

July, 2004

Revision of Pension Forms for Relative Value Delayed

Qualified pension plans have long been required to provide notices to participants explaining the qualified joint and survivor annuity (QJSA) and any rights to waive it in favor of optional forms of distribution. In late 2003, the IRS issued final regulations requiring that the QJSA explanation include a detailed description of the relative values of any optional forms of distribution available to a participant, as compared to the QJSA. The "relative value" regulations were scheduled to apply to explanations of the qualified pre-retirement survivor annuity (QPSA) effective July 1, 2004 and to explanations of the QJSA effective for annuity starting dates beginning October 1, 2004. In response to an outcry from employers and consultants, in late June 2004, the IRS announced a delay in most aspects of the regulations. This Management Alert describes briefly what the regulations require and when pension distribution forms will need to be revised.

Relative Value Regulations

The regulations require plan administrators to provide either participant-specific information or generally-applicable information, with participant-specific information available on request, on the relative value of optional benefits offered under defined benefit pension plans, money purchase pension plans and certain defined contribution plans. The regulations require that there be a numerical presentation comparing the relative value of each optional distribution form to the QJSA. The regulations are intended to help participants understand that some benefits may have subsidies that the participant gives up when electing other forms of benefit which are not subsidized. For example, if the early retirement annuity is subsidized but the lump sum benefit is not, the regulations are aimed to require disclosure of that fact.

Delay in Effective Date

The effective date of the relative value regulations has been delayed to apply to QJSA explanations for annuity starting dates on or after February 1, 2006. Generally QJSA explanations are sent out at least 30 days (but not

more than 90 days) before the annuity starting date. Depending on plan administration practices, QJSA explanations with the new relative value disclosures will need to be ready in the fourth quarter of 2005.

The regulations were delayed, in part, to wait for the IRS to finalize regulations permitting sponsors of defined benefit pension plans to eliminate certain optional forms of benefits without violating the anti-cutback rules of Code Section 411(d)(6). The assumption is that elimination of certain optional forms may simplify the relative value explanation.

No Delay for Some Plans

If a plan provides a lump sum benefit or other optional form that is subject to the requirements of Code Section 417(e)(3) — including a decreasing annuity, such as a Social Security adjustment option — for which the actuarial present value is less than the actuarial present value of the QJSA, then the relative value disclosures are still effective for annuity starting dates on or after October 1, 2004 (affecting QJSA explanations starting in July or August 2004, depending on plan administration practices).

Pension plans that charge for a QPSA by reducing the participant's benefit must provide a QPSA explanation as part of the waiver election. Plans that fully subsidize the QPSA are not required to give waiver elections. There has been no delay in the application of the new rules for QPSA explanations; July 1, 2004 remains the compliance date. The new regulations require either a participant-specific estimate of the reduction in normal retirement benefit if the QPSA is elected or a generally applicable estimate participant-specific information provided on request. Employers sponsoring plans that are required to provide QPSA explanations should review their explanations for compliance with the new regulations.

Employer Action

Plan sponsors need to immediately determine if their defined benefit retirement plan or money purchase pension plan offers a lump sum benefit or other optional form of benefit subject to Code Section 417(e)(3) which is less valuable than the QJSA on an actuarial present value basis. If so, compliance with the relative value regulations will require immediate revision of the QJSA explanation. Plans that charge for a QPSA should review their waiver election disclosures as well.

Many employers have already started to revise the QJSA explanation to comply with the relative value regulations before the delay was announced. These employers may choose to proceed with compliance prior to the delayed effective date. Factors such as optional forms that may be considered for elimination, and variation in relative values, could influence the decision to proceed or wait.

Please contact the Seyfarth Shaw Employee Benefits Group attorney with whom you work or any employee benefits attorney listed on the website at www.seyfarth.com if you have any questions about the relative value regulations or revisions of QJSA explanations or your pension plans generally.

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