

METRO NEWS – Report #62

March 31, 2006

To our clients and friends:

This is another in a series of newsletters designed to keep you clearly informed of current events in the area of employee benefit plans (plus other actuarial stuff).

Pension Funding Reform – Update:

The House and Senate have passed different versions of legislation that would tighten funding rules for certain types of pension plans (“defined benefit plans”). We’ll be advising our affected clients later this year. One of the main goals is to protect the PBGC (“the government”) from further huge losses as bankrupt companies continue to dump their unfunded liabilities.

However, there are also provisions in the legislation that would impact 401(k) plans:

- Currently, it is very difficult for the Employer to arrange for “investment advice” for its employees, i.e., to provide for education on their 401(k) investment options. This is because of concerns about legal liability if things go poorly. Both the House and the Senate versions of the bill would allow for the Employers to provide for this type of advice.
- “Automatic enrollment” for 401(k) plans would be encouraged. Congress is concerned about Americans’ (low) rate of savings, and so both versions would provide incentives to plans that “push” employees into 401(k) savings arrangements. This pushing (called automatic enrollment) would provide that if a new employee does not decline to have a payroll deduction savings, then they are (by default) “in” the plan, at some pre-set level of payroll deduction. One version of the legislation would have the level of savings as high as 10% of pay – this seems very high. In exchange for adopting this provision, Employers would get a break on certain aspects of 401(k) discrimination testing. Note that this “default option” has been available for a few years – the new idea here is tying incentives to it.

MetroNews #62
March 31, 2006
Page Two

- We'll let you know how this turns out in the next issue. Let us know if you'd like to discuss these ideas in the meantime.

This Reminds Me.....

How silly the whole idea of 401(k) discrimination testing is, anyway. Even if the Employer makes the plan available to all employees, there are still restrictions on how much the highly-paid can save, based upon how much the other employees actually participate. It ought to be enough to lead the horses to water, i.e., to make the 401(k) savings arrangement available to all.

Information on Information:

If you are worried about the high cost of dialing 411 (or whatever) to find a phone number, you may wish to try out 1-800-FREE411. It worked for me. (Notes: No promises/don't blame me if problems/thanks, Brian = my son for pointing this out for me/us!)

This is a BIG Problem:

As most of you know, all plan documents have to be "re-done" every few years to reflect new laws since the last document. Historically, these "restatements" have been required every 7 or 8 years. Until now, the IRS has allowed the plan to operate in compliance with the new laws until the next restatement is due. Then, these laws are included with a retroactive effective date (to the date of the legislation.) This kind of made sense.

No more!

The IRS is not as "kind and gentle" as it used to be. They now want the plan document to be amended every time that new 401(k) legislation is passed, which means almost every year. They feel uncomfortable allowing the plan to operate differently than its written terms, even if the legislation involves only technical changes which involve no Employer discretion.

This is a terrible idea. It will waste everyone's time and money. I have already told this to the IRS, but I am not sitting next to my mailbox awaiting a response or a change.

Specifically, this resulted in the silly \$1,000/\$5,000 amendments last year, and will further require amendments by (a) 3/15/07 to reflect final 401(k) regs. (effective 1/1/06) and (b) perhaps 3/15/08 to reflect final regs. on maximum benefits. We need a PR campaign to fix this. Let me know if you are interested (or if you disagree).

Reader Feedback – “Chocolate Update”:

Thanks to Paul Bock (John Hancock, formerly Manulife) for his advice on why vanilla ice cream is typically used to make chocolate milkshakes. “Based on my own recipe for hot cocoa, too much chocolate would make it bitter, and you actually need vanilla to make it taste like chocolate”. Thanks, Paul, you’ve made the honorary “All-Chocolate” team!

Coffee, Tea or Staples?:

Never having thought about it, I always assumed that a multi-page business letter would have a neatly-placed staple in the upper left-hand corner. I am now realizing that this may be a breach of business etiquette. Apparently, the “rules” indicate that to staple or paper clip is to mar the pristine document.

Isn’t this a little silly? People “in the know” advise that this rule is designed so that the (a) final product looks crisp and clean, and (b) envelope doesn’t have any bulges. Do you find a staple (or a paper clip) offensive? Isn’t there a risk of having the pages separate and get misplaced on your desk?

Do we care about this? Let me know. Maybe we can include this with our IRS comments (above) and wrap everything up with another new law.

State Taxation of 401(k) Payouts in PA:

Pennsylvania seems like a goofy State, and so it does not allow employees to defer taxation on their 401(k) payroll savings. While the employees can defer Federal tax, they must pay State tax when the funds are deducted from their paycheck.

If an employee withdraws their funds after retirement, if he/she is over 59 ½ years old, then the entire payout comes out tax-free. If someone withdraws earlier than this age (which most do), then tax is (apparently) due on (a) less (b), where:

(a) = The entire payout, and

(b) = the amounts that the employee has already paid taxes on.

This difference represents the accumulation of all investment income and all historical Employer contributions to the Plan, if any. One major problem is that very few people (do you know any?) actually track their own historical contributions (the (b) item, above). Without this, double-taxation is likely.

MetroNews #62
March 31, 2006
Page Four

Whether people actually report the payouts as “taxable income” to the State is another question. Also, people who retire and move to another state are on their own, and may not be able to receive credit on the previously-taxed employee 401(k) contributions.

You should discuss this with your Accountant, if you’d like to explore this further.

Welcome to Metro!:

We’ve added three new Assistant Analysts to our staff – Bryon DiGiorgio, Leann Malloy and Todd Szramowski. They are graduates of University of Pittsburgh-Johnstown (Bryon) and Robert Morris University (Leann and Todd). We anticipate great things from all three of them and welcome them to our team!

Best Wishes and Good Luck, David M. Lipkin, F.S.A., Editor

Metro Benefits, Inc. is a regional consulting and administration firm, based in Pittsburgh, PA. We provide a wide range of services for employee benefit plans. While we make every effort to verify the accuracy of the information that we present here, you should consult with your Plan attorney or other advisor before acting upon it.