Snell & Wilmer L.L.P.

EMPLOYEE BENEFITS UPDATE

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Same-Sex Marriage and Its Impact on Employee Benefit Plans

On May 15, 2008, the California Supreme Court in In Re Marriage Cases held that domestic partnership is not a suitable substitute for marriage. In doing so, it struck down California's 1977 "one woman one man" marriage law and Proposition 22, which banned same-sex marriage and was passed by voters in 2000.

Conservative groups asked the California Supreme Court to stay the ruling until after the November election when voters will consider a ballot measure that would amend the California Constitution to again outlaw same-sex marriages. On June 4, 2008, the California Supreme Court refused to enter a stay. California started performing same-sex marriages on June 16, 2008. Same-sex marriages are also currently legal in Massachusetts, as well as Canada, Belgium, the Netherlands, South Africa and Spain.

With same-sex marriages now being performed in California, it's just a matter of time before employers in the western United States will be asked whether they provide same-sex spouse benefits.

The Defense of Marriage Act of 1996 ("DOMA") provides that for all federal laws "marriage" means only a legal union between one man and one woman as husband and wife, and the word "spouse" refers only to a person of the opposite-sex who is a husband or wife. DOMA further provides that no state, territory, possession, or Indian tribe is required to recognize same-sex marriage from another state, territory, possession or Indian tribe. Accordingly, for all federal purposes, including the Internal Revenue Code (the "Code") and the Employee Retirement Income Security Act ("ERISA"), which are the primary federal laws governing employee benefit plans, the term "spouse" refers only to persons of the opposite-sex who are husband and wife.

Due to ERISA preemption and DOMA, ERISA employee benefit plans are not required to provide same-sex spouse benefits, and those that do provide same-sex spouse benefits have wide latitude in designing their plans. However, for employers who wish to provide same-sex spouse benefits on the same basis

they provide opposite-sex spouse benefits, the DOMA definition of spouse is a significant impediment to doing so. For example, a same-sex spouse cannot be treated as a spouse for certain purposes under the Internal Revenue Code, including the required minimum distribution rules and the qualified joint and survivor annuity requirements. It is also currently unclear whether a same-sex spouse may be treated as a spouse under a qualified domestic relations order, meaning that it may be impossible to award pension benefits to a same-sex spouse in a divorce.

Regardless whether employers do or do not want to provide same-sex spouse benefits, they should review the definition of spouse in their employee benefit plans. Employers also should review their insurance policies to determine whether they have any hidden same-sex spouse benefits and/or domestic partner benefits and notify participants regarding such benefits. If employers want to provide same-sex spouse benefits, they should decide which benefits they want to provide and amend their plans and procedures accordingly. If employers do not want to provide same-sex spouse benefits, they should amend their plans to adopt a DOMA definition of spouse.

If you have any questions regarding same-sex spouse or domestic partner benefits, or would like to prepare appropriate plan amendments, please call Nancy Campbell at 602.382.6374.

Larue Decision Confirms a Participant's Right to Sue Plan Fiduciaries – Now is a Good Time to Review Fiduciary Practices

The United State Supreme Court's recent decision in LaRue v. DeWolff, Boberg & Associates, Inc. makes it clear that defined contribution plan participants may sue for alleged breaches of fiduciary duty. Prior to LaRue, some lower courts had concluded that a participant could only bring a claim against plan fiduciaries if the alleged injury affected the plan as a whole. In these courts, an individual participant could not bring a claim against plan fiduciaries alleging that only his or her account was affected.

In LaRue, a 401(k) participant alleged that the plan administrator failed to follow the participant's investment directions, causing the participant's account to be depleted by approximately $150,000. The participant sued for breach of fiduciary duty and the Fourth Circuit held that ERISA Section 502(a)(2) provides remedies only for entire plans, not for individuals. The Supreme Court, on review, held that Section 502(a)(2) does authorize recovery for fiduciary breaches that impair the value of plan assets in a participant's individual account.

In response to LaRue, plan sponsors and fiduciaries should review their administrative practices and procedures, paying particular attention to Section 404(c) compliance (see article immediately following). Plan fiduciaries also should review their fiduciary liability insurance to ensure that the coverage levels are adequate.

If you have any questions regarding the implications of LaRue, please call Nancy Campbell at 602.382.6374 or Tom Hoecker at 602.382.6361.

Does Your Participant Directed Investment Program Still Comply with ERISA Section 404(c)?

Employers that adopt Section 401(k) plans or profit sharing plans usually give plan participants some say in the investment of their accounts by implementing a "Participant Directed Investment Program" pursuant to

which participants are allowed to invest their accounts in an array of investment funds selected by plan fiduciaries.

ERISA Section 404(c) serves as the legal underpinning for Participant Directed Investment Programs. Section 404(c) provides that if a participant in a plan controls the investment of his or her account, the plan fiduciaries are not responsible if the investment turns sour.

Section 404(c) compliance can be difficult, so plan fiduciaries should reconfirm compliance at least annually. To help in that regard, we recently updated our *Section 404(c) Compliance Checklist* which can be found at www.swlaw.com/publications/detail.aspx?pub=243. The Checklist summarizes the requirements that a plan should satisfy in order for plan fiduciaries to have the benefit of Section 404(c) protection. The Checklist reflects the Pension Protection Act relief for mapped investments and qualified default investment alternatives, which are significant improvements.

If you have any questions about Section 404(c) compliance, please call Nancy Campbell at 602.382.6374 or Tom Hoecker at 602.382.6361.

Finding and Fixing Qualified Plan Mistakes Just Got Easier

The IRS continues to make finding and fixing qualified plan mistakes easier and more affordable. Most recently, the IRS revamped and improved the Employee Plans Compliance Resolution System. The changes take effect September 2, 2008. The most notable improvements include:

- Providing standardized application forms;
- Expanding the streamlined procedures for the Voluntary Correction Program to include nine categories which will make correcting those categories quicker, easier and less expensive;
- Expanding the circumstances under which the IRS may exercise its discretion to waive income and excise taxes;
- Increasing the limit for the distribution of small benefits from $50 to $75, which will allow plans to avoid making corrective distributions of $75 or less if the administrative expense of making the distribution exceeds the amount of the distribution;
- Allowing earnings to be computed using the Department of Labor's Voluntary Fiduciary Correction Program online earnings calculator if it is not possible to make a reasonable estimate of actual plan earnings; and
- Reducing the filing fee for certain loan failures.

The IRS also recently issued a 401(k) Fix-It Guide with tips on how to find, fix, and avoid the following common mistakes in 401(k) plans:

- failure to update a plan document to reflect recent changes in the law;
- failure to follow the terms of a plan document;
- incorrect application of a plan's definition of compensation;
- incorrect allocation of matching contributions;
- failure of nondiscrimination testing;
- exclusion of eligible employees;
- failure to limit elective deferrals to the amounts required under the Code;
- failure to timely deposit employee contributions;
- improper hardship distributions;
- failure to make any required top-heavy minimum contributions; and

- failure to file Form 5500 and distribute a summary annual report.

The Guide is available at www.irs.gov/pub/irs-tege/401k_mistakes.pdf.

If you have questions concerning a possible qualified plan defect, please call any member of our Employee Benefits Group. Wondering whether you should correct a defect? See the IRS *Top Ten Reasons to Identify and Correct Mistakes in Your Retirement Plan Operations* at www.irs.gov/retirement/article/0,,id=112851,00.html.

Department of Labor Proposes 7-Business Day Safe Harbor for Employers to Forward Employee Contributions to Small Plans

The Department of Labor ("DOL") has issued a proposed rule for small employee benefit plans (i.e., plans with 100 or fewer participants as of the first day of the plan year) relating to when employee contributions must be forwarded to the plan.

Under existing guidance, participant contributions that are withheld from wages or are received from employees (such as 401(k) contributions or loan payments) must be forwarded to the plan as soon as such amounts can reasonably be segregated from the employer's general assets, but in no event later than the 15th business day of the month following the month in which such amounts are withheld or received. Welfare plan contributions (such as employee health premiums) must be forwarded to the welfare plan as soon as such amounts can reasonably be segregated from the employer's general assets, but in no event later than 90 days from the date on which the employer receives or withholds the amounts.

During recent DOL audits, the DOL has sometimes asserted that amounts could reasonably be segregated in as little as 2-3 days. To provide employers with more certainty, the DOL has issued a proposed rule which gives small employee benefit plans a 7-business day safe harbor. The proposed rule provides that participant contributions to small pension plans and welfare plans will be treated as having been made as soon as such amounts can reasonably be segregated from the employer's general assets if contributions are forwarded to the plan no later than the 7th business day following the date on which the employer receives the amounts from the employee or the 7th business day following the date on which the amount would otherwise be payable in cash to the employee.

Although the final rule has yet to be published, effective February 29, 2008, the date the proposed rule was published, the DOL has indicated it will not assert a plan asset violation so long as participant contributions or loan payments to a plan with fewer than 100 participants are transferred to the plan in accordance with the 7-business day safe harbor.

If you have any questions regarding the general or safe harbor deadlines, please call Anne Meyer at 602.382.6595.

IRS Opens Determination Letter Cycle for Pre-Approved Defined Contributions Plans – Cycle Ends April 30, 2010

The IRS has issued opinion and advisory letters for master and prototype and volume submitter defined contribution plans that were filed in connection with the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA").

Employers using these pre-approved defined contribution plans now have until April 30, 2010 to adopt the EGTRRA-approved plan document. Employers who would like a determination letter covering their EGTRRA restatement should also submit for a determination letter by April 30, 2010.

If you have any questions, please call Anne Meyer at 602.382.6595.

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