Pension ANALYST
COMPLIANCE BULLETIN

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Removing Old Minimum Payment Rules from Defined Contribution Plans

The IRS recently published final rules that let plan sponsors remove the old minimum payment rules from their plan documents without violating the protected benefit rules. These special rules do not apply to governmental plans or non-electing church plans, which have always been subject to the new minimum payment rules.

Last year, the IRS provided two alternatives for permanently dealing with the minimum payment rule changes made by the Small Business Job Protection Act of 1996 (SBJPA). Plan sponsors could:

1. Permit employees who are not 5% owners and are no longer required to begin receiving plan payments while they are still employed after reaching age 70½, the choice to begin receiving payments at age 70½ while still employed.
2. Eliminate the age 70½ payment "option" for actively employed non-5% owners, but only with respect to benefits that had not been earned as of the later of the date plan amendment adoption date or effective date.

New Alternative

The IRS is now offering a third, more attractive, alternative. A plan sponsor may amend its plan to remove completely the preretirement age 70½ payment provision for employees who are not 5% owners. However, this provision may only be eliminated for employees who reach age 70½ after December 31, 1998, or, if later, in calendar years beginning after the amendment adoption date.

For example, a plan sponsor may amend its plan to provide that employees who are not 5% owners and reach age 70½ after December 31, 1998, will not be able to receive plan payments until they terminate employment with the employer. However, the plan sponsor must adopt this amendment by December 31, 1998. If the plan sponsor waits until 1999 to adopt this amendment, it cannot apply to employees who reach age 70½ in 1999, but only to employees who reach age 70½ in 2000 or later.

Employees who are not 5% owners and reach age 70½ at any time before January 1, 1999, must be allowed to receive plan payments once they reach age 70½, as required under the old minimum payment rules. The IRS felt that these employees' age 70½ payment "option" had to be protected because their retirement planning may have been based on the belief that they would receive these payments.

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Amendment Timing

Plan sponsors that want to eliminate the preretirement age 70½ payment provision using the new approach must adopt the appropriate plan amendment by the last day of the plan's SBJPA amendment period. Generally, the SBJPA amendment period ends on the last day of a plan's 1999 plan year (December 31, 1999, for a calendar plan year).

However, the deadline for making this particular amendment to ***a collectively-bargained plan*** is the later of (1) the standard SBJPA amendment deadline, or (2) the last day of the 12th month beginning after the expiration of the last collective bargaining agreement that was ratified before September 3, 1998.

Timing Considerations

Plan sponsors that want to amend plans to remove the preretirement age 70½ payment provision as soon as possible (i.e., effective for non-5% owners who reach age 70½ in 1999) under the new alternative need to ***take action as soon as possible***. A Board of Directors' resolution making this change must be adopted by December 31, 1998, if it is to be effective for a plan year beginning January 1, 1999. In no event should an employer that has adopted a Prototype or Volume Submitter plan adopt a formal Plan amendment to make this change instead of or in addition to a Board of Directors' resolution, or that Plan will lose its Prototype or Volume Submitter status.

Special Rule for Profit Sharing and 401(k) Plans

A profit sharing plan, including a 401(k) plan, that lets employees take in-service distributions after age 59½ (or at any age before 70½), at any time and in any amount, does not have to be amended to protect the old minimum payment rules. Instead, the plan sponsor may simply amend such a plan to remove the old minimum payment rules and replace them with the new minimum payment rules, as long as the age 59½ payment option remains available.

While the IRS does not say so directly, it appears that a profit sharing plan or 401(k) plan that currently does not offer an age 59½ distribution option could be amended to add such a provision, while also removing the old minimum payment rules.

Next Steps

If you do not want to keep the old minimum payment rules in your plan, you should take action as soon as possible. Your choice of amendment alternative should be formalized by a Board of Directors' resolution and communicated to participants by a Summary of Material Modifications (SMM).

If you have questions regarding these minimum payment rules and alternatives, please contact your Prudential Retirement representative.

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