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IRS Proposes Guidance on Notices of Failure to Defer Distributions

The IRS has issued proposed regulations outlining the information required to be included in notices to participants regarding the consequences of failing to defer their distributions. This guidance is proposed to become effective for notices provided in 2010 and later plan years.

Background

Under Internal Revenue Code Section 411(a), a plan must obtain participant consent in order to immediately distribute benefits with a present value of over $5,000. Regulations under Section 411(a) provide that this consent is valid only if the participant is informed of the right, if any, to defer receipt of the distribution. The Pension Protection Act of 2006 (PPA) requires any such notice provided in a plan year beginning after December 31, 2006 to also describe the consequences of failing to defer receipt of the distribution.

In addition, for plan years beginning after December 31, 2006, PPA expanded the distribution notice period as well as the applicable election period from 90 days before benefit commencement to 180 days before benefit commencement.

In Notice 2007-7, the IRS indicated that plan sponsors must make a reasonable attempt to comply with the expanded content requirements and provided a safe harbor for doing so. (See our January 25, 2007 *For Your Information*.) Under the safe harbor, the notice must describe –

- for a defined benefit plan, how much larger the benefits would be if the distribution is deferred (based on the normal form of benefit)
- for a defined contribution plan, the investment options available (including fees) if distributions are deferred
- how participants may access the portion of the SPD containing any special rules that might materially affect their decision to defer receipt of the distribution.

Proposed Regulations

The IRS has now issued proposed regulations providing guidance on the information needed to inform participants of the consequences of failing to defer receipt of benefits. Also, the proposed regulations would amend existing regulations to reflect the expanded notice and election periods provided under PPA.

To satisfy the PPA requirements, notices must describe the federal tax implications of failing to defer, including –

- differences in the timing of inclusion in taxable income between an immediate distribution that is not rolled over and a deferred distribution
- the 10% additional tax on certain distributions before age 59-1/2
- for defined contribution plans, the loss of the opportunity for future tax-favored treatment of earnings upon immediate distribution if the distribution is not rolled over to an eligible plan.

For defined benefit plans, the notice must include the amounts payable under the normal form of benefit both upon immediate commencement and upon the later of age 62 or attainment of normal retirement age. This information does not have to vary based on the marital status of the participant, if the plan is permitted to provide a QJSA explanation that does not vary based on marital status.

For defined contribution plans, the notice must include –

- a statement that some of the investment options available under the plan may not be generally available on similar terms outside of the plan, and contact information for obtaining additional information on the availability of investment options
- a statement that fees and expenses outside the plan may be different from fees and expenses that apply to the participant's account, and contact information for obtaining additional information on fees.

Finally, the notice must include information on any plan provisions that could reasonably be expected to materially affect a participant's decision to defer receipt (e.g., a provision under which a participant who fails to defer may lose retiree health coverage).

In general, all of the required information must be provided in one notice. However, the notice may include references to other notices or information provided or made available to participants, as long as it includes a statement of how that information can be obtained without charge and why that information is relevant.

Effective Date

The regulations are proposed to be effective for notices provided in 2010 and later plan years. Until then, a plan will satisfy the PPA notice requirements if it complies with the proposed regulations or with Notice 2007-7.

Conclusion

The proposed regulations provide welcome guidance on the PPA notice requirements. They require less detailed information than many had anticipated, and the ability to use standard text and reference other available material (e.g., SPDs) should ease the compliance burden.

Buck's consultants would be pleased to discuss this latest guidance with you and help you prepare the required notices.

This FYI is intended to provide general information. It does not offer legal advice or purport to treat all the issues surrounding any one topic.