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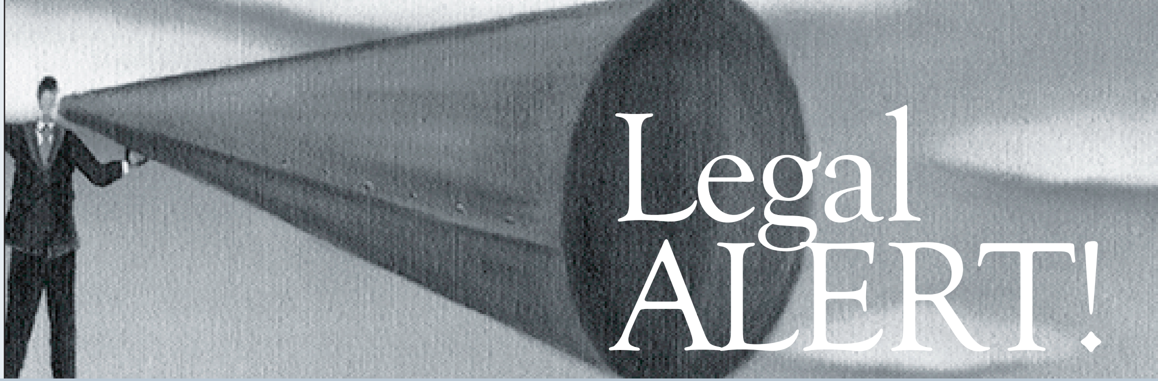

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IRS Permits Employees to Contribute Unused Paid Time-Off to 401(k) Plans: Rulings are Part of a New Administration and Treasury Initiative to Boost Retirement Savings

On September 4, 2009 the IRS announced that a 401(k) plan may accept the dollar equivalent of unused paid time off at year-end as an additional employee salary deferral contribution to the Plan (Rev. Rul. 2009-31). In a companion ruling, the IRS held that a 401(k) plan can also accept as an employee salary deferral contribution the value of unpaid time off of a terminated employee upon severance of employment. The new rulings are intended to allow employees to convert unused leave into retirement savings. Employers are not required to offer this feature to plan participants. If an employer wishes to offer the feature to its employees, the employer must amend its 401(k) plan to permit such contributions.

These revenue rulings are part of a blitz of guidance by the IRS to increase retirement savings. Other guidance includes:

IRS to Permit Use of Tax Refund to Purchase U.S. Savings Bonds. Beginning in the 2010 tax filing season (for filing 2009 tax returns), taxpayers can direct the IRS to use their tax refunds to purchase Series-I United States Savings Bonds. For the 2010 filing season, taxpayers who elect to use their tax refunds to purchase savings bonds will receive savings bonds issued in the name or names reflected on the taxpayer's return. Beginning in the 2011 tax filing season, taxpayers will be able to purchase savings bonds in their names and a co-owner's name (*e.g.*, child or grandchild). The IRS has posted 19 new "Q&As" to its website explaining the program.

Automatic Enrollment and Contribution Guidance. The IRS has issued additional guidance intended to make it easier for employers to automatically enroll participants in 401(k) plans and SIMPLE IRAs.

In Notice 2009-65, the IRS provided two pre-approved automatic enrollment amendments for sponsors, practitioners, and employers who want to add automatic contribution features to their 401(k) plans. The IRS also issued two notices relating to automatic enrollment in SIMPLE IRAs. Notice 2009-66 provides Q&As to facilitate automatic enrollment of participants in SIMPLE IRA plans. Notice 2009-67 provides a sample plan amendment that can be used by prototype sponsors of SIMPLE IRAs (generally, designated financial institutions) to provide for automatic contribution arrangements.

The IRS also issued guidance expanding the factors that a 401(k) plan may use to provide for automatic increases in default contributions in a plan providing for

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automatic contributions (*i.e.* a plan that provides for a default contribution at a certain rate for the first year and automatically increases that rate in each subsequent year unless the participant elects otherwise). In Revenue Ruling 2009-30, the IRS held that automatic increases may be computed by reference to increases in an employee's base compensation (*e.g.* a 1% increase in the automatic contribution for each 5% increase in base compensation).

Updated IRS Website. In connection with the new savings initiative, the IRS has revamped the section of its website carrying retirement plan savings options for employees (http://www.irs.gov/retirement/article/0,,id=212061,00.html).

Renewed Push for Congressional Action. The Obama Administration used the occasion of the Treasury's retirement security initiative to press Congress to enact two retirement savings proposals carried in the President's 2010 budget proposal. These proposals include a mandatory employer-based IRA program for employers that do not sponsor a retirement plan for their employees. Under the proposal, employers would be required to automatically enroll employees and process contributions to IRA accounts via payroll deposit contributions. A second Administration proposal would expand Savers Tax Credit. Under this proposal, the Treasury would match one-half of families' savings up to $500 per individual each year and deposit the tax credits directly into the individual's 401(k) plan account or IRA.

The principal author of this Alert is Raymond N. McCabe. Please contact Mr. McCabe or any member of our Labor and Employment Practice Area if you have any questions.

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