

New Law Pertaining to Blackout Periods for Defined Contribution Plans

Defined contribution plans generally allow participants to direct the investment of their accounts. From time-to-time, it is necessary to temporarily suspend the participants' right to make trades or to take loans from the plan. These are called "blackout periods" and can happen, for example, if the plan changes its service provider or its investment funds.

On July 30, a new accounting reform bill, the Sarbanes-Oxley Act of 2002, was signed into law. This new law contains provisions relating to defined contribution plans that require plan sponsors to notify participants in advance of certain blackout periods. It also prohibits insider trading by corporate officers during certain blackout periods to the extent that the plan holds employer securities.

Notice Requirement for Blackout Periods

Under the new law, defined contribution plan administrators will be required to provide participants and beneficiaries affected by a blackout period with **at least 30 days** advance notice. (One-participant plans are exempt from this requirement.) The notice will have to include:

- ✓ the reasons for the blackout period;
- ✓ a description of the investment or other rights affected;
- ✓ the expected length of the blackout period;
- ✓ a statement that the participant or beneficiary should evaluate their investment choices in light of the impending blackout period; and
- ✓ such other matters prescribed by the Department of Labor.

The notice can be delivered either in writing or electronically.

If there is a change in the expected length of the blackout period, the plan administrator will have to notify participants and beneficiaries of the change as soon as reasonably practicable. This notice must also specify whether any of the other matters in the above list have also changed.

The term "blackout period" means any suspension, restriction or limitation on the ability of participants to direct the investment of assets in their accounts, to obtain loans or to obtain distributions that is expected to last for a period of **more than three** consecutive business days.

The law specifically provides that any suspension, limitation or restriction necessitated in connection with a Qualified Domestic Relations Order (QDRO) or by reason of the application of securities laws is not considered a blackout period. Further, some changes to plans that otherwise provide for a regularly scheduled suspension, limitation or restriction (e.g., quarterly investment direction) will also not be considered blackout periods. In the case of an emergency the 30-day advance notice requirement is waived.

If a plan fiduciary determines that complying with the notice requirement would violate his or her fiduciary responsibility or if the inability to provide the 30-days advance notice is due to events that were unforeseeable or circumstances beyond the reasonable control of the plan administrator, the notice can be provided as soon as reasonably possible, even if this is after the blackout period. In order to take advantage of this exception, the plan fiduciary or plan administrator would have to keep a written record of the facts and rationale justifying the exception. A further exception to the 30-day advance notice requirement would be provided in the case of certain mergers and acquisitions involving the plan or plan sponsor, in which case the notice needs to be provided as soon as reasonably practicable.

The Department of Labor can assess penalties of up to \$100 per day for each failure to comply with these requirements.

The new requirements become effective in January 2003. The Department of Labor is directed to issue a model notice and other guidance, including possible additional exceptions to the notice requirement. Good faith compliance applies in the absence of this guidance. Any plan amendments required by this provision must be made by the end of the first plan year beginning after the effective date of the provision. For calendar year plans, amendments will have to be made by December 31, 2004.

Restrictions on Insider Trading During a Blackout Period

The new law also prevents corporate officers and directors from trading in employer securities acquired in connection with their employment during any plan blackout period to the extent the plan holds employer securities. This prohibition only applies with respect to publicly traded employer securities. An individual violating this prohibition will have to forfeit to the issuer of the securities any profits that result from the trading.

For this purpose, a blackout period is a period of more than three consecutive business days during which the ability of 50 percent or more of the plan participants to direct the investment of employer securities is suspended, limited or restricted. Any regularly scheduled suspension, limitation or restriction (for example, quarterly investment direction) previously disclosed to participants will not be considered a blackout period. Also, a suspension, limitation or restriction arising in connection with a merger or acquisition involving the plan or plan sponsor is not considered a blackout.

The issuer of the employer securities (presumably the plan sponsor) is responsible for timely notifying affected corporate officers and directors and the SEC of the plan blackout period.

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