Limited Exceptions for Certain Single-Employer Plans

Paragraph (a)(2)(ii)(B) of the proposal provided similar relief for a plan that distributed assets in satisfaction of all benefit liabilities in a standard termination pursuant to section 4041(b). One commenter requested that this exception be expanded to provide relief from the annual funding notice requirements for plan years after the plan's termination, but before the plan actually distributes assets in satisfaction of all benefit liabilities. Typically this occurs when a plan is waiting for a favorable determination letter from the Internal Revenue Service (IRS). Such plans, according to a commenter, ordinarily will not have the information they need to complete annual funding notices during this period. The funding target attainment percentage, value of assets and liabilities that determine the plan's funding target attainment percentage, and year-end liabilities will not be readily available because such plans are no longer subject to the minimum funding requirements in section 430 of the Code (ERISA§ 303) or the requirement to file a Schedule SB to the Form 5500 Annual Return/Report after the plan year of termination.[1] Thus, in the absence of the exception in paragraph (a)(2)(ii) of the final regulation, such plans would have to hire an actuary as if the plan were subject to these requirements, solely to obtain the missing section 101(f) information. The commenter argues that valuable resources will be expended unnecessarily in this regard. The Department agrees with this commenter that such an outcome is not in the best interests of plan participants and beneficiaries in these limited circumstances. For these reasons, and after consulting with the PBGC, Treasury and the IRS, the Department adopts paragraph (a)(2)(ii)(C) of the final rule which exempts the plan administrator from providing a funding notice for a plan year if the due date for the funding notice is on or after the date and the plan administrator files a standard termination notice (i.e., PBGC Form 500) pursuant to 29 CFR § 4041.25, provided that the proposed termination date is on or before the due date of the funding notice and a final distribution of assets in satisfaction of the plan's benefit liabilities proceeds according to the requirements of section 4041(b) of ERISA. If, for some reason, the termination does not proceed according to the requirements of section 4041(b) of ERISA with a distribution of assets in satisfaction of all benefit liabilities and the plan again becomes subject to the minimum funding standards, the exception ceases to apply.

One commenter recommended expanding the exception to excuse the plan administrator of a single-employer plan from furnishing a funding notice if the plan administrator reasonably believed that the PBGC would appoint itself trustee within the next 12 months. The same commenter also recommended excusing the plan administrator from furnishing a funding notice after commencement of the distribution of assets under a standard or distress termination instead of after the final distribution of all assets as set out in the proposal. Neither of these recommendations is adopted in the final rule. The first recommendation, without more, would give too much discretion to the plan administrator to determine whether or not to provide the funding notice. In addition, unlike the other exceptions in the final rule, the first

[1] *See also* the instructions to Schedule SB of the 2012 Form 5500 Annual Return/Report, which state: "For terminating plans, Rev. Rul. 79-237, 1979-2 C.B. 190 provides that minimum funding standards apply until the end of the plan year that includes the termination date. Accordingly, the Schedule SB is not required to be filed for any later plan year."

recommendation is not grounded on a factor such as cost savings to the plan or an absence of information needed to complete the annual funding notice (for example, because the plan is no longer subject to the funding rules under the Code or ERISA's annual reporting requirements); nor does it appear to rest on any separate disclosure requirements applicable to such plans under title IV of ERISA. The commenter's second recommendation was not adopted for essentially the same reasons against the first recommendation, but also because the new exception in paragraph (a)(2)(ii)C), in the Department's view, provides substantially equivalent relief in the case of a standard termination.

Mergers and Consolidations

Paragraph (a)(3) of the final regulation, like the proposal, provides relief in the case of a merger or consolidation of two or more plans. The final plan year of a plan that has legally transferred control of its assets to a successor plan (hereafter the "non-successor plan") ends upon the occurrence of the merger or consolidation. Under this exception, the plan administrator of a non-successor plan is not required to furnish a funding notice for its final plan year.

One commenter requested clarification whether the funding notice of the successor plan for the year of the merger must reflect the funding percentages, assets, and liabilities of the non-successor plan for the two preceding plan years. Because the assets and liabilities of the non-successor plan were not assets and liabilities of the successor plan before the merger or consolidation, the successor plan's funding notice for the year of the merger would not have to reflect this information. The year-end data in this funding notice, however, would reflect the combined assets (both single and multiemployer plans) and liabilities (single-employer plans only). No changes to the operative text were needed for this clarification.

Funding Percentage (§ 2520.101-5(b)(2))

Paragraph (b)(2) of the final regulation, like the proposal, requires disclosure of a plan's funding percentage. Specifically, in the case of a single-employer plan, paragraph (b)(2)(i) of the final regulation provides that a notice must include a statement as to whether the plan's funding target attainment percentage for the notice year, and for each of the two preceding plan years, is at least 100 percent (and, if not, the actual percentages). The term "funding target attainment percentage" is defined in section 303(d)(2) of ERISA, which corresponds to Code section 430(d)(2). Guidance issued by the Department of the Treasury under Code section 430 also applies for purposes of section 303 of ERISA. Treasury regulations under Code section 430 provide that the funding target attainment percentage of a plan for a plan year is a fraction (expressed as a percentage), the numerator of which is the value of the plan's assets for the plan year (determined under the rules of 26 CFR 1.430(g)-1) after subtracting the prefunding balance and funding standard carryover balance (collectively the "credit balances") under section 430(f)(4)(B) of the Code and § 1.430(f)-1(c), and the denominator of which is the funding target of the plan for the plan year (determined without regard to the at-risk rules of section 430(i) of the Code and § 1.430(i)-1).[2] Thus, this percentage for a plan year is calculated by dividing the value of the plan's assets for that year (after subtracting the credit balances, if any) by the funding target of the plan for that year (disregarding the at-risk rules).

One commenter expressed concern with using the funding target attainment percentage calculated in the manner described above. This commenter believes there are circumstances when this percentage does not necessarily show the most accurate picture of the plan's funded status. For instance, this commenter believes it is misleading to subtract the credit balances discussed above when the plan otherwise is 100 percent funded. Such a subtraction, according to this commenter, could show a funding target attainment percentage of less than 80 percent when the plan is 100 percent or more funded before such subtraction and needlessly raise the concerns of participants regarding the application of the benefit restrictions and limitations of section 436 of the Code.[3] ERISA section 101(f)(2)(B)(i), however, specifically requires a plan administrator to disclose the funding target attainment percentage determined by subtracting the credit balances from the value of the plan's assets.

Assets and Liabilities (§2520.101-5(b)(3))

Section 101(f)(2)(B)(ii)(I)(bb) of ERISA states that a funding notice must include, in the case of a single-employer plan, "the value of the plan's assets and liabilities for the plan year to which the notice relates as of the last day of the plan year to which the notice relates determined using the asset valuation under subclause (II) of section 4006(a)(3)(E)(iii) and the interest rate under section 4006(a)(3)(E)(iv)[.]"

Based on the foregoing, paragraph (b)(3)(i)(B) of the proposal provided that a single-employer plan must include a statement of the value of the plan's assets and liabilities determined as of the last day of the notice year. For purposes of this statement, plan administrators must report the fair market value of assets as of the last day of the plan year. In addition, a plan's liabilities as of the last day of the plan year are equal to the present value, as of the last day of the plan year, of benefits accrued as of that same date. With the exception of the interest rate assumption, the present value should be determined using the assumptions used to determine the funding target under ERISA section 303. The interest rate assumption is the interest rate provided under section 4006(a)(3)(E)(iv) of ERISA in effect for the last month of the notice year rather than the rate in effect for the month preceding the first month of the notice year. For the reasons set forth below, this proposed provision is adopted without change.

Some commenters expressed their concerns that this aspect of the proposal would lead to confusion. More specifically, they argued that participants and beneficiaries will be confused by seeing year-end figures that are calculated with different assumptions than those used to

[2] *See* 26 CFR 1.430(d)-1(b)(3)(i); 74 FR 53004, 53036 (Oct. 15, 2009).

[3] Section 436(j)(3) of the Code states that if the funding target attainment percentage is 100% or more before the value of plan assets is reduced by the credit balances, the funding target attainment percentage is determined without regard to such reduction for purposes of calculating the adjusted funding target attainment percentage used to determine whether the benefit restrictions and limitations of Code section 436 apply.

calculate beginning-of-the-year figures. To illustrate the confusing effect of the proposal, the commenters explained by way of example that a plan's assets and liabilities as of one second before midnight on December 31 could be dramatically different from that plan's assets and liabilities one second later on January 1, for no reason other than the different assumptions prescribed by paragraphs (b)(3)(i)(A) and (b)(3)(i)(B) of the proposal.

The solution offered by one of these commenters is that the proposal should be revised to mandate use of identical assumptions for both dates. Thus, the same interest rate, mortality, and other actuarial assumptions would be used to determine the present value of both the year-end liabilities for the notice year and the valuation date liabilities of the next plan year. This would eliminate the December 31/January 1 difference described above. In this regard, the commenter suggested using the same assumptions used by the plan sponsor to determine pension liabilities in its SEC filings.

The Department did not adopt this recommendation. Because the disclosure requirements in paragraph (b)(3)(i)(B) of the proposal track the statutory requirements in section 101(f)(2)(B)(ii)(I)(bb) of ERISA, adopting this commenter's recommendation would effectively read these requirements out of the statute. Whatever the differences that might exist between year-end assets and liabilities and the next year's valuation date assets and liabilities, such differences result from the actuarial assumptions and methods mandated by the statute.

Other commenters recommended enhanced disclosure of the assumptions behind the year-end figures, including an explanation of how such assumptions differ from the assumptions used for the beginning-of-the-year (i.e., valuation date) figures. These commenters suggested that enhanced disclosure of this type could be helpful in explaining the December 31/January 1 difference described above. Because paragraph (b)(12) of the final regulation permits plan administrators to add additional or supplemental information to funding notices, if appropriate, the Department decided against mandating the specific disclosures suggested by these commenters.

Finally, the Department, in the preamble to the proposal, recognized that some plans may need to estimate their year-end liabilities for the notice year. For instance, this would be necessary if the plan lacked up-to-date information (e.g., hours of service, compensation, eligibility status, etc.) to calculate year-end liabilities by the due date of the funding notice. The preamble discussion further provided that, inasmuch as section 101(f) of ERISA does not specifically set forth any standards to govern such estimations, pending guidance to the contrary, plan administrators may, in a reasonable manner, project liabilities to year-end using standard actuarial techniques. While the Department specifically solicited comments on this issue, none were received. Accordingly, the Department has no reason at this time to provide contrary guidance.

One commenter noted that instructions to "round off all amounts in this notice to the nearest dollar" located under the "Funding Target Attainment Percentage" chart in Appendix A would be difficult in the context of estimating year-end liabilities. The commenter interpreted these instructions to mean plan administrators must estimate year-end liabilities to the nearest dollar. The Department intended for the rounding instruction to apply to valuation date liabilities used to determine the funding target attainment percentage because by the due date of the funding notice, the valuation date liabilities should be precise to the nearest dollar. Accordingly, no change was made to the rounding instruction in the final version of the model notice. With respect to year-end liabilities, however, the plan should use rounding conventions that are standard for estimating projected plan liabilities and are reasonable with regard to the plan. The Department recognizes that plans may not be able to achieve the same level of precision with respect to estimated year-end liabilities as with valuation date figures.

Multiemployer plans – assets and liabilities as of the valuation date

In the case of a multiemployer plan, paragraph (b)(3)(ii)(A) of the final regulation, like the proposal, requires a statement of the value of the plan's assets (determined in the same manner as under section 304(c)(2) of ERISA) and liabilities (determined in the same manner as under section 305(i)(8) of ERISA, using reasonable actuarial assumptions as required under section 304(c)(3) of ERISA) for the notice year and each of the two plan years preceding the notice year. The assets and liabilities are to be measured as of the valuation date in each of these three years. These are the same assets and liabilities used to determine the plan's funded percentage required to be disclosed under paragraph (b)(2)(ii) of the final regulation. Thus, the recipients of a funding notice will receive not only their plans' funded percentage, pursuant to paragraph (b)(2)(ii), but, pursuant to paragraph (b)(3)(ii)(A), they also will receive the numbers behind that percentage. Under section 305(i)(8) of ERISA, liabilities are determined using the unit credit funding method whether or not that actuarial method is used for the plan's actuarial valuation in general. There were no comments on this provision and it is adopted without change.

Addressing changes in assets and liabilities after the notice is furnished

One commenter requested clarification on whether a plan administrator would be required to issue a revised funding notice for a plan year if the funding percentage data (described by this commenter as valuation date assets and liabilities and the funding percentage derived therefrom) in the notice were to change between the date the notice was furnished to participants and the date of the filing of the plan's Form 5500 Annual Return/Report for that same year. The commenter stated that this might occur, for example, because of an error or mistake in preparing the notice or if a plan were to change its actuarial assumptions in the period between the respective due dates of the notice and the Form 5500. The view of the Department, generally, is that funding percentage data in the notice for a particular plan year should not differ from the funding percentage data that must be reported on that plan's Schedule SB or MB, as applicable, for that same plan year. However, in those rare circumstances where there is a difference because of a good faith error or changes in actuarial assumptions, for example, the view of the Department is that a plan administrator is not obligated by section 101(f) of ERISA to revise and restate the funding notice for that year. If the difference in the data in the notice and the data in the annual report is substantial, plan administrators should consider explaining the discrepancy in the funding notice for the next plan year.

Demographic Information (§ 2520.101-5(b)(4))

Paragraph (b)(4) of the final regulation, like the proposal, requires a statement of the number of participants who, as of the valuation date of the notice year, are: (i) retired or separated from service and receiving benefits; (ii) retired or separated from service and entitled to future benefits (but currently not receiving benefits); or (iii) active participants under the plan. Plan administrators must state the number of participants in each of these categories and the sum of all such participants. For purposes of this statement, the terms “active” and “retired or separated” have the same meaning given to those terms in instructions to the latest annual report filed under section 104(a) of the Act (currently, instructions relating to lines 5 and 6 of the 2012 Form 5500 Annual Return/Report).

In response to one comment, the Department clarifies that beneficiaries of deceased participants should be accounted for in the disclosure of demographic information required under paragraph (b)(4) and should be reflected in the relevant “retired or separated” category based on whether the beneficiary of the deceased participant is receiving benefits or is entitled to receive benefits in the future (but currently is not receiving them). These beneficiaries are similar to retired or separated participants who are themselves receiving, or are entitled to receive, benefits under the plan in that the plan’s liabilities include benefits accrued by such deceased participants.

A few commenters asked the Department to enhance this disclosure requirement by mandating the disclosure of demographic information covering a longer period of time, such as the notice year and two preceding plan years, similar to disclosure of the plan’s funding percentage over a three year period. Such information, they suggest, could help participants and, in the case of multiemployer plans, unions and contributing employers, draw a positive correlation between demographic trends and changes in funding status, e.g., a downward slope in active participants would offer a possible explanation of a declining funding percentage or, possibly, be indicative of such a decline in the future. Other commenters, however, questioned whether such information would be helpful to participants, even if the data allowed for a positive correlation, and pointed out that such information already is publicly available. They also noted that any new disclosure mandate would come at a cost. The Department notes that this data already is required to be reported in the Form 5500 Annual Return/Report, so there would be little cost associated with the commenter’s suggested expansion. Nonetheless, the Department declined to adopt the requested expansion. The Department agrees with the commenters who question the value to participants of the additional information. A plan, for example, may have few active participants and a high funding percentage or many active participants and a low funding percentage. In addition, the statute affords no clear basis for imposing such a requirement. Congress was careful to specify a three-year period in other parts of section 101(f) of ERISA but failed to do so in section 101(f)(2)(B)(iii) of ERISA.

Investment Policy

One commenter was opposed to the proposed requirement to include a “general description of any investment policy of the plan.” The commenter argued that this requirement is not explicitly in the statute, that investment policies often can be complex and lengthy, and that such policies may be irrelevant to participants and beneficiaries.[4] Even though a particular plan's investment policy might be lengthy and complex in its totality, the final regulation requires only a "general description" of the policy. Thus, except in rare cases, the Department does not expect that a plan's entire investment policy would be restated in the annual funding notice. Further, to ensure relevance, the final regulation requires that the general description must relate to the funding policy and asset allocation of investments. The purpose of the requirement to include a "general description of any investment policy of the plan" simply is to provide participants and beneficiaries with contextual information to help them better understand and appreciate the plan's approach to funding benefits.[5] Use of the word "any" in paragraph (b)(5)(iii) reflects that the maintenance of a written statement of investment policy is not specifically required under ERISA, although the Department expects that it would be rare for a plan subject to section 101(f) of ERISA not to have such a policy.

Year-end asset allocation of investments

Section 101(f)(2)(B)(iv) of ERISA, in relevant part, provides that a funding notice must include a statement setting forth "the asset allocation of investments under the plan (expressed as percentages of total assets) as of the end of the plan year to which the notice relates[.]" Like the proposal, paragraph (b)(5)(ii) of the final regulation directly incorporates this statutory requirement. The Department anticipates that plan administrators may satisfy the requirements in paragraph (b)(5)(ii) in any number of ways.

For example, one way a plan administrator may satisfy this requirement is by using the appropriate model notice in the appendices to the final rule. The asset classes in the models are based on the asset classes listed in Part 1 of the Asset and Liability Statement of Schedule H of the Form 5500 Annual Return/Report.[6] Plan administrators who use the models must insert an appropriate percentage with respect to each asset class, using the same valuation and accounting methods as for Form 5500 Schedule H reporting purposes. For this purpose, the master trust investment account (MTIA), common/collective trust (CCT), pooled separate account (PSA), and 103-12 investment entity (103-12IE) investment categories have the same definitions as for the Form 5500 instructions. If a plan held at year-end an interest in one or more direct filing entities (DFEs), i.e., MTIAs, CCTs, PSAs, or 103-12IEs, the plan administrator should include in the model notice a statement apprising recipients how to obtain more information regarding the plan's DFE investments (e.g., a plan's Schedule D and R and/or the DFE's Schedule H). The model notice provides a statement immediately following the asset allocation table for contact

[4] Section 101(f)(2)(B)(iv) of ERISA provides that a funding notice must include "a statement setting forth the funding policy of the plan and the asset allocation of investments under the plan (expressed as percentages of total assets) as of the end of the plan year to which the notice relates[.]"

[5] A requisite feature of every employee benefit plan is a procedure for establishing a funding policy to carry out plan objectives. *See* section 402(b)(1) of ERISA. The maintenance by an employee benefit plan of a statement of investment policy is consistent with the fiduciary obligations set forth in ERISA section 404(a)(1)(A) and (B). A statement of investment policy is a written statement that provides the fiduciaries who are responsible for plan investments with guidelines or general instructions concerning various types or categories of investment management decisions. A statement of investment policy is distinguished from directions as to the purchase or sale of a specific investment at a specific time. *See* 29 CFR 2509.08-2(2) (formerly 29 CFR 2509.94-2).

[6] *See* lines 1a, 1c, 1d and 1(e) of the 2012 Schedule H. The asset classes identified in the models do not include any receivables reportable on Schedule H of the Form 5500 (*see* lines 1b(1)-(3) of the 2012 Schedule H).

information, which a plan administrator should complete and include if the plan held an interest in one or more DFEs. The reason for this special treatment for plans investing in DFEs is that such plans often do not know the precise year-end holdings of a DFE by the due date of the annual funding notice. One commenter questioned whether this special treatment is appropriate for single-employer plans that use MTIAs, on the theory that administrators of such plans have more control over and access to information about such investment arrangements than, say, CCTs. Given that plan fiduciaries have a duty not to misrepresent material information relating to the plan, plan administrators should not report a percentage interest in MTIAs if they know the MTIA's actual asset allocation sufficiently in advance of the due date of the annual funding notice. Instead, they should use the other asset categories in Schedule H.

A number of commenters on the proposal favored the asset categories in Schedule R over the asset categories in the Schedule H. The Schedule R categories are stocks, investment-grade debt, high-yield debt, real estate, and other. These commenters suggested either replacing the Schedule H approach in the model notice with the categories in Schedule R, or perhaps establishing the Schedule R approach as an alternative to the Schedule H approach. In some cases the asset categories in Schedule R may better align with a plan's investment policy. In other cases, the asset categories in the Schedule R may be more informative to participants and beneficiaries. For these reasons, the Department has determined that the Schedule R asset categories are an acceptable alternative to the asset categories in the Schedule H for purposes of the model notices in the appendices to the final rule. Thus, the Department is of the view that a plan administrator may substitute the Schedule R categories for asset categories in Schedule H in the model notices, and remain eligible for the relief provided in paragraph (h) of the final regulation. Plan administrators who use the Schedule R alternative must insert an appropriate percentage with respect to each asset class.

Another commenter suggested allowing the plan administrator discretion when using the model notice to break out the investments held in a DFE among the other Form 5500 Schedule H asset classes where the plan administrator knows the underlying make-up of the assets held by the DFE. The Department never intended to preclude plan administrators from breaking out the DFE's investments among the other asset classes, since the disclosure of such information will better inform participants about the plan's asset allocation of investments. To make this option clear, the final model notice instructions expressly permit plan administrators to break-out DFE investments in the notice, or to include a statement informing participants how to get additional information regarding DFE investments. See the model notice in appendices A and B.

One commenter recommended deleting the phrase "Under the plan's investment policy" from the section of the model notice addressing the year-end percentage allocation of investments. The commenter believes this language implies that the allocation percentages reflect the investment policy. The commenter opposes this implication because the asset allocation percentages under paragraph (b)(5) of the regulation are a snapshot of information and may not accurately reflect the plan's long-term investment policy. The Department declined to adopt this recommendation. The commenter appears to be concerned with inferences of wrongdoing or investment imprudence that might be drawn by participants and others if their plan's asset allocation percentages do not precisely match the plan's investment policy, and believes those inferences would be less likely with the recommended deletion. The Department disagrees with the commenter that the quoted phrase would imply wrongdoing if the asset allocation differed from the investment policy. The objective of the disclosures under paragraph (b)(5), in the aggregate, is to help participants and other recipients understand that there is a relationship between funding, investment policies, and asset allocations. The commenter's recommendation appears to run contrary to that objective.

Material Effect Events (§ 2520.101-5(b)(7) and § 2520.101-5(g))

Paragraph (b)(7) of the proposed regulation directly incorporated the requirements of section 101(f)(2)(B)(vi) of ERISA, which requires: "in the case of any plan amendment, scheduled benefit increase or reduction, or other known event taking effect in the current plan year and having a material effect on plan liabilities or assets for the year (as defined in regulations by the Secretary), an explanation of the amendment, schedule increase or reduction, or event, and a projection to the end of such plan year of the effect of the amendment, scheduled increase or reduction, or event on plan liabilities [.]"

Beyond this direct incorporation, the Department took three other steps in the proposal to clarify and implement the material effect requirements.

First, the preamble to the proposal noted ambiguity with respect to the term "current plan year" in the language quoted above. The question is whether this term refers to the notice year or the plan year following the notice year. The proposal adopted the view that such term means the plan year following the notice year (i.e., the plan year in which the notice is due). Thus, for a calendar year plan that must furnish its 2010 annual funding notice no later than the 120th day of 2011, the "notice year" is the 2010 plan year and the "current plan year" for purposes of paragraph (b)(7) of the proposal is the 2011 plan year. The Department's rationale for this interpretation, as explained in the preamble of the proposal, was that it is difficult to find meaning in the phrase "a projection to the end of such year" if "current plan year" is interpreted to mean the notice year because the notice year has already ended. Comments were solicited on this issue specifically.

Second, in an effort to bring clarity to the language "having a material effect on plan liabilities or assets for the year" in section 101(f)(2)(B)(vi) of ERISA, the proposal set forth two tests for determining whether an event has a material effect on assets or liabilities. The first test, at paragraph (g)(1)(i) of the proposal, provided that a plan amendment, scheduled benefit increase (or reduction), or other known event has a material effect on plan liabilities or assets for the current plan year if it results, or is projected to result, in an increase or decrease of five percent or more in the value of assets or liabilities from the valuation date of the notice year. For example, if the liabilities of a calendar year plan were $100 million on January 1, 2010, (the valuation date for the 2010 notice year), a scheduled increase in benefits taking effect in 2011 will have a material effect if the present value of the increase, determined using the same actuarial assumptions used to determine the $100 million in liabilities, equals or exceeds $5 million. Under the second test, an event has a material effect on plan liabilities or assets for the current plan year if, in the judgment of the plan's enrolled actuary, the event is material for purposes of the plan's funding status under section 430 or 431 of the Code, without regard to an increase or decrease of five percent or more in the value of assets or liabilities from the prior plan year. The second test is in paragraph (g)(1)(ii) of the proposal.

Third, the preamble to the proposal also specifically solicited comments on an issue addressed in the Department's Field Assistance Bulletin 2009-01 (February 10, 2009). In that Bulletin, the Department provided interim guidance under section 101(f) of ERISA in the form of an enforcement policy. Under this policy, if an otherwise disclosable event first became known to the plan administrator 120 days or less before the due date for furnishing the funding notice, the administrator did not have to disclose the event in the notice. See Question 12 of FAB 2009-01. The rationale behind this policy is that at some close point in time before the due date for furnishing the notice, it becomes impracticable for, and unreasonable to expect, plan administrators to satisfy the detailed material effect provisions even though an otherwise disclosable event is known. In addition, the event's effect on the plan's assets and liabilities will in any event be reflected in the next annual funding notice. This policy was not included in the operative text in the proposal. However, the preamble to the proposal solicited comments on whether this 120-day "rule" should be included in the final regulation.

In general, the public comments on the material effect provisions focused on the 120-day policy articulated in FAB 2009-01 and its absence from the operative text of the proposal. One commenter, however, criticized the position of the Department on the "current plan year" language. This person is concerned that some material events would not be covered if "current plan year" means the plan year following the notice year. Another commenter believes the five percent test to determine materiality is unnecessary in light of the actuary judgment test. This commenter, therefore, recommends deleting the five percent test. This commenter also asked the Department to consider a third alternative based on Code section 436.

"Taking effect" and "current plan year"

As mentioned above, one commenter raised a concern that by interpreting "current plan year" as the year after the notice year, as opposed to the notice year itself, the proposal effectively created a loophole that might result in a substantial number of events not being covered by the material effect disclosure provisions. To illustrate the commenter's point, assume the same facts as in the example above. Also assume the amendment was not known by the plan administrator before January 1, 2014. Applying the proposal, the early retirement amendment would not be explained in the 2014 notice because it does not take effect in the current plan year (i.e., 2015). Nor would the amendment be explained in the 2013 notice because it was not known by the plan administrator more than 120 days before the deadline of that notice.

New paragraph (g)(2) of the final regulation addresses this loophole. Specifically, it states that "[a]n event described in paragraph (b)(7) is recognized as 'taking effect' in the current plan year if the effect of the event is taken into account for the first time for funding under section 430 or 431 of the Internal Revenue Code, as applicable." Thus, a material effect event is recognized as "taking effect" in the first plan year that the effect of the event is taken into account for funding. Events occurring in the notice year, therefore, would not escape disclosure as feared by the commenter, if the effect of the event is taken into account for funding for the first time in a subsequent plan year. The term "taking effect" under the final regulation does not have the same meaning as "take effect" under Code sections 430 and 436 and the regulations promulgated thereunder.

Materiality – the five percent test

As noted above, one commenter recommended eliminating the five percent materiality test on the grounds that it is unnecessary in light of the actuary judgment test. It is unnecessary, according to this commenter, because five percent events are the kind of events that also would be considered material to funding under the actuary judgment test. From this premise, the commenter argues that plans should not have to incur the cost of performing an unnecessary test. No data were provided regarding potential cost savings if the recommendation were adopted. The Department does not agree that the actuary judgment test makes the five percent test unnecessary. The five percent test is an objective test; it has all the certainty of a bright line, numerical test. It ensures that participants will be informed automatically of any event if its financial impact meets or exceeds this percentage. The plan has no discretion when the effect of an event is at or above the established numerical threshold. It effectively reflects the Department's determination of baseline materiality for purposes of section 101(f) disclosures, without regard to what a plan, or its enrolled actuary, may think of the significance of the event. The actuary judgment test in the proposal, by contrast, operates underneath the five percent ceiling. Below the ceiling, the plan has discretion and is not required to explain the effect of each and every event that has any effect on assets or liabilities. Instead, disclosure is required only if the plan's actuary determines the effect of the event is material for funding purposes. Even if, as is suggested by the commenter, there is some overlap in the two-test approach in the proposal, the framework recommended by the commenter would lack the certainty and consistency of the proposal and it would confer too much discretion on the plan to decide whether and what events are material under section 101(f) of ERISA. For these reasons, the Department declined to adopt this commenter's recommendation, and the final rule therefore continues to contain the five percent test.

As mentioned above, if, in the judgment of the plan's enrolled actuary, the effect of an event is material for purposes of the plan's funding status under section 430 or 431 of the Code, paragraph (g)(1)(ii) of the proposal deemed the event to have a material effect under paragraph (b)(7). The final rule retains this provision. See paragraph (g)(4). The purpose of this "actuary judgment test" is to disclose any event that is not picked up by the five percent test which the actuary determines has a material effect on the funding status of the plan under section 430 or 431 of the Code (sections 303 and 304 of ERISA). Although the actuary's exercise of judgment under paragraph (g)(4) of the final regulation would not ordinarily rise to the level of fiduciary conduct, see 29 CFR 2509.75-5 D-1, it is expected that the plan's enrolled actuary will make a determination under paragraph (g)(4) in a manner that is consistent with the standards for performance of actuarial services set out in 20 CFR 901.20.

Other known events

Paragraph (g)(2) of the proposal contains a non-exclusive list of events that could constitute an “other known event” for purposes of paragraph (b)(7) of the regulation. Paragraph (g)(6) of the final rule retains this list with two noteworthy modifications. First, the examples in paragraph (g)(2)(iv) and (v) of the proposal, relating to a retirement window benefit and a cost-of-living increase for retirees, were eliminated because they describe events that typically do not happen in the absence of a plan amendment or scheduled benefit increase. Since such events constitute amendments or increases already covered by other language in the regulation, the Department, on reflection, determined that the two examples were not very helpful and possibly misleading. The second change clarifies that the Department does not view general market fluctuations (as compared to a fraud, such as a Ponzi scheme, or other similar event affecting the value of a specific investment) as an event contemplated by the material effect disclosure provision in section 101(f) of ERISA. Market fluctuations theoretically could result in numerous, yet offsetting, material effect disclosures all in the same funding notice. For instance, assume a precipitous decline in the equity market in a given month results in a 10 percent reduction in the value of a plan’s assets. Also assume the decline is followed by a market correction in the next month and the correction results in a 10 percent increase in the fair market value of the plan’s assets. Thus, although the plan has no net gain or loss over this two month period, its assets have changed more than five percent twice during this time. Such a decline and correction could happen over the course of two days rather than two months. The Department agrees with the commenters who believe that this kind of information is not likely to be very helpful or informative to participants in defined benefit plans, and possibly confusing to them. The Department also thinks it would be administratively burdensome for small plans to track and explain market fluctuations. Accordingly, the proposal was modified and paragraph (g)(6) of the final regulation clarifies that market fluctuations are not “other known events” for purposes of the material effect disclosure requirement in paragraph (b)(7), and are not required to be explained or projected in funding notices. The Department is of the view that a voluntary explanation of the effect of a market fluctuation could be added to the notice pursuant to paragraph (b)(12) of the final rule, if the plan administrator determined that the explanation would be helpful and the explanation is not misleading or confusing.

Finally, we have been asked if changes in actuarial assumptions constitute a material event for this purpose. The Department is not prepared to conclude categorically that changes in actuarial assumptions should never be subject to the material event disclosure provisions. Minor changes in actuarial assumptions or methods sometimes can result in substantial increases or decreases in liabilities whether the change in assumptions arises by operation of law, from an election or action of the plan sponsor, or automatically under the terms of the plan. Disclosure of a change in actuarial assumptions or methods could help participants better understand a material increase or decrease in the value of the plan’s liabilities. Consequently, such changes have not been given the same treatment as market fluctuations and, therefore, in deciding whether such changes trigger disclosure, plans must determine whether, in the aggregate, any change or changes in actuarial assumptions or methods are material under the applicable tests.

Projection of Liabilities

The Department received a number of inquiries regarding the requirement in section 101(f)(2)(B)(vi) of ERISA to project the effect of a material effect event on liabilities to the end of the current plan year. Section 101(f)(2)(B)(vi), in relevant part, requires "a projection to the end of such plan year of the effect of the amendment, scheduled increase or reduction, or event on plan liabilities[.]" The inquiries illustrated numerous approaches to carry out such projection and asked whether the Department contemplated a specific methodology. The Department does not contemplate a single projection method. The Department expects only that plan administrators act reasonably and in good faith when choosing a projection method. A reasonable interpretation of the projection requirement would be to show liabilities with and without the material effect event as of last day of the current plan year based on the interest rate as of the valuation date of the notice year, with the difference expressed as a percentage, dollar amount, or both. For example:

Plan Liabilities Before the Scheduled Benefit Increase	Plan Liabilities After the Scheduled Benefit Increase	Increase in Liabilities	Percentage Change
$ 525 million	$ 5 57 million	$ 32 million	6%

The projection requirement in section 101(f)(2)(B)(vi) of ERISA applies to any material effect event. However, paragraph (g)(7) of the final regulation gives plan administrators the option of foregoing projections in limited situations. Specifically, if an event is not expected to change the plan's liabilities by five percent or more, then a projection is not required, but the funding notice must contain an explanation of why the specific event is considered material. This special provision will reduce administrative burdens on plans because they will not have to perform projections, which may be complex and time consuming. At the same time, participants and beneficiaries will not be adversely affected by the special provision because they will receive an explanation of why the event is considered material. Knowing why an event is considered material may be significantly more helpful to participants and beneficiaries than the projection contemplated by section 101(f)(2)(B)(vi).

PBGC Guarantees (§ 2520.101-5(b)(9))

Paragraph (b)(9) of the final regulation, like the proposal, requires a funding notice to include a general description of the benefits under the plan that are eligible to be guaranteed by the PBGC, and an explanation of the limitations on the guarantee and the circumstances under which such limitations apply. The requirement in paragraph (b)(9) directly incorporates the requirements of the statute. See section 101(f)(2)(B)(viii) of ERISA. One commenter observed that the information required under paragraph (b)(9) is somewhat similar to information that pension plans already must include in their summary plan descriptions pursuant to 29 CFR 2520.102-3, although the commenter also noted that the funding notice is an annual disclosure and the summary plan description is not. This commenter asked the Department to consider exercising its authority under section 110 of ERISA to establish an alternative method of compliance under which a plan administrator's obligation under paragraph (b)(9) of the regulation (and, therefore, section 101(f)(2)(B)(viii) of ERISA) would be considered satisfied if the plan administrator otherwise complied with summary plan description requirements under

§2520.102-3. Section 110 of ERISA grants the Secretary of Labor authority to prescribe an alternative method of compliance for any requirement of part 1 of subpart B of title I of ERISA, under certain circumstances, if the Secretary makes certain findings, including that the requirement would increase the costs to or impose unreasonable administrative burdens on the plan and be adverse to the interests of plan participants in the aggregate and that the alternative is consistent with the purposes of title I of ERISA and provides adequate disclosure to the participants and beneficiaries in the plan. The public record, however, does not contain sufficient information on whether, and to what extent, the specific content requirement of section 101(f)(2)(B)(viii) would increase the costs to plans or impose unreasonable administrative burdens. Nor does it contain sufficient information on whether, and to what extent, the specific content requirement of section 101(f)(2)(B)(viii) would be adverse to the interests of plan participants in the aggregate. In the absence of such information, and evidence that the proposed alternative method provides adequate disclosure to the participants and beneficiaries in the plan, the Department is unable to accommodate the commenter's request. Nothing in this final rule, however, precludes the commenter, or any other interested person, from pursuing this matter further with the Department in the future and supplying the information needed for the Department to make the requisite determinations under section 110 of ERISA.

Timing Requirements (§ 2520.101-5(d))

Paragraph (d) of the final regulation, like the proposal, describes when a funding notice must be furnished to recipients. Paragraph (d)(1) provides that notices generally must be furnished not later than 120 days after the end of the notice year. Paragraph (d)(2) provides that in the case of small plans, notices must be furnished no later than the earlier of the date on which the annual report required by section 104 of ERISA is filed or the latest date the report could be filed (with granted filing extensions). For this purpose, a plan is a small plan if it had 100 or fewer participants on each day during the plan year preceding the notice year. See section 101(f)(3)(B) of ERISA (referencing section 303(g)(2)(B) of ERISA). Although section 303(g)(2)(B) of ERISA relates to single-employer plans only, the Department interprets section 101(f)(3)(B) of ERISA as applying the 100 or fewer participant standard in section 303(g)(2)(B) of ERISA to both single-employer and multiemployer plans.

One commenter recommended that the deadline for furnishing the funding notice for large plans be shortened from no later than 120 days after the end of the notice year to no later than 180 days after the valuation date of the notice year. This would accelerate the deadline by approximately 10 months for plans whose valuation date is January 1. The commenter favors timelier information. The Department also favors timely information for participants and beneficiaries. However, the statutory deadline is clear and unambiguous, thereby limiting the Department's authority to accept this comment under section 101(f) of ERISA. In addition, adopting the commenter's recommendation would make it impossible for many plan administrators to comply with other content requirements in section 101(f) of ERISA. For instance, section 101(f)(2)(B)(iv) of ERISA requires that funding notices contain a statement setting forth the asset allocation of investments under the plan as of the end of the plan year. For plans with a January 1 valuation date, the plan administrators could not comply with the foregoing requirement because the end of the plan year always would be after the 180-day deadline recommended by the commenter. Accordingly, the Department did not adopt this recommendation.

Persons Entitled to Notice (§ 2520.101(5)(f))

Paragraph (f) of the proposed regulation defines a person entitled to receive a funding notice as: each participant covered under the plan on the last day of the notice year, each beneficiary receiving benefits under the plan on the last day of the notice year, each labor organization representing participants under the plan on the last day of the notice year, the PBGC, and, in the case of a multiemployer plan, each employer that, as of the last day of the notice year, is a party to the collective bargaining agreement(s) pursuant to which the plan is maintained or who otherwise may be subject to withdrawal liability pursuant to section 4203 of ERISA.

One commenter asked for clarification whether alternate payees must be furnished annual funding notices under this provision. The language in the proposal could be read as mandating disclosure to alternate payees only after they have entered pay status. We agree with the commenter that there is a need for further clarification on this issue. Section 206(d)(3)(J) of ERISA, in relevant part, explicitly states that "a person who is an alternate payee under a qualified domestic relations order shall be considered for purposes of any provision of this Act a beneficiary under the plan." Section 101(f) of ERISA, in relevant part, states that for each plan year the plan administrator shall provide a funding notice to "each plan participant and beneficiary." Unlike the summary plan description and summary annual report requirements of sections 104(b)(1) and 104(b)(3) of ERISA, respectively, the annual funding notice disclosures are not limited expressly to beneficiaries "receiving benefits under the plan." Of course, the Department is concerned that furnishing annual funding notices to all beneficiaries could result in costs and burdens that outweigh the benefits. However, the Department agrees with the commenter that alternate payees, especially those who have a separate interest qualified domestic relations order, have an interest in the plan's funding status equal to the other categories of persons entitled to notices listed in paragraph (f) of the proposal. The Department, therefore, has provided the clarification requested by the commenter by adding "[e]ach alternate payee under the plan on the last day of the notice year…" to the list of persons entitled to a funding notice under paragraph (f) of the final regulation. See § 2520.101-5(f)(3).

Another commenter suggested that plan administrators should have the option of using either the first or last day of the notice year to determine whether someone is entitled to a notice, subject to a consistency rule. According to this commenter, valuation date data may be the most up to date data available to a plan sponsor without additional cost and effort to the plan. In the Department's view, however, the identity of each participant and alternate payee covered under the plan and each beneficiary receiving benefits on the last day of the plan year should be readily available to the plan administrator by the due date of the funding notice. The commenter offers no empirical data showing a cost differential between valuation date determinations and determinations on the last day of the plan year. In addition, if, in accordance with the commenter's recommendation, the participant/beneficiary population were determined on the valuation date, which is generally the first day of the plan year, any individuals who become participants, alternate payees or beneficiaries receiving benefits during the notice year would not receive a notice for that year. For these reasons, the Department did not adopt the commenter's suggestion.

Model Notices (§ 2520.101-5(h))

The appendices to § 2520.101-5 include two model notices (one for single-employer plans and one for multiemployer plans) that may be used by plan administrators for purposes of section 101(f) of ERISA. The model in Appendix A is for single-employer plans (including multiple employer plans) and the model in Appendix B is for multiemployer plans. These models are intended to assist plan administrators in discharging their notice obligations under section 101(f) of ERISA and the regulation. Use of a model notice is not mandatory. However, the regulation provides that use of a model notice will be deemed to satisfy the content requirements in paragraph (b) of the regulation, as well as the style and format requirements in paragraph (c) of the regulation.

The Department solicited comments on how the models could be improved to enhance understandability and comprehensibility. One commenter submitted an alternative to the Department's model for single employer plans. This alternative essentially would move definitions and descriptions to a glossary at the end of the notice on the premise that it would help participants to focus on the funding status data located in the chart in the front of the notice. Another commenter subjected both notices to a passive sentences readability test, the Flesch Reading Ease Test, and the Flesch-Kincaid Grade Level Test. The tests were applied to both models and to each paragraph within the models. Both models are below the suggested readability scores according to the commenter. This commenter recommended improving readability by replacing much of the content in the models with a single sentence; for single-employer plans, the sentence would state whether the plan is or is not "at risk;" for multiemployer plans, the sentence would state whether the plan is a "green, yellow, orange or red" zone plan. Another commenter encouraged the Department to create a model notice that does not exceed a single page. This commenter would limit the content to the name of the plan, the funded percentage, the dollar amount of the shortfall, the risk of not being able to fund pension obligations, a description of the plan sponsor's plan to reduce such risk, and an explanation of how to get more information, in order to meet the one page standard. Other miscellaneous comments were made to improve the single-employer plan model. Many of these comments focused on emphasizing or deemphasizing certain information relative to other information, such as, for example, emphasizing the fact that the notice is "required by law."

The Department retained the general framework of the proposed models. The Department was unable to accommodate the single page and single sentence approaches discussed above without eliminating statutorily mandated information. However, the models were revised to eliminate passive sentences where possible. Modifications to address the Flesch scores, on the other hand, were more difficult given the nature of the specific disclosure requirements under section 101(f) of ERISA. Nonetheless, where possible, lengthy sentences were made shorter and more concise, funding jargon was removed, and readability was improved determined using the same testing methods used by the commenter. The Department was not persuaded that the alternative with a glossary, submitted by one commenter, is any more userfriendly or understandable than the models appended to the final rule. Finally, the opening paragraph of the models now contains the following sentence: “The notice is required by federal law.”

The Department’s intent behind models, in part, is to ease the burden on plan administrators by providing model language to satisfy applicable regulatory requirements. As noted above, use of a model notice is not mandatory. To the extent a plan administrator elects to include in a model notice additional information described in paragraph (b)(12) of the regulation, such additional information must be consistent with the style and format requirements in paragraph (c) of the regulation. Thus, such additional information should not have the effect of misleading or misinforming recipients.

Alternative Method of Compliance for Multiemployer Plans that Terminate by Reason of Mass Withdrawal (§ 2520.101-5(k))

The Department sought comments on whether a special rule should be provided for multiemployer plans that terminate by mass withdrawal pursuant to ERISA section 4041A(a)(2). ERISA section 4041A(a)(2) provides that the termination of a multiemployer plan occurs as a result of the withdrawal of every employer from the plan or the cessation of the obligation of all employers to contribute under the plan. Specifically, the Department noted that while some information required by the regulation may not be relevant, other information, such as PBGC guarantee levels, assets and liabilities, participant status, and insolvency information may still be important to participants and beneficiaries receiving benefits from such plans. Specific comments were requested on whether a special rule should be provided, and if so, information that should be excluded from the notice as well as the information that should be included, and any data on cost savings as a result of a special rule.

Commenters made the following observations about these plans. First, the minimum funding standards cease to apply to these plans and the Schedule MB of the Form 5500 is no longer required. Second, because of that, the Code’s critical/endangered status rules become inoperable. Third, since the minimum funding and Schedule MB reporting requirements no longer apply, there is no reason for the plan’s enrolled actuary to perform a funding valuation. Thus, information needed to satisfy section 101(f) and the requirements of the regulation is not readily available. Fourth, the actuarial and other costs needed to generate such information will be borne entirely by the participants and beneficiaries because there are no contributing employers to defray the costs. Fifth, participants in these plans might be better served with different or less information than is otherwise included in an annual funding notice.

Based on the foregoing, the Department has adopted an alternative method of compliance in paragraph (k) of the final regulation for plans that terminate pursuant to section 4041A(a)(2) of ERISA. These plans no longer have any contributing employers and, therefore, typically have no cash in-flow other than investment return and, perhaps, withdrawal liability payments. Thus, such a plan exists merely to pay benefits to participants, until such time as the plan's trust runs out of money. This "wasting trust" period often can span several years depending on the particular plan.

The rules in paragraph (k), on the one hand, acknowledge that such plans hardly ever have all the section 101(f) information because they are no longer required to comply with the minimum funding rules. At the same time, however, these rules acknowledge that participants and beneficiaries continue to have an interest in the funding status of the plan during the wasting trust period. Thus, instead of the specific funding information required by the regulation more generally, the final rule allows plan administrators of a plan terminated by mass withdrawal to comply with the annual funding notice rules under ERISA section 101(f) through this alternative method. The rules in paragraph (k) focus mainly on the plan's assets and benefit payments being made so that participants are able to draw a rough estimate of how long the plan will be able to pay benefits. Paragraph (k) also focuses on information about PBGC guarantees, insolvency and possible benefit reductions, i.e., the kind of information that is directly relevant to participants when their plan is in this situation. The rules do not require disclosure of this special notice to labor organizations representing participants, contributing employers, or the PBGC under paragraphs (f)(4), (5), and (6) of the final regulation.