

BLACK OUT PERIODS

In the wake of the Enron situation, Congress passed a law containing blackout period requirements that apply to all defined contribution retirement plans. Blackout periods (times when participants lose control over their accounts) can occur for a number of reasons, but the most common are if the plan changes its third party administrator, investment fund provider or other service providers. The DOL issued a model notice and Interim Final Rules that were published in the 'Federal Register' on October 21, 2002.

Most defined contribution plans allow participants to direct the investment of their accounts in the plan. Sometimes, a plan sponsor must temporarily suspend the ability of participants to change investment selections under the plan, or to take loans or distributions. These periods, known as "blackout periods," can occur for a number of reasons, but the most common are when changes occur in the plan's third party administrator, investment fund provider or other service providers.

In the wake of Enron, on July 30, 2002, Congress passed an accounting reform bill known as the Sarbanes-Oxley Act of 2002 (Act). You've probably heard about the provision in the Act that restricts executives and directors from selling stock or exercising stock options when their company's retirement plan (which contains company stock) has a "blackout period" which prevents employees from transacting in stock within the plan. However, the Act also contains blackout period requirements that apply to all defined contribution retirement plans.

The Act directed the Department of Labor (DOL) to issue a model notice and other guidance. The DOL issued a model notice and interim final rules that were published in the Federal Register on October 21, 2002.

What Must Be In The Notice

Under the Act, defined contribution plan administrators are required to provide affected participants and beneficiaries with at least 30 (but not more than 60 days) advance notice of a blackout period if the blackout period is expected to last more than 3 days. This period is measured from the last day on which the participant or beneficiary may exercise the right or rights that will be affected (blacked out). The notice must contain the following information:

- The reasons for the blackout period;
- An explanation of the investments and other rights affected;
- The expected beginning date and the length of the blackout period;
- A statement informing the participants and beneficiaries that they should evaluate their current investment selections in light of their inability to direct or diversify their investment choices during the blackout period;
- The name, address and telephone number of the plan administrator or other person responsible for answering questions about the blackout period; and
- Such other matters the DOL may require by regulation.

When Notice Is Not Required

The 30-day notice requirement contains certain exceptions. These include when: (1) waiting to initiate the blackout period would result in a fiduciary

breach, and the fiduciary reasonably determines this in writing; (2) the inability to provide 30-days advance notice is due to unforeseeable events beyond the control of the plan administrator, and the fiduciary reasonably determines so in writing; and (3) the blackout is due to certain provisions of federal securities laws. In these situations, the fiduciary must prepare a written memorandum describing the rationale for the failure to provide the 30-day notice. The preamble to the DOL interim final rules gives examples for the exceptions above. For the first exception, the example describes a company that will declare bankruptcy, and the plan administrator determines that it would be prudent to immediately suspend the ability of participants to invest in company stock. For the second exception, the example describes a computer failure that makes it impossible to process loans and distributions. Another exception to the 30-day notice requirement arises in certain merger and acquisition situations affecting the plan or the plan sponsor. In such cases, the notice must be provided as soon as reasonably possible.

The notice can be delivered in writing or electronically (if participants can be reasonably expected to receive the notice, if it provided in electronic form). The same standard used for electronic delivery of summary plan descriptions applies to blackout notices.

Changes In Length Of Blackout Period

If the beginning date or the length of the blackout period is changed after the initial notice is given, the plan administrator must give a subsequent notice of this change as soon as possible to all affected participants and beneficiaries. The subsequent notice must state whether any matters discussed above have changed.

Penalties For Failure To Comply

The DOL may assess a civil penalty of up to \$100 per day for each failure to comply with the notice requirements. Each participant to whom the plan administrator fails to timely give notice is treated as a separate violation. For example, if a plan has 10 affected participants, and the notice is provided 10 days late, the civil penalty could be as much as \$10,000, calculated as follows: [10 (participants) x 10 (days) x \$100] = \$10,000. However, the DOL may charge a lesser penalty.

The rules require that the DOL give a plan administrator 30 days, from the date the DOL gives notice of an intent to levy, to file a “statement of reasonable cause” demonstrating (i) that the administrator did comply or (ii) the mitigating circumstances regarding the degree or willfulness of the non-compliance. Based on this statement, the DOL may either determine that no penalty assessment is warranted or waive all or a part of the penalty.

Effective Date Of The New Rules

Plan administrators must comply with these requirements no later than January 26, 2003. According to the DOL's interim final rules, the new rules apply only to blackout periods that begin on or after January 26, 2003. However, the Act requires plan administrators to comply in good faith with these requirements even before the effective date of the Act. This means that fiduciaries should, at a minimum, attempt to provide at least 30 days notice of a blackout period right now even though the Act is not yet effective.

Any plan amendments required to comply with the provisions of the Act must be adopted by the end of the first plan beginning after the effective date of the Act. This means December 31, 2004 for a calendar year plan.

What If The Blackout Period Starts Before January 26, 2003 And Ends After That Date?

Inevitably, some plan transitions that begins before the effective date of the Act will extend beyond January 26, 2003. The DOL interim final rules state that for the period from January 26, 2003 to February 25, 2003, plan administrators should provide notice as soon as reasonably possible. Although not required to do so, it would be prudent for a plan administrator to provide the type of notice required by the Act at least 30 days in advance for any blackout period, even if that blackout period begins before January 26, 2003. If a blackout period begins before January 26, 2003, was originally anticipated to end after January 26, 2003, and needs to be extended beyond the ending date that appeared on the initial notice, it would be prudent, although not mandatory, for the plan administrator to give a subsequent notice indicating the new anticipated length of the blackout period as soon as reasonably possible.