

## Part I

### Section 411.--Minimum Vesting Standards

26 CFR 1.411(d)-4: Section 411(d)(6) protected benefits.

(Also, § 401; § 1.401(a)(31)-1.)

Rev. Rul. 2000-36

## ISSUE

Will an amendment to change the default method of payment to a direct rollover for involuntary distributions when a distributee fails affirmatively to elect to make a direct rollover or to elect a cash payment under the facts described below cause the plan to fail to satisfy § 401(a)(31) or § 411(d)(6) of the Internal Revenue Code?

## FACTS

Employer X maintains Plan A, a qualified defined contribution plan that does not include any after-tax contributions or other amounts that would not be included in gross income upon distribution. Plan A provides for an involuntary distribution to an employee upon separation from service if his or her vested account balance is \$5,000 or less. Plan A includes a direct rollover option for all distributions. Plan A provides that if a separating employee's vested account balance is \$5,000 or less, and the separating employee does not elect a direct rollover either to another qualified plan or to an individual retirement arrangement ("IRA"), the vested account balance is to be paid in a single sum cash payment to the employee.

Employer X amends Plan A to provide that the default form of payment of any involuntary cash-out from Plan A greater than \$1,000 but less than or equal to \$5,000 will be a direct rollover (an eligible

rollover distribution that is paid directly to an eligible retirement plan for the benefit of the distributee) to an IRA, but that separating employees will instead receive a cash payment if they so elect. Under the amendment, this default direct rollover applies only if the separating employee fails to request affirmatively (1) a cash payment to that employee or (2) a direct rollover to another qualified plan or an IRA designated by the separating employee. The amendment also provides that in the case of a default direct rollover, the plan administrator will select <sup>1</sup> an IRA trustee, custodian, or issuer (the “trustee”) that is unrelated to Employer X, establish the IRA with that trustee on behalf of any separating employee who fails affirmatively to elect a direct rollover or a cash payment, and make the initial investment choices for the account.

The administrative procedures of Plan A are changed with respect to any § 402(f) notice provided on or after the effective date of the amendment to a separating employee with a vested account balance greater than \$1,000 but not greater than \$5,000. After the change, the plan administrator will include with the § 402(f) notice an explanation, as required by § 1.401(a)(31)-1 of the Income Tax Regulations, of the default direct rollover (and other appropriate information such as the name, address, and telephone number of the IRA trustee and information regarding IRA maintenance and withdrawal fees and how the IRA funds will be invested). The default direct rollover will occur not less than 30 days and not more than 90 days after the § 402(f) notice with the explanation of the default direct rollover is provided to the separating employee.

---

<sup>1</sup>The Department of Labor (the “DOL”) has advised Treasury and the Service that, under Title I of the Employee Retirement Income Security Act (“ERISA”), in the context of a default direct rollover described in this ruling, where the distribution constitutes the entire benefit rights of the participant, the participant will cease to be a participant covered under the plan within the meaning of 29 CFR § 2510.3-3(d)(2)(ii)(B), and the distributed assets will cease to be plan assets within the meaning of 29 CFR § 2510.3-101. The DOL also noted that the selection of an IRA trustee, custodian or issuer and IRA investment for purposes of a default direct rollover would constitute a fiduciary act subject to the general fiduciary standards and prohibited transaction provisions of ERISA. In addition, plan provisions governing the default direct rollover of distributions, including the participant’s ability to affirmatively opt out of the arrangement, must be described in the plan’s summary plan description furnished to participants and beneficiaries.

## **LAW AND ANALYSIS**

Section 401(a)(31) provides, in part, that a trust shall not constitute a qualified trust unless the plan of which the trust is a part provides that if the distributee of any eligible rollover distribution (i) elects to have the distribution paid to an eligible retirement plan, and (ii) specifies the eligible retirement plan to which the distribution is to be paid, the distribution will be paid in a direct rollover to the eligible retirement plan specified.

Section 402(f) requires a plan administrator, within a reasonable period of time before making an eligible rollover distribution from an eligible retirement plan, to provide to the recipient a written explanation of the rollover provisions of § 401(a)(31) and § 402(c) (direct rollover and 60-day rollover), the 20-percent mandatory withholding requirement under § 3405, and other tax provisions in § 402 that apply to the eligible rollover distribution.

Section 411(d)(6)(A) provides, in part, that a plan participant's accrued benefit may not be decreased by a plan amendment other than by an amendment described in § 412(c)(8) of the Code or § 4281 of the Employee Retirement Income Security Act of 1974. Section 411(d)(6)(B) provides that an amendment eliminating or reducing an optional form of benefit is treated as an amendment reducing an employee's accrued benefit unless otherwise provided in Income Tax Regulations.

Section 1.401(a)(31)-1, Q&A-7 provides, in part, that a plan administrator may establish a default procedure so that if a distributee fails to make an affirmative election, he or she is treated as having made a direct rollover election. However, that regulation requires the plan administrator to first furnish the distributee with an explanation of the default procedure and an explanation of the direct rollover option within the time period provided in § 1.402(f)-1, Q&A-2 for the written explanation described in § 402(f).

Section 1.402(f)-1, Q&A-1 prescribes the general rule with respect to the contents of the written explanation (§ 402(f) notice) that must be provided to a distributee by a plan administrator before an eligible rollover distribution is made. Section 1.402(f)-1, Q&A-2 provides generally that the plan

administrator must provide a distributee of an eligible rollover distribution with a § 402(f) notice no less than 30 days and no more than 90 days before the date of the distribution. Although a participant may, under the circumstances described in § 1.402(f)-1, Q&A-2, affirmatively elect to receive a distribution before the expiration of the 30 days after the receipt of a § 402(f) notice, that rule would not apply to a default direct rollover.

Section 1.411(d)-4, Q&A-1(a) defines a “section 411(d)(6) protected benefit” as a benefit described in § 411(d)(6)(A), early retirement benefits and retirement-type subsidies described in § 411(d)(6)(B)(i), and optional forms of benefit described in § 411(d)(6)(B)(ii) and provides that those benefits, to the extent that they are accrued, are subject to the protections of § 411(d)(6).

The default status of an optional form of benefit is not a section 411(d)(6) protected benefit. Thus, an amendment to change Plan A's default method of payment for an involuntary distribution from a direct cash payment to a direct rollover does not violate § 411(d)(6). As required in § 1.401(a)(31)-1, Q&A-7, Plan A's procedures provide that each distributee subject to the default will receive an explanation of the default procedure and the direct rollover option within a time period before the default direct rollover that satisfies the timing requirements of § 1.402(f)-1, Q&A-2. Thus, the provision of a direct rollover as the default method of payment under the facts described above does not cause Plan A to fail to satisfy § 401(a)(31).

## **HOLDING**

An amendment to change the default method of payment to a direct rollover as the default when a distributee fails affirmatively to elect to make a direct rollover or to elect a cash payment under the facts described above does not cause Plan A to fail to satisfy § 401(a)(31) or § 411(d)(6).

## **DRAFTING INFORMATION**

The principal author of this revenue ruling is Michael Rubin of the Tax Exempt and Government Entities Division. For further information regarding this revenue ruling, call the Employee Plans' taxpayer

assistance telephone service at (202) 622-6074/6075 (not toll-free numbers) between 1:30 and 3:30 p.m. Eastern Time, Monday through Thursday. Mr. Rubin's telephone number is (202) 622-6214 (also not a toll-free call).