

IRS and Treasury Release New Guidance Aimed at Improving Retirement Savings

September 29, 2009

On September 5, the Internal Revenue Service (IRS) and the Department of Treasury issued new guidance as part of the Obama administration's initiatives aimed at retirement and savings. The guidance, issued in the form of four notices and three revenue rulings, is intended to make saving for retirement easier by expanding savings opportunities in employer-sponsored retirement plans through a better explanation of rollover options, contribution of payments for unused leave, and updated model language for automatic enrollment programs. The guidance will require action on the part of plan sponsors before January 1, 2010.

New Safe-Harbor Tax Notices—Changes Required by January 1, 2010

The guidance provides updated model safe-harbor tax notices that plan sponsors may provide to participants eligible to roll over a distribution from a qualified plan with or without designated Roth accounts. The updated model notices are intended to simplify the distribution options for participants and encourage tax-free rollover options; they also update the information to reflect changes made through the Economic Growth and Tax Relief Reconciliation Act of 2001, the Pension Protection Act of 2006, and the Worker, Retiree, and Employer Recovery Act of 2008.

Plan sponsors may continue to use the existing model notices through December 31, 2009, but should begin using the new model notices by January 1, 2010. As with prior model notices, these too may be modified to suit specific plan terms and procedures.

Contributions of Paid Time Off

Under this guidance, plan sponsors will be permitted to amend plans to provide methods by which employees may contribute unused paid time off to qualified retirement plans, on a tax-deferred basis, through conversion of the value of unused leave to additional contributions to a qualified 401(k) plan, profit-sharing plan, or stock bonus plan. These contributions can be made either annually by current employees or at termination of employment, or both. As with other deferral contributions, these contributions will be subject to the annual deferral (\$16,500 in 2009) and annual addition (\$49,000 in 2009) limits and must satisfy the nondiscrimination requirements. The guidance explains how these requirements apply to paid time off contributions. Safe-harbor plans, which are currently exempt from certain nondiscrimination testing, will generally be required to conduct testing for these additional

deferrals, as the deferrals will vary for each participant, and thus use of this approach in a safe-harbor plan may be undesirable. In addition, employers with a “use it or lose it” vacation policy should consider the economic implications of this approach.

Automatic Enrollment

The guidance simplifies the addition of an automatic enrollment option in 401(k) plans by providing sample plan amendments. The guidance also confirms that qualified plans may automatically increase amounts contributed on behalf of participants under these arrangements. The sample plan amendments must generally be adopted by the later of the end of the plan year in which the amendment is effective or the last day of the first plan year beginning on or after January 1, 2009. Employees affected by these changes must receive notice in advance of the amendment effective date.

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