

MEMO# 12559

September 5, 2000

IRS FINAL REGULATIONS ON ELIMINATION OF OPTIONAL FORMS OF BENEFIT UNDER ANTICUTBACK RULE

[12559] September 5, 2000 TO: PENSION MEMBERS No. 44-00 PENSION OPERATIONS ADVISORY COMMITTEE No. 63-00 MAY 4TH AND JUNE 12TH CONFERENCE CALL PARTICIPANTS RE: IRS FINAL REGULATIONS ON ELIMINATION OF OPTIONAL FORMS OF BENEFIT UNDER ANTICUTBACK RULE The Internal Revenue Service has issued final regulations, which provide relief from the application of the Code section 411(d)(6) anticutback rule, permitting the amendment of qualified defined contribution plans, including prototype plans, to eliminate alternative forms of benefit distribution, eliminate or modify certain rights to in-kind distributions and expand the types of permissible transfers of account balances between defined contribution plans. These final regulations are effective September 6, 2000, and apply to plan amendments that are adopted and effective on or after that date. The Institute had submitted comments on these regulations in August, 1998¹ (in response to a request for comment on the issue) and June, 2000² (in response to the proposed regulations). The final regulations generally permit defined contribution plans to be amended to eliminate all forms of benefit provided under a plan as long as individuals are able to obtain a lump sum distribution from the plan, an approach recommended in the Institute's June, 2000 comment letter. The final regulations also address the Institute's comments regarding the elimination of rights to in-kind distributions. Elimination of Optional Forms of Benefit. The proposed regulations had required plans in which optional forms of benefit were eliminated to retain at least one previously available, extended form of distribution and to offer a lump sum distribution option.³ The Institute and other commentators proposed eliminating the requirement to retain an extended form of benefit. The final regulations adopt this suggestion: a plan in which forms of benefit previously available are eliminated must provide participants with only a lump sum distribution option. No other form of benefit distribution need be retained in the plan. 1 See Institute Memorandum to Pension Committee No. 55-98, dated August 28, 1998. 2 See Institute Memorandum to Pension Committee No. 44-00, Pension Operations Advisory Committee No. 44-00, and May 4th and June 12th Conference Call Participants, dated June 28, 2000. 3 See Institute Memorandum to Pension Committee and Pension Operations Advisory Committee, dated March, 31, 2000, for the proposed regulation. 2The Service has included a rule to protect participants taking distribution shortly after the plan is amended and who, therefore, may have planned on the availability of the payment form that is being eliminated or restricted. Specifically, plan amendments eliminating or restricting forms of benefit distribution cannot apply to a distribution that has an annuity starting date earlier than the 90th day after the date the participant receiving the distribution has been furnished a summary reflecting the amendment⁴ or, if earlier, the first day of the second

plan year following the plan year in which the amendment is adopted. (The 90-day rule is similar to that which the Institute recommended in its August, 1998 letter.) Elimination of Rights For Distribution of In-Kind Securities. The final regulations clarify and modify the proposed rules regarding the elimination or restriction of a right to receive benefit distribution in kind from defined contribution and defined benefit plans. In response to comments, including those of the Institute, the examples in the final regulations were modified to clarify that a plan amendment that limits the right of a distribution in specified types of property to certain participants need not itself contain a list of those participants.

Elective Transfers. The final regulations adopt the provisions of the proposed regulations relating to elective transfers, with some modifications. The final rule provides relief from the application of section 411(d)(6) in the following cases: (1) direct rollovers described in section 401(a)(31), under existing rules;⁵ (2) voluntary transfers in any case in which a participant is entitled to a distribution from a defined contribution or defined benefit plan, but the participant is not eligible to receive an immediate distribution in a lump sum distribution that can be entirely rolled over (referred to as “distributable event” transfers); and (3) cases in which a participant is not entitled to a distribution, but in connection with a corporate merger or acquisition or change in the participant’s employment status, seeks to transfer his or her accrued benefit from a defined contribution plan to another defined contribution plan of the same type (referred to as “transaction or employment change” transfers). Under the proposed regulations, “distributable event” transfers were available only for transfers from defined benefit plans to defined benefit plans and from defined contribution plans to defined contribution plans. The final rules would permit the transfers of amounts between different plan types. With respect to “transaction or employment change” transfers, however, the Service has not expanded the rule; the final regulation continues to restrict such transfers to those between defined contribution plans of the same type, e.g., 401(k) plan to 401(k) plan, rejecting an Institute request to expand the rule.⁶

According to the Service, the restrictions on the types of 4 The amendment must also satisfy DOL regulations at 29 CFR 2250.104(b)-3 relating to summary material modifications. 5 The final rules eliminate duplication between previously issued elective transfer rules and section 401(a)(31), which permits direct rollovers of eligible rollover distributions. As a result, under the final regulations, plans and participants will not be able to rely on the distributable event transfer rules if the participant is eligible to receive a distribution consisting entirely of an eligible rollover distribution within the meaning of section 401(a)(31)(C), and instead, will be required to offer a section 401(a)(31) direct rollover. 6 The Institute, in its comment letters, had suggested that this rule be expanded to permit participants to elect to transfer benefits from one defined contribution plan to other defined contribution plan of any type. 3 plans between which such transfers are permitted “facilitate administration of the qualified plan distribution rules by ensuring that amounts transferred to the receiving plan, in a transfer that is not itself a distribution, will be subject to similar legal restrictions with respect to the in- service distributions.” The final regulations also clarify that the right to a transaction or employment change transfer is an “other right or feature” for purposes of section 401(a)(4) (unlike the distributable event transfer, which is treated as an optional form of benefit for purposes of that section). However, the final regulations specify certain conditions of section 401(a)(4) that may be disregarded.

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