401(k) & Roth Distributions and Rollover Guidance, Canadian Retirement Plan Reporting Changes Under FBAR, and Items to Watch and a Couple of Brighter Notes

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Revised Roth Rollover Rules Require Immediate Plan Administration Changes and Participant Education

Previous guidance on participant rollovers from 401(k) plans which included Roth accounts had required that participant accounts that included both pre-tax 401(k) contributions and Roth contributions go through multiple steps to preserve the special tax treatment of the Roth 401(k) funds for the participant. While there were some plan vendors that had followed different rules on Roth 401(k) rollovers, the IRS recently issued guidance so that all Roth 401(k) rollovers would be handled consistently and participants electing to rollover their Roth 401(k) accounts would be able to do so more easily and without triggering taxation or being subject to additional unnecessary requirements.

The recently issued IRS Notice 2014-54 and proposed regulation relax the rollover rules and **can be used by individuals who have terminated employment and who are electing to rollover their retirement plan account on and after September 18, 2014**, provided the individual makes a reasonable interpretation of the last sentence of a particular subsection in the Internal Revenue Code that relates to the taxation of amounts rolled over requiring in certain situation the amount first be treated as coming from pre-tax funds. Individuals seeking to use the new rollover rules between September 18, 2014 and December 31, 2014, should consider obtaining tax advice to ensure the rollover does not have adverse tax consequences if all funds in the plan are not rolled over directly to another qualified plan (that separately accounts for Roth or after tax funds or to one or more IRAs and any funds are retained by the individual. An individual who has terminated employment and is entitled to a retirement plan distribution and who has more than $5,000 in his or her retirement plan account may always choose to retain the funds in that plan until they are eligible to roll the prior employer's plans funds into a new plan that has both pre-tax salary deferrals and Roth salary contributions or until such later date when they desire to take distributions for retirement.

For tax qualified retirement plans, the new rules apply to distributions after January 1, 2015 will be subject to the new rules and so **plans must have all procedures and forms in place to handle the new rules by January 1, 2015.** These changes will require plans to change the contents of the tax notice provided to participants when they are entitled to a distribution, potential changes to the forms communicating the information regarding the distribution to possibly include new or additional information and to explain to the individual participants why that information is important to them from a tax standpoint, administrative procedures related to distributions and reporting of distributions, possibly changes to summary plan description information regarding distributions and rollovers.

Plan sponsors should anticipate additional questions from persons entitled to receive plan distributions about the new options available to them and the information on their forms related to distributions and rollovers. Thus, the new options may create a need for participant education on the distribution alternatives and tax consequences, including a reminder of the reason individuals should consider keeping Roth funds in Roth accounts via direct rollovers to other Roth accounts to preserve the years of participation the individual has in the Roth account toward the 5 year participation and age 59 and ½ requirement for the current tax-free nature of distribution of earnings on Roth funds.

The Notice permits individuals who receive a distribution check from their plan which includes Roth or after-tax funds to rollover such funds to an IRA or Roth IRA by depositing the funds in such accounts within 60 days and instead of requiring each account to have a pro-rata portion of pre-tax and Roth/after tax funds, to permit and treats all of the distributions to separate destination accounts (e.g., a traditional pre-tax individual retirement account and a Roth individual retirement account established to receive the Roth 401(k) rollover) as a single distribution and as long as the individual is not receiving cash out of the account being rolled over to preserve the tax treatment of both the pre-tax and Roth and after-tax

funds. **The IRS provides a chart to assist with rollovers as a quick reference when a total account is to be rolled over which is attached to this news alert for your reference.**

Additional complexities are added if the full account is not rolled over and a portion is retained in cash by the individual. Individual should ensure that any plan or IRA receiving Roth funds is set up with separate accounting for the Roth funds to preserve the tax nature of the Roth amounts toward obtaining a qualified distribution at or after age 59 and ½ with 5 years of participation (funds in Roth account for 5 tax years).

FBAR Changes for Persons with Certain Canadian Retirement Plan Accounts

Employers who sponsor or have affiliates who sponsor retirement plans in Canada may want to alert the Canadian plan participants who are U.S. resident aliens or U.S. citizens that there has been some relief related to the Foreign Based Account Reporting (FBAR) requirements. These changes apply to Americans and Canadians living in the U.S. with registered retirement savings plans (RRSPs) and registered retirement income funds (RRIFs) and permit these individuals to now automatically qualify for tax deferral similar to that available to participants in U.S. 401(k) plans and IRAs. There are filing requirements and the requirements vary based upon tax elections these individual may or may not have previously made. There is also some retroactive relief for persons who failed to properly choose the taxation with respect to the RRSPs and RRIFs in the past. More detail on the different elections and requirements for different situation can be found in IRS Revenue Procedure 2014-55 which is posted on IRS.gov.

The Form 8891 previously used for reporting and making tax election is obsoleted as of December 31, 2014. The relief is effective for tax years beginning on or after January 1, 1996 (yes that date is the correct date).

New Movements to Watch on Participant Directed Investments, Brokerage Windows and Professionally Managed Account Alternatives in 401(k) and Other Defined Contribution Plans

The U.S. Supreme Court has agreed to hear during this term the *Tibble v. Edison* International case in which the Ninth Circuit Court of Appeals decided that in a dispute about the monitoring of investment funds offered to participants that the act that started the limitation period on when a participant can bring suit based on an allegation of a breach of fiduciary duty on the prudence of an investment fund runs only from the date the fund is initially selected and not from each time the plan fiduciary decides not to change the funds, whether the use of retail investment funds instead of institutional funds which have lower fee rates is a breach of fiduciary duty and whether the plan's revenue sharing arrangement violated ERISA's fiduciary rules. The Ninth Circuit's application of the statutory statute of limitations on claims for breach of fiduciary for only the initial selection of the investment fund runs contra to the U.S. Department of Labor's position that there is a duty to monitor the plan investment funds after the initial selection of the fund. The review of these issues will have implications for plan fiduciaries and for how plan administration record keeping agreements are structured for the vast majority of 401(k) plans.

While the U.S. Supreme Court is looking at those fiduciary issues, the U.S. Department of Labor is investigating brokerage windows and how those are structured and offered to employees and the disclosures that plan administrators make regarding the fees related to the selection of a brokerage window. The General Accounting Office (the "GAO") recently published its audit report on retirement plans offering participants the alternative to elect to invest their retirement accounts in a professionally managed accounts which is a feature being offered in 401(k) plans by which the participants can elect to turn the investment decisions on their individual accounts to a third party. The GAO's report included in its recommendations that the U.S. Department of Labor look at how professionally managed investment accounts are offered to plan participants and the disclosures made regarding the fees, the restrictions on such accounts and the investment manager(s) available to the participant as well as historical data on the investment manager. Plan sponsors may want to consider instructing their plan fiduciaries to review the various options offered with their participant directed investment account plans and this should not be limited to just the investment funds, but also to investment advice, brokerage windows and professionally managed accounts so that they are aware of the arrangements, requirements and related fees, in addition to the other fee disclosures they review.

There is a continued focus on disclosures, fees, investment opportunities and the investment disclosures for participant directed investment plans. The U.S. Supreme Court's decision will impact a number of critical issues for plan sponsors

and plan fiduciaries. Plan sponsors may want to review their plan governance structures in light of the continued scrutiny and emphasis by regulators on fiduciary issues Plan fiduciaries should consider education to remain current on the developing trends in the fiduciary litigation under ERISA.

Ending on a Couple of Brighter Note-Investment Policy Not Required to be Provided to Participant Upon Request Under ERISA 104

In a glimmer of a better news, the Fifth Circuit recently found in *Murphy v. Verizon Communications Incorporated* that a plan administrator is not required to produce the plan's investment policy to a participant upon the participant's request under ERISA section 104 because the investment guidelines were not alleged to be binding on the plan or participants and the investment guidelines did not define the rights, duties, entitlements or liabilities. This follows the interpretation of the disclosure obligation taken by a majority of the Circuit Courts of Appeal ruling on this issue.

While The U.S. Supreme Court acknowledged that ERISA plans can include a binding plan term that limits when a participant can bring suit based on a denied claim in *Heimeshoff v. Hartford Life & Accident Insurance Co*. in 2013, an employer's ability to use a choice of venue provision in a plan to limit where actions can be brought against it by participants and beneficiaries has not yet been decided by the U.S. Supreme Court. Recently, the Sixth Circuit provided a second glimmer of hope for plan sponsors trying to control plan costs when it permitted a choice of venue provision in a pension plan to stand and permitted dismissal of a case brought in a different district court than the court chosen as the venue in the plan document in *Smith v. Aegon Companies Pension Plan* (October 14, 2014) .

The Sixth Circuit upheld the choice of venue over the objecting amicus brief filed by the U.S. Department of Labor and refused to give any deference to the U.S. Department of Labor's position because it was only contained in their amicus briefs and not in any authoritative guidance. While this is only the law in the Sixth Circuit at this point, a number of District Courts have also accepted these forum selection clauses. Employers who have not included such clauses may want to consider whether such a clause should be added to their non-collectively bargained plans. Employers with collectively bargained plans may want to consider whether the addition of such a clause is permitted under their collective bargaining agreement or if it is a point worth bringing to the negotiating table.

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