

WORKER, RETIREE, AND EMPLOYER RECOVERY ACT OF 2008

Signed into law in late December 2008, the Worker, Retiree, and Employer Recovery Act of 2008 (the "Act") includes technical corrections to the Pension Protection Act of 2006 (PPA), along with short-term relief to help individuals and plan sponsors cope with the recent economic turmoil. Here are some highlights of the Act.

RMDS WAIVED

The Act waives "required minimum distributions" (RMDs) from tax-deferred retirement accounts – including 401(k)s, 403(b) tax-sheltered annuities, 457(b) governmental plans, individual retirement accounts (IRAs), and others. The waiver applies to RMDs for calendar year 2009 only for plan participants, IRA owners, and designated beneficiaries.

Under the tax law's RMD rules, individuals generally must take RMDs from their plan accounts annually after reaching age 70½ or pay a 50% tax penalty on the amount that should have been withdrawn but wasn't.* In most cases, the deadline for a plan participant's first RMD is April 1 of the year following the year the participant turns 70½. RMDs for each subsequent year must be taken by December 31 of that year.

The new law provides that participants who turn age 70½ in 2009 will not have to take their first RMD – technically, the RMD for 2009 – by April 1, 2010. Instead, the first RMD will be for 2010, and the deadline for taking it will be December 31, 2010. Participants who have already begun taking RMDs may skip their 2009 RMD. But, if they do take a withdrawal in 2009 that is not an RMD for 2008, they may be able to roll over the withdrawn amount into an IRA or other eligible retirement plan. Beneficiaries who are receiving distributions over a five-year period may waive the distribution for 2009, effectively extending the distribution period to six years.

The Act provides no relief to individuals who turned 70½ in 2008. These taxpayers are still required to take their 2008 RMDs by April 1, 2009. RMDs will resume for all for 2010, and they must be taken by December 31, 2010.

NONSPOUSE ROLLOVER OPTION REQUIRED

PPA allows plans to offer a nonspouse beneficiary the option to directly roll over an eligible rollover distribution to an IRA set up to receive the distribution on behalf of the beneficiary. The Act requires employers that sponsor 401(k), 403(b), and 457(b) plans to offer this option for plan years beginning after December 31, 2009. Sponsors must provide nonspouse beneficiaries with a Section 402(f) notice explaining the tax options for distributions.

EACA DEFINITION BROADENED

Under PPA, automatic contributions to eligible automatic contribution arrangements (EACAs) had to be invested in a qualified default investment alternative (QDIA) as prescribed by U.S. Department of Labor regulations, unless otherwise directed by the participant. Participants in EACAs could make "permissible withdrawals" within 90 days of the date the first automatic contribution was made to the participant's EACA.

"...the technical corrections to PPA are generally effective as though they were included in PPA."

The Act repeals the QDIA requirement for EACAs. It also broadens the definition of applicable plan to include SIMPLE IRAs and Simplified Employee Pension (SEP) plans that have a salary reduction arrangement (SARSEPs) and makes permissible withdrawals available to participants in these plans.

COMBINED PLAN DEDUCTION LIMIT CLARIFIED

For employers with both a defined benefit plan and a 401(k) or other defined contribution plan, the Act clarifies that, if contributions to the defined contribution plan do not exceed 6% of compensation, the defined benefit plan is not subject to the combined plan deduction limit. If contributions to the defined contribution plan exceed 6% of compensation, only

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FIRST QUARTER
2009

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the contributions in excess of 6% of compensation count toward the combined deduction limit.

OTHER PPA CORRECTIONS

The Act clarifies that the income restriction on rollovers to a Roth IRA does not apply to rollovers from a designated Roth account under a 401(k) or 403(b) plan to a Roth IRA. In addition, the Act repeals the requirement that “gap period income” (the income from the last day of an employee’s taxable year to the date an excess deferral distribution is made) be calculated and distributed to employees along

with the excess deferrals. It also provides relief to underfunded pension plans by adjusting the phase-in to PPA’s new full funding rules.

With the noted exceptions, the technical corrections to PPA are generally effective as though they were included in PPA.

** Some plans allow employees who are still working for the employer that sponsors the plan when they reach age 70½ to delay the start of RMDs until after retirement, provided the employee is not a 5% owner of the employer.*

403(b) UPDATE

In 2007, the IRS issued comprehensive regulations that are designed to bring 403(b) plans more in line with 401(k) plans. In response to the difficulties some 403(b) plans were having with putting a written plan document in place by January 1, 2009, as required by the regulations, the IRS has released a notice providing some relief.*

MORE TIME TO MEET WRITTEN PLAN REQUIREMENT

The final regulations generally require 403(b) plans to have a written plan document. The IRS has extended the written document deadline by a year to December 31, 2009.

The notice says that the IRS will not treat a 403(b) plan as failing to satisfy the final regulations or Internal Revenue Code Section 403(b) for the 2009 calendar year if the sponsoring employer:

- ▶ Adopts a written 403(b) plan that satisfies the final regulations on or before December 31, 2009
- ▶ Operates the plan in accordance with a reasonable interpretation of Section 403(b), taking into account the final regulations
- ▶ Before the end of 2009, makes its best effort to retroactively correct any operational failure during the 2009 calendar year to conform to the terms of the written plan, with such corrections to be based on the general principles of correction found in the IRS’s Employee Plans Compliance Resolution System (EPCRS)

In granting the extension, the IRS noted that, other than through a private letter ruling, there is no current program under which an employer can obtain

assurance that the written form of its plan satisfies Section 403(b). The IRS plans to issue further guidance, including a prototype plan program and a determination letter program for individually designed 403(b) plans. These programs will include a means for plans to make remedial amendments to retroactively fix plan provisions. The IRS also plans to modify the EPCRS to include additional 403(b) issues.

OTHER REQUIREMENTS ARE IN EFFECT

Employers that sponsor 403(b) plans need to be aware that other provisions of the final regulations are now in effect. These include, among others, the requirements that:

- ▶ Employer contributions (contributions other than a participant’s elective deferrals) and after-tax employee contributions satisfy certain nondiscrimination rules similar to those for 401(k) plans
- ▶ 20% federal income-tax withholding be applied to any eligible rollover distribution that is not directly rolled over to an IRA or another employer plan accepting 403(b) rollovers
- ▶ Employees receiving a distribution be provided a 402(f) notice explaining the tax options for distributions

If you would like to review your 403(b) plan provisions and discuss how the regulations affect the administration of the plan, please contact us.

** Notice 2009-2, 2009-IRB, IR 2008-140*

The general information in this publication is not intended to be, nor should it be, treated as tax, legal, or accounting advice. Additional issues could exist that would affect the tax treatment of a specific transaction and, therefore, taxpayers should seek advice from an independent tax advisor based on their particular circumstances before acting on any information presented. This information is not intended to be, nor can it be, used by any taxpayer for the purpose of avoiding tax penalties.

ANSWERING YOUR FIDELITY BONDING REQUIREMENTS QUESTIONS

As a retirement plan sponsor, you should be aware that every person who handles the property or funds of the plan must be bonded. The U.S. Department of Labor's Employee Benefits Security Administration (EBSA) has issued a field assistance bulletin (FAB) that provides guidance on fidelity bonding requirements. Understanding these requirements fully will help protect your plan and your business.

The bulletin includes the following information about applying the fidelity bonding requirements.

What is the purpose of a fidelity bond? The purpose of a fidelity bond is to protect your organization's retirement plan from risk or loss due to acts of fraud or dishonesty by individuals handling the plan's assets. These acts include theft, embezzlement, and forgery.

Who must be bonded? Generally, plan fiduciaries and any other person who handles plan funds or other property (a "plan official") must be bonded. For example, officers and employees of the plan or plan sponsor who handle the receipt, safekeeping, and disbursement of plan funds are subject to bonding. Service providers and fiduciaries don't need to be bonded if they don't handle plan funds or property. Several specific exemptions also are included in the pension law.

What is meant by "handling" plan funds? Generally, "handling" plan funds refers to activities that pose a risk that the funds or property could be lost in the event of fraud or dishonesty, such as:

- ▶ Physical contact with cash or checks
- ▶ Power to transfer funds or property from the plan to oneself or a third party
- ▶ Authority to direct disbursement
- ▶ Authority to sign checks or other negotiable instruments over activities that require bonding
- ▶ Supervising or decision-making responsibility over activities that require bonding

How much coverage must the bond provide? Each plan official must be bonded in an amount equal to at least 10% of the amount of funds he or she handled in the previous year, with a minimum bond requirement of \$1,000. Generally, the maximum bond amount that can be required for any one plan official is \$500,000 per plan. However, the maximum required bond amount is \$1,000,000 for plan officials of plans that hold employer securities.

Is a fidelity bond the same as fiduciary liability insurance? A fidelity bond is not the same as fiduciary liability insurance. Fiduciary liability insurance is additional coverage that generally protects the plan

against claims for losses sustained because of a plan fiduciary's breach of duty.

Can any bonding or insurance company issue an ERISA fidelity bond? No, fidelity bonds must be placed with a surety or reinsurer that is named on the Department of the Treasury's Listing of Approved Sureties, Department Circular 570 (<http://fms.treas.gov/C570/c570.html>).

Are any plans exempt from the bonding requirements? Plans that are completely unfunded or not subject to Title I of ERISA are exempt from the bonding requirements. An unfunded plan is one that pays benefits only from the general assets of the organization.

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Can a bond insure more than one plan? If your organization sponsors more than one retirement plan, you can purchase one bond to cover all of your plans. However, the bond's amount must be sufficient to allow for a recovery by each plan in an amount at least equal to the amount that would have been required for each plan under separate bonds.

Can the bond have a deductible? No. The bond must provide coverage from the first dollar of loss up to the maximum amount required.

If the amount of funds handled by the plan increases after the bond is purchased, must the bond be updated during the plan year? No. The bond amount must be fixed annually (or estimated at the beginning of the plan's year pending receipt of necessary information) for each covered person based on the highest amount of funds handled by that person in the preceding plan year. So the bonding amount can change from year to year, but not during the year. If the plan doesn't have a complete preceding reporting year, the amounts covered must be estimated.

BENEFIT NOTES

MORE EDUCATION = MORE PLAN PARTICIPATION

Whether or not workers participate in employer-sponsored retirement plans may depend in part on educational attainment. According to the Employee Benefit Research Institute, workers with lower levels

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of education participated in retirement plans at lower levels than more highly educated workers. Of workers who earned \$50,000 or more in 2007, 50.7% of those without a high school diploma participated in a retirement plan, 65% of those with a high school diploma participated, and 76.1% of those who had a graduate or professional degree participated in a plan.

RELUCTANT TO RETIRE?

If asked, many recent retirees would have stayed longer with their employers instead of retiring. In a recent Employee Benefit Research Institute survey, 61% of recent retirees said they would have viewed a request to stay on longer positively. Nearly half reported that such a request would have encouraged them to delay retirement. A pay

increase, continuing to receive subsidized health insurance benefits, meaningful work, locking in already-earned pension benefits, telecommuting, and being able to work part-time rather than full-time all were highly rated incentives to working longer.

RETIREMENT SAVERS AND CURRENT ECONOMIC CONDITIONS

Despite the year-long recession and significant drop in stock prices, the majority of participants in the defined contribution retirement plans surveyed by the Investment Company Institute continued to participate in their plans. Only 3% of participants stopped contributing in 2008. And only 3.7% withdrew money from their plans last year. Fewer than one in seven participants changed the asset allocation of their account balances, and fewer than one in ten changed the allocation of their contributions.

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