



The
ERISA
Industry
Committee

August 14, 2009

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Room 5203
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, D.C. 20044

Ladies and Gentlemen:

The ERISA Industry Committee (“ERIC”) is pleased to submit this comment on the proposed regulations amending §§ 1.401(k)-3 and 1.401(m)-3 to permit the reduction or suspension of qualified non-elective contributions (“QNECs”) in “safe harbor” section 401(k) plans, as published in the *Federal Register* on May 18, 2009, at 74 Fed. Reg. 23,134. A QNEC is a type of contribution by an employer that is designed to satisfy the nondiscrimination rules applicable to 401(k) plans.

ERIC is a nonprofit association committed to the advancement of the employee retirement, health, incentive, and welfare benefit plans of America’s largest employers. ERIC’s members provide comprehensive retirement, health care coverage, incentive, and other economic security benefits directly to some 25 million active and retired workers and their families. ERIC has a strong interest in proposals affecting its members’ ability to deliver those benefits, their costs and effectiveness, and the role of those benefits in the American economy.

ERIC appreciates the efforts of Treasury and the Service to provide relief to section 401(k) plan sponsors who are suffering in the midst of the worst economic environment in many decades. By recognizing and responding to the financial downturn, Treasury and the Service increase the likelihood that employers will adopt and maintain employee benefit plans, one of the original overarching goals of ERISA.

The proposed regulations would permit an employer to reduce or suspend QNECs that otherwise would provide a design-based safe harbor that would automatically satisfy the automatic deferral percentage (“ADP”) and actual contribution percentage (“ACP”) tests as applicable to the plan. The proposed relief is substantially similar to existing regulations (Treas. Reg. § 1.401(k)-3(g)) that permit the reduction or suspension of qualified matching contributions (“QMACs”). However, unlike relief from QMAC contributions, the proposed regulations would permit relief from QNEC contributions only if the plan sponsor incurs a “substantial business hardship.”

The proposed regulations define a “substantial business hardship” as “comparable to a substantial business hardship described in section 412(c)” of the Internal Revenue Code (the “Code”). Code section 412(c) provides factors that the Service shall take into account to determine whether to grant an application for a waiver of the annual funding requirements. The factors include whether or not:

- (A) the employer is operating at an economic loss,
- (B) there is substantial unemployment or underemployment in the trade or business and in the industry concerned,
- (C) the sales and profits of the industry concerned are depressed or declining, and
- (D) it is reasonable to expect that the plan will be continued only if the waiver is granted.

A plan sponsor should not be required to incur a substantial business hardship in order to reduce or suspend QNECs. The analogy to a funding waiver is misplaced. While sponsors of defined benefit plans (and, in some cases, defined contribution plans) are required to comply with the funding requirements, a sponsor of a 401(k) plans may elect whether or not to use the section 401(k) safe harbors to comply with the ADP and ACP tests. Indeed, if a plan sponsor elects not to use a safe harbor, the plan must still comply with the ADP and ACP tests. Under the proposed regulations, the ADP and ACP tests continue to apply for a plan year even if the sponsor satisfies the criteria to reduce or suspend QNECs during the plan year.

Furthermore, the substantial business hardship requirement is unduly burdensome. Most significantly, it is not clear whether a plan sponsor could demonstrate that a 401(k) plan will continue only if QNECs are reduced or suspended. Distress terminations are not available to section 401(k) plans. In addition, while it is not clear the extent to which each factor would need to be satisfied, the proposed regulations would at least require taking into account not only whether an employer experiences financial difficulty, but also whether an entire industry suffers economically. These criteria are not necessary to ensure compliance with the nondiscrimination rules. If imposed by the final regulations, these requirements would make the intended relief available to few, if any, section 401(k) plans.

Finally, the substantial business hardship requirement would impose a vague standard on which plan sponsors would be reluctant to rely. Not only are the terms “substantial unemployment” and “depressed” unclear, the proposed regulations would require a “comparable” hardship without explaining what “comparable” means. Furthermore, it is not clear the extent to which any factor must be present to constitute substantial business hardship. The criteria for a substantial business hardship set forth in Code section 412(c) are deliberately vague: they are factors to be taken into account by the Service to evaluate a funding waiver. A plan sponsor applies for a funding waiver pursuant to Rev. Proc. 2004-15, and the Service issues a ruling determining whether the criteria have been satisfied. By contrast, plan sponsors are not expected (and would likely not have time) to seek advance rulings to determine whether QNECs could be reduced or suspended mid-year. Plan sponsors therefore need clear standards.

In sum, flexibility to respond to the current economic crisis -- and relief from the QNEC requirements for safe harbor plans in particular -- are important. Issuing guidance providing such relief encourages employers to sponsor retirement plans. The substantial business hardship requirement, however, is inappropriate, unduly burdensome, and vague. The goals of the nondiscrimination rules can be achieved without this requirement. Instead, relief from the QNEC requirements should be available on a basis similar to the relief available with respect to the QMAC requirement.

ERIC appreciates the opportunity to submit this comment. We will continue to solicit member analysis of these and other proposed regulations to assist the Department of Treasury and Internal Revenue Service as it fashions relief for employers during these difficult economic times. If we can be of any further assistance, please let us know.

Sincerely,

Mark J. Ugoretz
President

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