise as to the prudence of a diversified portfolio.

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There is a penalty of \$100 per day per participant for failure to give notice, and the failure must be reported on Form 5500.

## **IT'S NOT EASY BEING GREEN**

Many companies are making efforts to "go green" by using electronic communication in lieu of paper. The IRS and DOL permit electronic delivery of most notices to employees who access the electronic delivery system as part of their jobs. Since participant disclosures must generally be "pushed" to employees rather than posted in a common location, providing kiosks to access notices does not satisfy this requirement. Participants without job-related access can follow a detailed process to consent to e-delivery. Employees not fitting into one of these categories must receive hard copy notifications.

## **CONCLUSION**

These are only a few of the many notices plan sponsors and participants must juggle. There are additional notices for plans that map investments when changing service providers, request a determination letter from the IRS or permit distributions in the form of annuities. Several industry organizations are working with the government agencies to identify more efficient and effective methods to communicate retirement benefits to employees. In the meantime, your participants are on a need to know basis...and they need to know!

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