ERISA Update

PENSION & EMPLOYEE BENEFITS ISSUES

A periodic review of the latest legal developments affecting employee benefits, of interest to clients, union officials, fund administrators, trustees and attorneys.

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INSIDE THIS ISSUE:

DOL Provides Guidance on "Float" Income	1
Allocation By Trustees of Employer Contributions Between Retirement Plans, A Fiduciary or Settlor Function?	1
The IRS Issues Final Regulations on the Return of Mistaken Employer Contributions and Withdrawal Liability Payments Made to Multiemployer Retirement Plans	2
Employer's Failure to Provide Summary Plan Description to Participant is a Costly Mistake	4
Private Letter Ruling Explains Deductibility of Employer Contributions Made to Multiemployer Defined Benefit Pension Plans	5

DOL PROVIDES GUIDANCE ON "FLOAT" INCOME

By: Timothy R. Bauman, Esq.

Custodians (and directed trustees) often maintain general accounts to facilitate the transactions of employee benefit plans. Typically, such accounts hold either contributions and assets pending investment directions or funds in connection with the issuance of a check to make a plan distribution or other disbursement. In regard to these accounts, the custodians often retain earnings, called "float", from the short-term investment of funds held in these accounts. The Department of Labor, in Advisory Opinion 93-24A, stated that a custodian or trustee's exercise of discretion to earn income for its own account from the float attributable to outstanding benefit checks constitutes prohibited fiduciary self-dealing. In a subsequent information letter, however, the DOL indicated that if a bank fiduciary openly negotiates with an independent plan fiduciary to retain float then the use of float would not be self-dealing. To avoid problems, banks were encouraged, as part of their fee negotiations, to provide full and fair disclosure regarding the use of float on outstanding benefit checks.

In Field Assistance Bulletin 2002-3, issued on November 5, 2002, the

(Continued on page 2)

ALLOCATION BY TRUSTEES OF EMPLOYER CONTRIBUTIONS BETWEEN RETIREMENT PLANS A FIDUCIARY OR SETTLOR FUNCTION?

By: George H. Sallaway, Esq.

The United States Department of Labor recently released a Field Assistance Bulletin (FAB 2002-2) explaining its views on the appropriate use of plan assets by multiemployer plan trustees to pay expenses. The facts presented to the Department of Labor and its analysis are described below.

Multiemployer Fund Z was funded by Employer Association X according to a contribution formula specified in a collective bargaining agreement between Employer Association X and Union Y. The Fund Z trust agreement provides that amendments to the trust agreement may be made by Employer Association X, Union Y, or Fund Z's board of trustees.

From 1955 until it was frozen in 1989, thereby disallowing any new employee participants, a defined benefit plan ("DB") received its employer contributions through Fund Z. After 1989, existing DB plan participants accrued no further benefits. In 1987, a defined contribution plan ("DC") was established and

(Continued on page 3)

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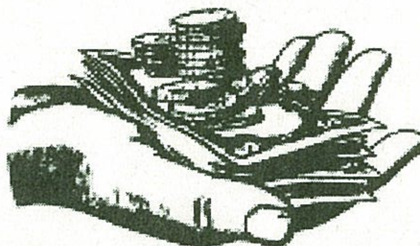
(Continued from page 1)

Department of Labor elaborated on "negotiation and full and fair disclosure." Regarding plan fiduciaries such as Boards of Trustees, if the service provider will receive compensation in the form of float, the selection and monitoring process engaged in by the fiduciaries should include the following: (1) A review of comparable providers and service arrangements (e.g., quality and costs) to determine whether such providers may credit float to the provider's own account, rather than the plan; (2) A review of the circumstances under which float may be earned by the service provider; (3) A review of sufficient information to enable the plan fiduciary to evaluate the float as part of the total compensation to be paid for the services to be rendered under the agreement. (In this regard, fiduciaries should request and review the rates the provider generally expects to earn). Additionally, a plan fiduciary must periodically monitor compliance by the service provider with the agreement and the reasonableness of the compensation under the agreement in order to ensure that continuation of the agreement meets the requirements of the applicable sections of ERISA.

As to service providers, the primary issue is whether the provider has disclosed sufficient information. To avoid self-dealing, the service provider should take the following steps: (1) Disclose the specific circumstances under which float will be earned and retained; (2) In the case of float on contributions pending investment discretion, establish specific time frames within which cash pending investment direction will be invested following direction from the plan fiduciary, as well as any exceptions that might apply; (3) In the case of float on distributions, disclose when the float period commences and ends; and (4) Disclose the rate of the float or the specific manner in which such rate will be determined. In addition, the agreement should not permit the service provider to affect the amount of its compensation in violation of ERISA (e.g., by giving the service provider broad discretion over the duration of float).

Thus, float must be regarded as part of the service provider's compensation for services to the plan. Therefore, the plan fiduciary must have an adequate understanding of how the service provider will earn float and how it contributes to the compensation of the service provider. In addition, the service provider must make disclosures sufficient to permit the fiduciary to make an informed decision regarding the proposed float arrangement. To avoid having the arrangement give rise to a self-dealing violation, both parties must avoid giving the service provider discretion to affect the amount of compensation it receives from float. In light of this DOL Field Assistance Bulletin, employee benefit funds should review their service provider agreements with custodians and directed trustees to ensure the treatment of float income is proper.



THE IRS ISSUES FINAL REGULATIONS ON THE RETURN OF MISTAKEN EMPLOYER CONTRIBUTIONS AND WITHDRAWAL LIABILITY PAYMENTS MADE TO MULTIEMPLOYER RETIREMENT PLANS

By: Michael S. Travinski, Esq.

The Internal Revenue Service issued final regulations on the return of mistaken employer contributions and withdrawal liability payments made to tax-qualified multiemployer retirement benefit plans. The regulations provide plan administrators and contributing employers with guidance in complying with the Multiemployer Pension Plan Amendments Act of 1980 ("MPPAA"), most importantly specifying the conditions under which mistaken employer contributions and withdrawal liability payments may be returned to contributing employers. The regulations were made effective for refunds made after July 22, 2002.

(Continued on page 3)

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also funded by employer contributions to Fund Z. After the DB plan was frozen in 1989, all Employer Association contributions in Fund Z were allocated solely to the DC plan. At the time the DB plan was frozen, Fund Z's trustees believed that the DB plan would not need any further contributions in order to pay all benefits due under the plan. Fund Z's trust agreement specifies the contribution allocation between the plans.

In 1999, because funding problems had developed in the DB plan, Employer Association X and Union Y amended the Fund Z trust agreement, allowing Fund Z's allocation of employer contributions to the DB plan to match the amount of annual forfeitures in the DC plan. In 2002, facing further DB plan shortfalls, Fund Z's trustees voted to amend the trust agreement and increase by 20% the amount of employers' contributions allocated to the DB plan. The amendment stated that the trustees were acting "in their settlor capacity."

The question was raised as to whether Fund Z's trustees, when they amended the Fund Z trust agreement, were acting in a fiduciary capacity, thereby subjecting themselves to ERISA's fiduciary standards, or were they instead acting in a settlor capacity. Settlor activities would include the establishment, design, and termination of retirement plans. Fiduciary activities relate to management of the retirement plan. The question is significant for several reasons. Expenses for activities carried out by multiemployer plan trustees in their "settlor" capacity may not be charged to the plan, but instead must be borne by another entity, such as the employer organization.

In addition, under ERISA Section 406(b)(2), a fiduciary with respect to a plan is prohibited from acting in any transaction involving the plan whose interests are adverse to the interests of the plan, its participants or beneficiaries. A fiduciary must act in the best interest of the plan participants and beneficiaries and is responsible for the "management" of the plan. Imposing fiduciary duties on a plan sponsor's decision to amend the plan would divide the sponsor's loyalties among the participants and beneficiaries of the various plan, violating the prohibited transaction rule, thereby making amendments impossible.

The DOL held that in this multiemployer plan, where the collective bargaining agreement and trust agreement vested broad authority in the trustees to establish the fund, allocate contributions between the plans and amend the trust agreement and the plan documents, Fund Z's trustees acted in a settlor capacity, and not as a fiduciary, in amending the trust agreement and reallocating employer contributions to the DB plan. Thus, any costs incurred by the trustees to implement the change would not be appropriate for a multiemployer retirement plan to pay.

Before you decide to pay any expense from plan assets, read carefully the relevant documents (i.e., the plan, trust and collective bargaining agreements) to determine whether their language contemplates the activity as a settlor function or a fiduciary act.

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Prior to the 1980 enactment of the MPPAA, the Internal Revenue Code's "exclusive benefit rule" (which prohibits fiduciaries of tax-qualified employee benefit plans and their related tax-exempt trusts from using any part of the trusts' principal or income for purposes other than the exclusive benefit of employees and beneficiaries) barred tax-qualified retirement benefit plans from refunding employer contributios unless the contributions were made due to a mistake of fact and were returned to the employer within one year of the contribution date. The MPPAA amended this exception, as it was too narrow in the multiemployer retirement plan context. As a result of the enactment of the MPPAA, mistaken employer contributions may be returned to contributing employers without violating the exclusive benefit rule if the contributions were made because of a mistake of fact or law and the contributions are returned within six months after the date the plan administrator determines that the contributions were made in error. Similarly, mistaken withdrawal liability payments may be returned to employers without violating the exclusive benefit rule if the payments were made because of a mistake of fact or law and are returned within six months after the plan administrator determines that the payments were made in error.
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According to the final regulations, contributing employers must satisfy two conditions before retirement plans are permitted to return mistaken employer contributions and withdrawal liability payments to satisfy the exclusive benefit rule exception. First, employers must establish a right to a refund by filing a claim with the plan administrator within six months after the date on which the plan administrator determines that the mistake occurred. Second, employers must demonstrate that mistaken contributions or withdrawal liability payments were made due to a mistake of fact or law. Mistaken contributions or withdrawal liability payments made under a mistake relating to whether a retirement plan was qualified or whether a related trust was tax-exempt is not considered to be a mistake of fact or law which entitles employers to a refund.

The final regulations also provide a plan administrator with guidance for determining the amount of the excess contribution or overpayment to be returned. The amount of the excess contribution or overpayment is the excess of the amount contributed or paid over the amount that would have been contributed or paid had no mistake occurred. Earnings attributable to excess contributions cannot be returned to contributing employers. Any losses attributable to excess contributions must reduce the amount of the contributions returned (applying plan-wide investment experience would be an acceptable method of calculating losses under the regulations). And, a refund of excess contributions cannot reduce a participant's account balance in a defined contribution plan to an amount less than that amount which would have been in the participant's account had no mistake occurred. Finally, interest on the overpayment of withdrawal liability may be returned to employers if the refund is made pursuant to Pension Benefit Guarantee Corporation regulations on the overpayment of withdrawal liability (the overpayment is refunded in a lump sum and interest is credited from the date of the overpayment to the date on which the overpayment is refunded to the employer at the same rate as the rate for overdue withdrawal liability payments).

As a result of the issuance of these regulations, it is no longer enough that plan administrators return mistaken employer contributions or withdrawal liability payments within six months after their determination that they were made in error to satisfy the exclusive benefit rule exception. Plan administrators are now charged with a more active role- the responsibility of determining whether contributing employers have in fact satisfied the two required conditions before any excess employer contributions or overpayments can be returned. If either condition is not satisfied, then any excess contributions or overpayments cannot be returned without violating the exclusive benefit rule.

EMPLOYER'S FAILURE TO PROVIDE SUMMARY PLAN DESCRIPTION TO PARTICIPANT IS A COSTLY MISTAKE

By: Melvin H. Pizer, Esq.

In the Sunderlin v. First Reliance Standard Life Insurance Company case, which was decided by the Federal District Court in the Western District of New York, an employee (Sunderlin) participating in the company's long term disability insurance benefit plan began receiving benefits in November 1995. Mr. Sunderlin returned to work on a part-time basis in June 1996 and in May 1999, First Reliance denied Mr. Sunderlin any further benefits.

As part of the appeal of the insurance company's decision, Mr. Sunderlin's attorney requested the summary plan description for the long term disability benefit plan. The insurance company did not provide a copy of the summary plan description, but instead directed him to request the document from the employer. The employer provided Sunderlin a copy of the insurance policy issued by First Reliance. In addition to suing for benefits under the long term disability plan, Sunderlin also claimed that the employer was liable for penalties under ERISA for the failure to provide a copy of the summary plan description.

In addition to finding that Sunderlin was entitled to benefits, the court found that the employer was liable for failing to provide a copy of the summary plan description. The court stated that the insurance policy provided to Sunderlin was not a summary plan description as defined by ERISA. The court imposed penalties of $15.00 per day for 1,165 days (approximately $17,000) due to the employer's failure to provide Sunderlin with a copy of the summary plan description. The court also stated that the employer acted in bad faith when it provided Sunderlin with a copy of the insurance policy rather than the summary plan description.

As you can see from this case, trustees and plan administrators should not take lightly a participant's request for plan documents. When you receive such a request, you should act promptly and provide the documents required to be given to a plan participant. The documents include the latest summary plan description, the latest annual report, any terminal report, the collective bargaining agreement, the trust agreement, contracts or any other instruments under which the plan is operated. Remember that a plan administrator who fails to supply requested information within 30 days may be held personally liable to the participant for an amount up to $110.00 per day for each day that the failure continues.

PRIVATE LETTER RULING EXPLAINS DEDUCTIBILITY OF EMPLOYER CONTRIBUTIONS MADE TO MULTIEMPLOYER DEFINED BENEFIT PENSION PLANS

By: James C. Shake, Jr., EA

The Internal Revenue Service recently issued a private letter ruling that is of interest to multiemployer defined benefit pension plans and the employers contributing to them. Large stock market gains during the 1990s which provided surplus asset values have caused the gap to narrow considerably between the minimum required funding contribution and the maximum allowed deductible contributions to multiemployer defined benefit pension plans.

The defined benefit plan's actuary usually calculates, in accordance with Internal Revenue Service guidelines, the expected total employer contributions that will be made to the defined benefit plan for the coming year based upon the labor wage rates, estimated hours worked, and anticipated employer contributions per hour. If the total expected employer contributions are less than the maximum allowed employers deductible amount for that year, then there is usually no concern that the contributions will not be deductible by the employers.

Questions may arise as to whether contributions are fully deductible by the employers when more hours are worked during the year, and therefore more contributions received by the plan, than anticipated at the beginning of the plan year. This is especially true when the actuary's contribution estimates made at the

beginning of the plan year are very close to the employers' maximum deductible amount allowed to a defined benefit plan under the Internal Revenue Code.

The private letter ruling states that all employer contributions made to a multiemployer defined benefit plan will be deductible by the contributing employers on their business income tax returns if the good faith estimates of expected contributions to the plan fall within the maximum deduction limits, even when actual contributions as of the end of the year turn out to exceed those limits.

The key to this ruling is that the plan's projected employer contributions as normally calculated by the Fund actuary for a defined benefit plan must be within the maximum deductible limit. If the projected contributions exceed the maximum deductible limit, then corrective steps must be taken at that time.

This ruling, while it only apples to the multiemployer defined benefit pension plan that requested it, is an indication of the current thinking of officials at the Internal Revenue Service regarding multiemployer defined benefit pension plans and the deduction by employers of their contributions.

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