



IRS Issues Final Regulations on 204(h) Notices

The IRS recently issued final regulations on the notice requirements for amendments that would significantly reduce the future rate of benefit accruals in a qualified pension plan. The regulations clarify when notices are required in light of changes made by the Pension Protection Act of 2006 (PPA), provide rules on timing for retroactive amendments, and coordinate the requirements for these notices with other statutory notice requirements.

Background

ERISA Section 204(h) and Internal Revenue Code Section 4980F require that all affected pension plan participants be given advance notice of a plan amendment that would cause significant reductions in the rate of future benefit accruals. Reductions in the rate of future accruals include the elimination or reduction of early retirement benefits or retirement-type subsidies. IRC Section 4980F also imposes an excise tax for failure to comply with these notice requirements. For both ERISA and IRC purposes, the required notices are referred to as “204(h) notices.” In 2006, PPA made several changes to the 204(h) notice requirements, and in March 2008, the IRS published proposed regulations reflecting these changes. (See our April 18, 2008 [For your Information.](#)) The IRS has now finalized these regulations.

Final Regulations

The [final regulations](#) are substantially similar to the proposed regulations, but contain some modifications and clarifications.

Change in Lump Sum Distribution Assumptions

PPA changed the required interest and mortality rates (IRC Section 417(e) assumptions) to be used in converting annuity benefits to a lump sum. The change in assumptions may result in a reduction of the lump sum benefit that would have otherwise been provided. The final regulations include prior IRS guidance that a 204(h) notice is not required for amendments adopting the PPA required IRC Section 417(e) assumptions.

General Timing With Respect to Retroactive Amendments

Like the proposed regulations, the final regulations provide that notice in connection with an amendment that is permitted to be retroactively effective generally must be given 45 days (15 days for multiemployer plans) before

the effective date of the amendment. The final regulations clarify that for this purpose the effective date is the earlier of the time the amendment is adopted or the time the plan begins to be operated as if the amendment were in effect.

Cash Balance Plan Amendments Eliminating Whipsaw

PPA eliminated “whipsaw,” under which cash balance plans could be required to pay lump sums that exceed the current value of an employee’s hypothetical account balance. Whipsaw in many cases resulted in lump sum payments greater than participants’ account balances, so implementing the PPA provision could be viewed as a cutback in benefits necessitating a 204(h) notice.

The final regulations reiterate the provision in Notice 2007-6 that if a 204(h) notice is required because the reduction in the rate of future benefit accrual due to the elimination of “whipsaw” is considered to be significant, the change cannot take effect until at least 30 days after notice is provided to participants. Further the regulations specify that the 30-day notice period only applies to amendments effective before January 1, 2009 – the regular 45-day rule applies to amendments effective thereafter.

BUCK COMMENT. *Under PPA, cash balance plans are required to use a market rate of return when determining the interest credits, but the IRS has not yet issued regulations defining market rate of return. The IRS notes in the preamble that it will likely issue guidance in the near future relating to the application of Section 4980F to plan amendments adopted to comply with these market rate of return requirements and that special timing rules for providing 204(h) notices may apply.*

Interaction With Other Notices

The final regulations provide that timely notices properly provided under certain IRC or ERISA provisions dealing with benefit reductions will be deemed to satisfy the 204(h) notice requirement and separate 204(h) notices will not be required. These include –

- notices provided to participants on retroactive amendments to comply with IRC Section 412(d)(2)
- notices required under ERISA Section 101(j) relating to amendments adopted to comply with the IRC Section 436 benefit limitation requirements
- notices required under IRC Section 418D and ERISA Section 4244A(b) when accrued benefits attributable to employer contributions to a multiemployer plan in reorganization are reduced or eliminated
- notices required under IRC Section 418E and ERISA Section 4245(e) to describe the effects of the insolvency of a multiemployer plan
- notices required under ERISA Section 4281 when a terminated multiemployer plan is amended to reduce benefits

- notices required under IRC Section 432(b)(3)(D) to comply with the IRC Section 432(f)(2) benefit limitations for multiemployer plans in critical status.

However, a separate 204(h) notice will still be required if a plan is amended to implement benefit reductions independent of the reductions permitted under the relevant notice requirement discussed above.

BUCK COMMENT. *The IRS notes in the preamble that it is developing notice requirements for multiemployer plans in critical status under IRC Section 432(e)(8)(C) and that the interaction between Sections 204(h) and 432(e)(8)(C) will be addressed in the Section 432 regulations.*

Notice to Contributing Employers

Effective for plan years beginning after December 31, 2007, PPA requires that all employers who have an obligation to contribute to a plan be provided 204(h) notices. The regulations make clear that this requirement only applies for contributing employers under multiemployer plans.

Timing of Notices for Certain Commercial Airlines

The final regulations reflect PPA's special notice timing rule for plans maintained by certain commercial airlines or employers in certain related businesses. For these plans, 204(h) notices must be provided at least 15 days before the effective date of the plan amendment (which for this purpose is the earlier of the time the amendment is adopted or the time the plan begins to be operated as if the amendment were in effect), instead of the usual 45 days.

Effective Date

The final regulations are generally applicable to 204(h) amendments that are effective on or after January 1, 2008. However, the timing rules relating to retroactive amendments apply to 204(h) amendments adopted in plan years beginning after July 1, 2008. In addition, with respect to 204(h) amendments to a lump sum based benefit formula, the rules relating to retroactive amendments apply to amendments adopted after December 21, 2006.

Conclusion

The final regulations provide important guidance on 204(h) notices, including on how the notice requirements may be satisfied through the issuance of other notices. Buck's consultants are available to discuss these final regulations and help you comply with the notice requirements.

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.