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WASHINGTON UPDATE

The (Almost) Post-Election Report

by Brian H. Graff, Esq.

American voters have spoken – but what did they say?

As the sorting out continues…a few things are clear: Once the process of vote counting is completed, the new President will lead a deeply – and almost exactly evenly – divided Congress. Republicans will remain in control of the House and Senate, but already razor-thin margins have been narrowed further, and may tighten more due to the five remaining undecided races (one in the Senate, four in the House). Thus, over the next two years, control of either House could flip upon the death or retirement of a single member or a small group of members.

Based on these margins, neither party in Congress will have the political strength to force its agenda on the other party. As a result, any new laws will come only from the center of American politics. Whether or not the new President actually wants to enact new laws is an entirely separate matter, but he must proceed knowing he has no "mandate" on any of the hotly debated election issues. Thus, the new occupant of the White House must

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New Comparability Plans Survive After New Regulations

by Sal Tripodi, APM, J.D., LL.M., and John P. Griffin, APM, J.D., LL.M.

As anticipated, the Department of Treasury has issued proposed regulations (IRS Reg. 2000-114697) regarding new comparability plans. Since February, when the Treasury indicated it was considering new restrictions on new comparability plans (Notice 2000-14), practitioners have anxiously awaited this guidance. Based on the February Notice, many practitioners were concerned about the continuing viability of the new comparability plan design. While the proposed regulations will narrow the maximum disparity of allocations between highly and nonhighly compensated employees, the impact of the regulations is far less restrictive than feared. With either minimal or no modification, the current design of most new comparability plans will survive. While final regulations may modify the proposed regulations, further restrictions are unlikely.

The proposed effective date for the regulations is plan years beginning on or after January 1, 2002. This would be a uniform effective date that would apply to all comparability plans, regardless of when the plan was initially adopted. Before reviewing the discussion of the regulations below, keep in mind that if this effective date is retained in the final

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regulations (which it likely will be), nothing changes in the way new comparability plans show they are nondiscriminatory for the 2000 and 2001 plan years.

What do the regulations do?

The proposed regulations establish a "gateway" rule for defined contribution (DC) plans to prove allocations are nondiscriminatory on the basis of benefits. (New comparability is simply a phrase used to refer to DC plans that do this. Sometimes these plans are referred to as "cross-tested" plans because of the manner in which they are tested.) In other words, before the plan can be tested on the basis of benefits (i.e., converting allocations to equivalent benefit rates (EBRs) and applying the rate group test using those EBRs), the "gateway" test must be satisfied. The gateway test establishes a minimum contribution rate that must apply to the nonhighly compensated employees (NHCs). However, certain DC plans are exempt from the gateway test by establishing that the allocation rates are "broadly available" (as defined in the regulations).

The "gateway" test

Under the "gateway" test, the lowest permissible allocation rate for any NHC who benefits under the plan is one-third of the highest allocation rate for any highly compensated employee (HCE). However, if each NHC receives an allocation that is no less than 5% of compensation [as defined under IRC §415(c)(3)], the gateway is deemed satisfied.

Example. A new comparability plan provides for two allocation groups: Group A consists of owners of the company, who are all HCEs, and Group B consists of other eligible employees. The employer makes a discretionary contribution for each group. The amount contributed for the benefit of each group is allocated to the eligible employees included in that group, using a pro rata allocation formula based on IRC §415(c)(3) compensation. For the last several years, the contribution rate for Group A has been in the range of 14% to 20%, and the contribution rate for Group B has been in the range of 6% to 8%. The plan passes the rate group test on the basis of equivalent benefit rates (EBRs). The proposed regulations would not affect this plan, so long as the contribution rate for Group B does not drop below 5%. Of course the plan would still have to show that the rate group test can be passed on the basis of EBRs on a plan year by plan year basis.

Example. Assume in the prior example that the plan has been passing the rate group test (using EBRs) by only contributing 3% for Group B. Under the proposed regulations, if the employer did not want to increase the contribution rate for Group B above

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ASPA members are retirement plan professionals in a highly diversified, technical, and regulated industry. ASPA is made up of individuals who have chosen to be among the most dedicated practicing in the profession, and who view retirement plan work as a career.

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Focus on GAC

IRS, Treasury, DOL, and PBGC Meetings

In October, members of ASPA's Government Affairs Committee (GAC) met in Washington, D.C., to assess the activities of the past and to set goals for the future. In conjunction with these meetings, teams of GAC members visited the offices of the Internal Revenue Service, Treasury, Department of Labor, and Pension Benefit Guaranty Corporation for face-to-face discussions with top agency officials. These meetings create an effective forum for retirement plan professionals, along with people inside the government, to review how the regulations function in practice. Following are summaries of the meetings prepared by GAC members in attendance.

Internal Revenue Service

by C. Frederick Reish, APM, Esq., and Bruce L. Ashton, APM, Esq.

At the semi-annual meeting of the ASPA Government Affairs Committee (GAC) held in Washington, D.C. in October, GAC representatives met with IRS and Treasury officials to discuss issues of importance to ASPA members. As a part of the restructuring of the Employee Plans/Exempt Organizations Division into the Tax Exempt and Governmental Entities Division (TE/GE), the Examination and Review section (the auditing arm of the Employee Plans function of TE/GE) is now headquartered in Baltimore. Officials from the Baltimore office, as well as from the determination letter section in Cincinnati, participated by conference call.

The principal issues we discussed were the following:

401(k) Plan Audit Project

As described in *ASPA ASAP* No. 2000-39 (released November 9, 2000), the IRS has issued a report on its audit project of 401(k) plans. (The IRS has posted the report on the internet at www.irs.gov/bus_info/ep/401k.html.) In the project, undertaken from 1995 through 1997, the IRS audited 472 plans ranging from very small plans to those it labeled "super large" plans with more than 60,000 participants. The project was intended to discover the levels of compliance by 401(k) plans with the objective of developing better ways of targeting plans for audit, additional areas where guidance is necessary, and areas where education of plan sponsors and their advisors would be appropriate. The IRS reported that it found violations in 44% of the plans audited (including qualification failures, prohibited transactions, deemed distributions, etc.) and that the level of non-compliance was relatively consistent regardless of the size of plan. Because the audit project apparently did not provide the level of data the IRS wanted, it will again be targeting 401(k) plans for audit in the upcoming year to gain further information.

On behalf of ASPA, the Committee expressed concern at the high level of non-compliance, which probably reflected that some rules were too complex and that practices in some portions of the benefits community were probably too lax. We urged the IRS, when they do future audit programs, to gather and tabulate data on the source of the plan administration (in house, third party administrator, bundled provider, etc.) so that they and we could best identify where the problems are, so that ASPA and other benefits organizations could design education programs to help improve the level of compliance.

Audit Priorities and Issues

For the year beginning October 1, 2000 and ending September 30, 2001, the Employee Plans national audit priorities will be the following: (1) 401(k) plans; (2) 403(b) annuity cases where the sponsor also has a 457 plan; (3) multi-employer plans, with a cross-section of plan sizes; and

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Washington Update

pick and choose his priorities carefully in the early days of his four-year term.

The following analysis summarizes the current dynamics shaping the coming Congress, the outlook on issues facing the 107th Congress, and how the election will affect the upcoming lame duck session and the outstanding tax bill, H.R. 2416, which includes the long-awaited pension reform legislation.

The Shape of the 107th Congress

The Senate: At present, the Senate will consist of 50 Republicans and 49 Democrats – the new Senator from Washington has not yet been determined. At this writing, challenger Democrat Maria Cantwell holds an approximate 1000-vote lead over her Republican incumbent opponent, Slate Gorton. If Ms. Cantwell has ousted Senator Gorton, the Senate stands evenly divided at 50 Republicans and 50 Democrats. If Gorton wins the recount, the breakdown will be 51 to 49 in favor of the Republicans.

But that's not all – the outcome of the Presidential election could affect the Senate directly. If Vice President Al Gore wins the presidency, his vice president would be sitting Senator Joe Lieberman, a Democrat from Connecticut. In order to fill the seat of Vice President, Senator Lieberman would have to resign his Senate seat, and Connecticut's Republican governor would appoint the seat's replacement. (Most insiders are betting on appointment of Rep. Nancy Johnson (R-CT), a senior member of the Ways & Means Committee whose district is in peril when redistricting begins next year.) Under this scenario, the Senate would split 51 Republicans to 49 Democrats if Senator Gorton loses, and 52 to 48 if Gorton retains his seat.

Said another way, a President Bush would deal with a 51 to 49 Senate, if Senator Gorton wins, or a 50 to 50 Senate if Ms. Cantwell wins. Vice President Dick Cheney would be the tie-breaking vote in an evenly divided Senate. On the other hand, a President Gore would deal with a Senate with 52 Republicans and 48 Democrats, if Senator Gorton wins, or a 51 to 49 split if Ms. Cantwell wins. Under any scenario, the Republicans retain control, but by the slimmest of margins.

However, Republican control could be fleeting given the state of health of both Strom Thurmond (R-SC) and Jessie Helms (R-NC). Senator Thurmond is 98 years old and Senator Helms has been seriously ill. If both men were to leave the Senate, Democrats could find themselves in control of the Senate.

A significant fact almost lost in the buzz over the too-close-to-call Presidential election is that at least five, and possibly six, incumbent Senators were defeated in their reelection bids. Two of these incumbent Senators were members of the Senate Finance Committee, the chief tax-writing committee with jurisdiction over pensions, including Republican Bill Roth from Delaware, the committee chairman. Consequently, beginning next year, the Finance Committee will have a new chairman and a new ranking minority leader. Fortunately, both of these Senators have been strong supporters of pension reform. The new chairman will be Senator Charles Grassley (R-IA). Senator Grassley was the original cosponsor, along with Senator Graham (D-FL), of the companion pension reform legislation to the Portman-Cardin legislation introduced in the House. The new ranking minority leader of the committee, Senator Max Baucus (D-MT), has been a very strong supporter of ASPA and small business pensions. As reported in previous Washington Updates, his support on the new comparability issue has been critical.

Further, approximately a full third of the Senate Finance Committee seats will be filled by new committee members. In addition to the two seats that must be filled due to the election losses of Senator Roth and Chuck Robb of Virginia (D), five other seats will be vacant. One was held by the late Senator Paul Coverdell (R-GA), whose death a few months ago resulted in an "interim-only" appointment to the committee and who must now be permanently replaced. Plus, four other committee members will retire at the end of the 106th Congress: Senator Connie Mack (R-FL), and Democrats Daniel Patrick Moynihan (NY), Bob Kerrey (IA), and Richard Bryant (NV).

The size of the Finance Committee is also likely to change. Despite Democratic Leader Tom Daschle's (D-SD) claim that Democrats are entitled to equal representation and co-leadership, the likelihood is that the Republicans will retain at least a single-seat majority. But whether it will be 11 Republicans and 10 Democrats, or 10 Republicans and 9 Democrats – as is the current speculation – is as yet unclear.

No matter how you slice it, the Senate will be a very different place in the 107th Congress. Democrats will demand far more input into agenda-setting as well as legislative substance. Legislation will have to attract broad bipartisan support in order to be enacted, and at the same time, leadership – on both sides – will have to accommodate individual

Senators who disagree with leadership on either strategy or substance.

The House: Voters have elected 220 Republican Representatives, and 211 Democrats in the House of Representatives. Four seats are undergoing recounts or are awaiting absentee ballot counts before the results can be certified.

Assuming a 50-50 split of the open races (a result anticipated by both the Democratic Congressional Campaign Committee and the National Republican Campaign Committee), the final count will be 222 to 213 (with two independents, one voting with each party). Thus, Republicans can lose only four votes on any issue. This means that virtually every bill must have bipartisan support to thread its way through the House.

The close split will raise questions and heated debate about "ratios" – the number of Democrats versus Republicans – on House committees. Most Democrats do not expect Republicans to budge on their heavily weighted committees, since that was the result in 1998, despite a very close split then. However, as the process of determining the winner of the November 7th Presidential election unfolds, more and more commentators – and lawmakers – are predicting the need for bipartisanship and legislation from the political center in order for the 107th Congress to accomplish anything. One scenario would be to narrow the ratios on the major committees, including Ways & Means. But with organizational meetings postponed until December, it's too soon to say with any certainty whether the House leadership will adopt a more conciliatory approach.

Also in the mix is the fact that under the current rules, Republicans have term-limited their committee chairs: no chair can serve more than three terms (six years). Thus, many of the committees' leaders will change.

At Ways & Means, six-year chairman Bill Archer (R-TX) will retire at the end of 2000, leaving the top spot at the tax-writing committee the subject of a contest between Rep. Phil Crane (R-IL), who's next in line to head the committee under the usual seniority system, and Rep. Bill Thomas (R-CA), who has been positioning himself for months to challenge Rep. Crane for the chairmanship.

Both Crane and Thomas are true-blue conservatives who can be expected to make major tax cuts a priority – and put estate tax repeal and marriage penalty relief among the top tier tax cut issues. But beyond that, look for more emphasis on trade from Rep. Crane or on health from Rep. Thomas.

The Issues

On the following page is a chart showing outstanding issues in the 106th Congress and/or touted by either Governor Bush or Vice President Gore during the Presidential campaign. The chart is only a forecast of the major debate topics. Keep in mind, some could be addressed in the coming lame duck session. However, most are increasingly skeptical of progress in 2000. As for 2001, it's possible – perhaps probable – that these and other issues will emerge as the year unfolds.

The Lame Duck Session

Congress is in recess until December 5th. When they come back, they are expected to finalize government funding for the next fiscal year, assuming they are not arguing over who is President. Many of the above issues could be settled this year, by the 106th Congress, if President Clinton and the current Congress come to terms on H.R. 2614, the Taxpayer Relief Act of 2000 – the year-end $240 billion tax cut bill. Among the issues that could be settled are new pension and IRA incentives, health insurance deductions, and long-term care insurance deductions. Given the lack of clarity over the election, the potential for enactment of H.R. 2614 is remote at best, despite leadership in both Houses saying publicly that they still intend to try to move the bill. Further, passage of the Foreign Sales Corporation provisions, which were needed to avoid trade sanctions by the European Union, right before Congress recessed, significantly reduces the pressure to enact tax legislation this year.

Although it does not appear that pension reform will be enacted this year, rest assured ASPA's Government Affairs Committee will be working hard for its consideration early next year. We believe the prospects for ultimate enactment remain excellent. Given the current unsettled political climate, Congress will likely be looking for bipartisan legislation to demonstrate its ability to govern. Certainly, the pension reform legislation, which passed the House by a margin of 401-25, satisfies that requirement. ▲

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Ideas? Comments? Questions? Want to write an article?

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Outstanding Issues in the 106th Congress

Issue	Origin	Outlook
Pensions	H.R. 1102 from the 106th Congress; pension items in the Gore campaign platform	Bipartisan support exists for increasing contribution limits on qualified plans and for simplifying administrative rules, including top heavy rules. In 2001, look for renewed debate on tax credits for new small business pension plans and for matching funds on retirement savings by low and middle-income workers – included in the Senate version of H.R. 1102 but dropped in conference.
IRAs	H.R. 1102 from 106th Congress	Broad support for increasing IRA contribution limits, but IRA's principal sponsor, Sen. Bill Roth (R-DE) lost his reelection bid. Some Democrats are not enamored, saying the proposal favors the better-off. If a tax bill gains momentum this year, it's got a good chance of enactment; but next year the proposal will need a new "white knight" and a renewed effort.
Financial Privacy	A host of bills by President Clinton and Congress in dealing with financial and health care information, which impose "opt in" and/or "opt out" requirements for consumers	Protecting customers' privacy will dominate the agenda next year. Business interests will require skilled handling to overcome consumer misunderstanding and fear of loss of privacy.
Estate Tax	Congressional proposals to repeal or reform the estate and gift tax	Under a Bush presidency, expect an early, hard push for repeal. Under a Gore presidency, the issue will be on the backs of the Republican Congress with swing votes coming from conservative Democrats. The ultimate fate of this issue may depend on the GOPs willingness to compromise on a proposal which does not include repeal.
Long-Term Care Insurance	Congressional proposals for an above-the-line deduction for individual LTC insurance purchases	Broad, bipartisan support exists, particularly if paired with a credit for out-of-pocket LTC costs.
Across the Board Rate Cuts	A key Bush campaign promise	A Bush White House is expected to push hard for across-the-board income tax rate reductions; Democrats are not expected to favor.
Charitable Giving	A congressional proposal to allow tax-free rollovers of IRAs to charities; Bush promoted making the individual charitable deduction "above the line," and raising the cap on corporate giving	While not a top tier item under either Administration, look for further proposals to arise in Congress.
Education	Bush advocates expanding Education IRAs to $5,000 per child; Gore promotes a "401(j) lifelong learning" account to save on a tax-favored basis for education expenses	Politically, both sides agree education is a top voter issue. But whether this translates into more education tax incentives is unclear. Expanded Education IRA legislation has a better chance under Bush than Gore.

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New Comparability Plans Survive

3%, it would have to limit the contribution rate for Group A to 9% (so the one-third test can be satisfied under the gateway test), even if the plan's EBRs could pass the rate group test if the contribution rate were greater than 9%. If the plan does not meet the gateway test, then the plan could not use EBRs to pass the rate group test.

Note that there is a different compensation rule for the one-third test than for the 5% test. The one-third test is based on the allocation rate. An employee's allocation rate is the percentage obtained by dividing the employee's allocation for the plan year derived from employer contributions (other than matching contributions, if the plan also includes a 401(k) arrangement) and forfeitures, divided by the employee's plan year compensation. Plan year compensation, in turn, is defined in the regulations as compensation determined under IRC §414(s) (generally measured for the plan year or the portion of the plan year that the employee is eligible for the plan). The 5% test, which is a safe harbor for meeting the gateway, is based on IRC §415(c)(3) compensation, which is the same definition used to determine top heavy minimum contributions. If the plan determines allocation rates on the basis of IRC §415(c)(3) compensation, then the gateway is simply satisfied if each NHC's allocation rate is at least 5% (or one-third of the highest HCE allocation rate, if that highest rate is less than 15%). Where the highest HCE allocation rate is 15% or greater, a 5% allocation rate will always satisfy the gateway because the definition of compensation being used to calculate allocation rates is the same definition that the Treasury uses to calculate the 5% safe harbor. However, if the plan determines allocation rates on the basis of a definition of compensation which satisfies IRC §414(s), but does not satisfy IRC §415(c)(3), it is possible that the one-third test may result in a minimum NHC allocation under the gateway test that is less than 5% of IRC §415(c)(3) compensation, even though the percentage under the one-third test is greater than 5%.

Example: Suppose the plan uses "net" compensation to determine allocation rates, meaning IRC §415(c)(3) compensation reduced by the amount of elective deferrals (e.g., 401(k) deferrals, cafeteria plan deferrals), which satisfies IRC §414(s), and the highest allocation rate of any HCE using this definition is 16%. The one-third test is satisfied if each NHC has an allocation rate (using the same definition of compensation) that is at least 5.33%. Therefore, if no NHC has an allocation rate less than 5.33%, the gateway is satisfied, even though some of the NHCs might have an allocation that is less than 5% of IRC §415(c)(3) compensation.

Broadly available allocation rates

The proposed regulations would not require a plan to pass the gateway test described above, so long as each allocation rate can meet a "broadly available" test. The broadly available test essentially treats each allocation rate in a manner similar to the way "benefits, rights or features" (BRFs) are treated under Treas. Reg. §1.401(a)(4)-4. That regulation requires that each BRF under the plan is available to a group of employees who, if they were treated as participating in a separate plan, could satisfy the nondiscriminatory classification test. The nondiscriminatory classification test is the first part of the average benefits test under the minimum coverage requirements. The coverage ratio needed to pass the nondiscriminatory classification depends on the percentage of employees who are NHCs and must be within a range of 20% to 50%.

Disregarding age and service conditions used to determine allocation rates

When determining whether an allocation rate is available to an employee, age or service conditions on the allocation (e.g., rates based on age or rates based on length of service with the employer) may be disregarded, but only if the plan uses an allocation formula that applies to all employees who benefit under the plan, and provides a single schedule of rates that are based solely on age **or** service (but not both age **and** service), and only if allocation rates increase smoothly at regular intervals.

Regular intervals

To determine if age-based or service-based allocation groups are determined in regular intervals, there would have to be uniform age brackets or service brackets (excluding the highest bracket). Furthermore, if the brackets are based on age, and the first bracket ends at an age younger than 25, the length of the first bracket is deemed to be the same as the others. For example, if the plan provides separate allocation rates based on age, the first bracket being participants under age 25, with subsequent brackets in 5-year groups (e.g., ages 25-29, ages 30-34, ages 35-39, etc.), and the highest bracket age 65 and older, the allocation formula would satisfy the regular interval requirement.

Smooth increases

The allocation method is considered to have smooth increases if two tests are satisfied:

1. The allocation rate for each age band or service band is greater than the allocation rate for the prior age band or service band, but by no more than 5 percentage points, and
2. the ratio of the allocation rate for an age band or service band to the allocation rate for the previous age band or service band is not more than 2.0 or, if less, the ratio of the allocation rates for the two preceding bands.

To illustrate, suppose the allocation formula provides for age bands based on 5-year increments, as described in the prior paragraph. Suppose for the 2002 plan year that the allocation rate for the lowest age band is 2% and the allocation rate for the 25-29 age band is 3%. That means the ratio of the 25-29 age band's rate (3%) to the ratio of the under 25 age band's rate (2%) is 1.5. Since that ratio is no more than 2.0 ratio, the smooth increase test is passed so far. To pass the smooth increase test with respect to the next age based (30-34), the allocation rate could not exceed 4.5%, because that produces a 1.5 ratio when compared to the allocation rate for the 25-29 age band (4.5%/3%), and the ratio cannot exceed the ratio for the prior two age bands (which was 1.5). All of the age bands would have to meet this test in order for the plan to be able to disregard the age condition when applying the broadly available test.

What if the "regular intervals" and "smooth increases" tests are not satisfied? All that means is that the age conditions or service conditions used to determine the allocation groups cannot be ignored when determining whether those allocation groups pass the nondiscriminatory classification test. If, as a result, not all of the allocation groups could pass the nondiscriminatory classification test, the plan would have to satisfy the gateway test in order to use EBRs to show that the rate group test is satisfied.

What's the practical implication of the broadly available allocation rates option?

The Treasury's primary motivation in proposing these rules was to address the fact that NHCs are often not able to "grow into" the higher allocation rates available under a new comparability plan. Take the plan described in the examples under the explanation of the gateway test above. In that plan, the higher allocation rates are provided only to owners, who are the eligible employees included in Group A. A non-owner, which would include any of the NHCs eligible for the plan, would not move into Group A, regardless of his age or how long he works for the company. In addition, Group A does not consist of a group of employees that could pass the nondiscriminatory classification test because 0% of the NHCs have the Group A contribution rate available to them. Therefore, this plan, starting in the 2002 plan year, would have to satisfy the gateway test in order to continue using EBRs to test under IRC §401(a)(4).

What type of plan design might meet the broadly available test?

Consider the following example. BMI Corporation has three allocation groups. Each group covers a different division. For each plan year, a different contribution rate is made for each division based on its profitability. For the 2002 plan year, Division A's group gets a 20% allocation rate, Division B's group gets a 7% allocation rate and Division C's group gets a 3% allocation rate. Assume there are HCEs and NHCs in each group. The gateway test is not satisfied because the NHCs in the Division C group have an allocation rate that is less than one-third of the allocation rate received by the HCEs in the Division A group, and they have not received an allocation equal to at least 5% of their §415(c)(3) compensation. But suppose that each division passes the nondiscriminatory classification test. Thus, the 20%, 7%, and 3% allocation rates are broadly available, and the plan would not have to pass the gateway test in order to be tested on the basis of EBRs.

Another example would be age-weighted plans. These plans are designed to make allocation strictly based on age, providing a higher allocation rate as the participant gets older to take into account that each year's contribution will be accumulated over a shorter period of time to normal retirement age because of the participant's advancing age. Generally, unless the 415 limits result in a lesser allocation, or the top heavy minimum contribution rules result in a greater allocation, the age-based allocation method will produce identical EBRs for each eligible participant. Age-weighted plans generally will satisfy the standards for disregarding age conditions, which is the sole reason why employees receive different allocation rates under the age-weighted formula. Thus, these plans will be able to ignore the gateway test under the proposed regulations because all participants would be deemed to have the highest allocation rate available to them. The age-weighted plan would still be able to use EBRs to pass §401(a)(4), even if some of the NHCs receive a lower contribution rate than would be required under the gateway test.

Impact on safe harbor 401(k) plans

Sometimes the employer maintains a safe harbor 401(k) plan in addition to (or as part of) a new comparability profit sharing plan. If the profit sharing contributions are tested on the basis of EBRs, and the gateway test has to be satisfied, the safe harbor nonelective contribution under the safe harbor 401(k) rules is permitted to be included in the determination of whether the gateway test is satisfied. For example, suppose an employer maintains a new comparability plan with a safe harbor 401(k) arrangement. To satisfy the 401(k) safe harbor, the employer provides the 3% safe harbor nonelective contribution. In addition, a discretionary profit sharing plan is provided using the plan design described in the examples under the explanation of the gateway test above. (Group A consists of owners, Group B consists of all other eligible employees). The 3% safe harbor nonelective contribution may be counted in determining whether the Group B employees satisfy the gateway test. Thus, if the gateway test requires NHCs to have at least a 5% allocation, and all the Group B employees are eligible for the 3% safe harbor nonelective contribution, then their allocation from the discretionary contribution would only have to equal at least 2% of compensation.

Defined benefit/defined contribution plan combinations

In some cases an employer maintains both a defined benefit plan and a defined contribution plan. Under these proposed regulations, if those plans are permissively aggregated in order to pass coverage and nondiscrimination testing (known as a DB/DC plan), and the nondiscrimination test is run on the basis of benefits (i.e., normal accrual rates under the DB plan plus EBRs under the DC plan), additional conditions would be imposed starting in the 2002 plan year.

What are the additional conditions?

The DB/DC plan would have to meet a special gateway test, on an allocations basis, unless:

1. The DB/DC plan is "primarily defined benefit", **or**
2. the DC component and DB component of the aggregated DB/DC plan are broadly available if tested separately.

A DB/DC plan would be treated as primarily defined benefit if 50% or more of the NHCs benefiting under the plan have a normal accrual rate under the DB plan that exceeds their EBRs under the DC plan. The special gateway test that would apply if the DB/DC plan could not satisfy (1) or (2) would require that each NHC's combined allocation rate (i.e., the sum of the NHC's allocation rate under the DC plan and the NHC's equivalent allocation rate under the DB plan) could not be less than 5%, if the highest combined allocation rate for any HCE is 25% or less. If the highest HCE combined allocation rate is more than 25%, the minimum combined allocation rate for the NHCs would be 5% plus 1% point for each 5% points (or portion thereof) that the highest HCE rate exceeds 25% (e.g., 6% if the highest HCE rate is more than 25% but not more than 30%). If one of these tests could not be satisfied, the DB/DC plan would not be permitted to test on the basis of benefits. In other words, it would have to test on the basis of contributions. If the DB plan is tested separately from the DC plan (i.e., there is no DB/DC plan for testing purposes), the requirements in this paragraph would not apply.

Review regulations and your plan designs now

Now is the time to review the regulations and determine how they will affect the plan designs of your clients (or your own plan, if you're also a plan sponsor of a new comparability plan). Assess whether contributions will need to increase for the NHCs (or some of the NHCs) in order to keep the HCEs at present levels. For your currently effective new comparability plans, look to see what the lowest contribution rate has been for the NHCs. If it is at least 5%, this regulation would not change a thing (unless the plan defines compensation different from the IRC §415(c)(3) definition, so that a 5% allocation under the plan might not be sufficient to meet the gateway). If the lowest NHC contribution rate is less than 5%, the employer will need to be prepared to raise the contribution rate for some of its NHCs if the lowest rate otherwise would be less than the applicable gateway percentage.

This is also the time to determine whether the proposed regulations are inadvertently disrupting legitimate plan designs that the Treasury did not intend to subject to the gateway test. If you identify any such situations, send your comments to the Department of Treasury as soon as possible. These proposed regulations are probably on a "fast track" for finalization. ▲

Sal Tripodi, APM, J.D., LL.M., is the principal of TRI Pension Services, a nationally-based consulting firm in Highlands Ranch, CO. Mr. Tripodi is the author of The ERISA Outline Book. *The 2001 edition is available December 2000 and is distributed exclusively by ASPA. TRI Pension Services provides numerous in-house seminars for financial institutions, administration firms, and other pension service providers throughout the country, and also publishes a quarterly newsletter* (ERISA Views). *For more information about TRI Pension Services, visit its website – www.cybERISA.com.*

John P. Griffin, APM, J.D., LL.M., is a principal with Global Benefit Advisors, LLC in Englewood, Colorado. He has over 20 years experience in the employee benefits area. His firm specializes in qualified plan drafting, employee benefit seminars, and compliance consulting. His firm, along with Sal Tripodi, drafted the new mass submitter M&P plan for FDP Corp. (now affiliated with SunGard Corbel).

A Special Thanks for making the 2000 ASPA Annual Conference a huge success!

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Memories from the

2000 ASPA
ANNUAL CONFERENCE

2000 ASPA Annual Conference

Scott D. Miller, FSPA, CPC, and Carol R. Sears, FSPA, CPC, take a breather from their ASPA volunteer work (Scott is ASPA's treasurer and Carol is an ASPA past president) and enjoy the opening general session.

Nancy D. Lapera, the Conferences' ers, had a copy of h signed by Helen T former White House spondent for United International. Ms. T spoke at one of t cheons.

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Howard J. Johnson, MSPA, presents Leslie S. Shapiro, J.D. the prestigious Eidson Award. Mr. Shapiro received the award in recognition of his tireless efforts toward gaining ASPA credibility among actuarial organizations in the United States.

Ilene H. Ferenczy, CPC, updates Conference attendees on 401(k) Plans in Mergers and Acquisitions.

ASPA's Conference attendees pack the room to learn from informative and often entertaining speakers.

Brian H. Graff, Esq., CPA, ASPA's Executive Director, updates the attendees on the latest news from Capitol Hill.

Annual Conference Chair, Beverly B. Haslauer, CPC, QPA, watches the Capitol Steps perform. John P. Parks, MSPA, 2000 ASPA President, and his wife, Iris, also enjoy the show.

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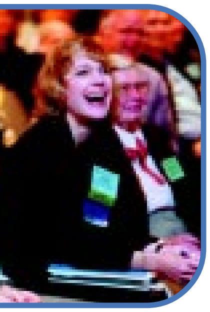

Craig P. Hoffman, APM, ASPA's President-Elect, is a frequent and respected speaker at ASPA's conferences.

Lou Campagna, Mabel Lum Capolongo, Scott Albert, QPA, and Joe Canary represent the Department of Labor and respond to questions submitted by Conference attendees.

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Cheryl L. Morgan, CPC, receives the 2000 Educator's Award from Education & Examination Committee Chair, Gwen S. O'Connell, CPC, QPA. Cheryl was recognized for her 19 years of continued involvement with ASPA's education program.

General Conference
Chair, Stephen L.
Dobrow, CPC, QPA,
is wife, Donna, the
Panda*, and Terri
Weatherby, QPA, en-
oy some camarade-
ie at the Gala.

Ken Morton, one of ASPA's meetings coordinators, takes note of the Gala's date – Halloween, and shows up in costume. Or is that how Ken always dresses at ASPA?

John P. Parks, MSPA, ASPA's 2000 President, and George J. Taylor, MSPA, ASPA's 2001 President, review the Conference brochure and decide which session to attend.

Exhibitors demonstrate the latest tools to help attendees streamline their businesses.

Special Gala entertainment was provided by the Drifters.

Mark your calendar now and plan to attend next year's ASPA Annual Conference – October 28-31, 2001!

* *The Panda was identified as Larry Starr, CPC, Co-chair of ASPA's Political Action Committee and member of ASPA's Government Affairs Steering Committee.*

CONTINUED FROM PAGE 3

Internal Revenue Service

(4) developing the methodology for examining the largest employers (which is not the same as auditing the plans of the largest employers or the largest plans).

The IRS also indicated that they were looking at the issue of "orphan plans," that is, plans where there is no longer a sponsor (because of bankruptcy, death, or business dissolution), but assets continue to be held in trust. They are working with the DOL to determine how to deal with these types of plans, from both a qualification standpoint – so as not to adversely affect participants with benefits still in the trust – and a fiduciary standpoint. If appropriate, GAC will provide comments on this issue.

"Cincinnati" Issues

We learned that the IRS is processing new cash balance plans for favorable determination letters (FDL). However, if the plan is a conversion from a defined benefit plan to a cash balance plan, they continue to automatically refer the plan to Washington, D.C., where the application will be held in abeyance pending resolution of the open legal issues. All defined benefit plans are receiving a caveat regarding cash balance conversions, just in case the reviewing agent is not aware that the plan document is a conversion from a defined benefit plan.

Regarding the age-discrimination issue present in cash balance plans, the IRS and Treasury officials indicated that they, the EEOC, and the DOL, are jointly working to resolve the issue. While they did not give us any indication of how or when the issues would be resolved, it appears that there is a common desire to allow employers to adopt new cash balance plans without there being an age-discrimination problem.

We pointed out that, in the FDL review process, ASPA's members are getting conflicting or extraneous requests from reviewers in different parts of the country. We stressed the need for uniformity and pointed out the cost burden of those conflicting and unwarranted requests. The IRS responded that they are currently revising the Form 5300 series, which should be out early next year, in an effort to eliminate some of the differences in requests. They are concerned about differences, and they make every effort to reduce or eliminate them. In fact, they are creating a new position, which is similar to an ombudsman, in Cincinnati, where complaints about differing treatment could be made and resolved.

We also discussed the possibility of significant changes to the FDL system. The IRS officials indicated that they were open to any and all ideas; that they were at the beginning of the process of re-examining the system and had not come to any conclusions about whether or how changes might be made. However, they are looking for ways to streamline the process and make it more efficient, including re-examining whether the IRS should continue to issue favorable determination letters. We stated that there was a critical need for FDLs, especially in the small plan market, and that shifting the burden on to private sector service providers to review and give assurances on plans would be cost-prohibitive. We urged the IRS to continue the FDL process.

However, GAC is setting up a committee to analyze changes which could be made to improve the system from both the IRS' and our members' perspectives. For example, the special committee will be looking at different levels of review, something akin to the current 401(a)(4) methodology. And we would expect to look at ways to reduce the workload for both the IRS and the private sector, including the rolling filing of plan documents by, for example, EIN numbers.

We also learned that the Cincinnati office is working on website development to assist plan sponsors and service providers in the filing process and on a newsletter for the same purpose.

EPCRS

The IRS is in the process of working on a new structure for the remedial programs, to combine the voluntary, IRS-supervised programs (VCR, SVP and Walk-in CAP) into a single program handled in the field offices. The IRS indicated that they expect the revised Revenue Procedure to be out next year. We urged them to consider ways to handle late filed 5500s under the new procedure, in light of the fact that the Form 5500s are now filed with the DOL. In the past, the late filings have been handled by the Revenue Agents and Walk-in CAP coordinators through Walk-in CAP. Also, we asked that the issue of restoration payments for fiduciary breaches be included in EPCRS, along with a formal "group VCR" program and a program for resolving excise tax issues (especially on prohibited transactions). The ability to voluntarily "walk-in" prohibited transaction excise taxes – at a reduced amount – would be supportive of the DOL's new Voluntary Fiduciary Correction program (VFC).

We asked the IRS what their experience with APRSC had been. They indicated that they have not been having their Revenue Agents gather data on APRSC corrections when they encountered it, either in a plan that had previously corrected under APRSC and was subsequently audited, or in a plan where the IRS found the defect during the audit and permitted it to be corrected under APRSC. We urged them to begin gathering that data so that it could be used for educational programs and thereby improve the quality of plan administration.

We also urged the IRS to implement an appeals procedure within EPCRS so that there would be a mechanism for resolving conflicts over the proper application of APRSC and the proper determination of sanctions under Audit CAP. We emphasized the importance of consistency in all of the programs, especially in light of the fact that APRSC and Audit CAP will be handled in the Examination Section of TE/GE and the voluntary programs will be handled through the Rulings Section.

We urged the IRS to review the Walk-in CAP fee structure.

The IRS indicated that in working on the new structure for EPCRS, they are considering ways to promote coordinate and consistent treatment for similar violations.

Finally, we discussed the findings in a recently released study of the IRS' remedial programs for disqualifying defects (EPCRS) by the GAO. Among other things, in its report, the GAO indicated that for the most recent year in the report, the Audit CAP sanctions were only about 30% higher than the Walk-in CAP compliance fees. While the GAO report measured fees and sanctions on a per-participant basis, it was consistent with data that we had previously obtained from the IRS which was prepared on a per-plan basis. We suggested that this reflected two things: first, it shows a more reasoned approach to the setting of Audit CAP sanctions; but, second, it shows that the compliance fees in Walk-in CAP are too high, especially for plans at the smaller end of the scale. We urged the IRS to review the Walk-in CAP fee structure.

Form 5500

We discussed the need for getting the forms out earlier in the year. We were advised that the 2000 plan year Form should be posted on the internet before the holiday season. We urged that the 2001 plan year Form also be published as soon as possible in 2001 so that we could avoid the problems encountered this year.

Additional Comments

In addition to this liaison meeting between the IRS and the Committee, there were other interesting IRS positions expressed at the Conference. In the IRS Q&A session with Jim Holland and Dick Wickersham, two sensitive insurance topics were discussed. The first dealt with the incidental death benefit rule and the so-called two-year or seasoned money rule. The question was whether, in a profit sharing plan, the taxation to a participant was the term cost or the full premium – if the plan used the seasoned money exception to avoid the incidental death benefit rule. The IRS stated that its position was that the full premium was taxable to the participant. The IRS speaker went on to say that, if the full premium was not taxed through to the participant, then the plan continued to be subject to the incidental death benefit qualification requirement.

The second insurance issue involved irrevocable subtrusts within the retirement plan. These subtrusts are established to hold the insurance policy in anticipation of avoiding estate taxes on the death of the participant. The IRS panelists took the position that the creation of an irrevocable subtrust within a qualified plan was a disqualifying defect – and stated several reasons for that conclusion. However, he also said that, if a favorable determination letter is obtained, it would preserve the plan's qualification.

Finally, in conversations with IRS officials, we learned that they were aware that overfunded defined benefit pension plans, and their sponsors, were being purchased by third parties to avoid the 50% tax on reversions under IRC §4980. The position of the IRS official was that, where the purchase lacked substantial economic and scrivener substance, the IRS would tax the transaction as a deemed reversion and impose the excise tax. A transaction would lack economic substance where, for example, there was not a sale of a viable, ongoing business, but instead the value of the sale was the excess in the defined benefit plan. ▲

C. Frederick Reish, APM, Esq., is a founder of and partner with the Los Angeles law firm Reish & Luftman. He is a former cochair of ASPA's Government Affairs Committee (GAC) and is currently the chair of GAC's Long Range Planning Committee. Bruce L. Ashton, APM, Esq., a partner with Reish & Luftman, is cochair of the Government Affairs Committee and serves on ASPA's Board of Directors.

Department of Treasury

by Jeffrey C. Chang, APM

On November 1st, members of ASPA's Government Affairs Committee met with Mark Iwry, Benefits Tax Counsel – Treasury, and members of his staff to share and discuss employee benefit issues and priorities for both the Treasury and ASPA. Representatives of the IRS also attended the meeting.

The meeting began with a discussion of the recently published results of the IRS's 401(k) audit project (results can be obtained at www.irs.gov). Both ASPA and Treasury agreed that the level of noncompliance indicated by the audit project (i.e., more than 44% of the 572 plans audited had some detected compliance problem) was disappointing and needed to be addressed.

A discussion followed during which a number of issues were raised:

- ASPA and Treasury agreed there is a need to better educate plan sponsors regarding the importance of complying with the qualification rules along with the importance of making sure that certain levels of compliance support and testing are being provided as part of their recordkeeping arrangement.
- Treasury was asked by ASPA to consider the long-term compliance implications of any changes to the current determination letter process. ASPA representatives indicated that the current IRS determination letter process is an important and essential mechanism to assist sponsors and advisors in making sure that plan documents are in compliance.
- ASPA and Treasury discussed the desirability of obtaining additional information regarding the incidence of noncompliance within 401(k) plans, particularly taking into account the type of service provider involved.
- ASPA's representatives noted that the average audit-CAP sanction indicated by the recent GAO study of EPCRS was only 30% higher than the average walk-in CAP sanction. ASPA requested that Treasury consider a further lowering of the Walk-in CAP sanctions as a way to encourage higher utilization of Walk-in CAP.
- The ASPA representatives renewed ASPA's request for, and support of, a group VCR program.
- Benefits Tax Counsel, Mark Iwry, invited ASPA to provide his office with written comments on ways ASPA believes overall plan compliance could be increased.

Next, the meeting moved to a discussion of compliance problems and the overall confusion surrounding the use of employee leasing arrangements and professional employer organizations (PEOs). The ASPA representatives provided several examples of the difficulties small businesses were having in understanding and complying with these complex rules. Mr. Iwry acknowledged that these issues were now a priority of his office and asked for ASPA's input.

The meeting closed with a discussion of the recently issued proposed regulations on new comparability plans. ASPA's representatives raised a number of issues with respect to the proposed regulations, including:

- The possibility that the proposed rules may unfairly burden certain sponsors of defined benefit/defined contribution combinations in a manner that Treasury and the IRS may not have intended. The Treasury officials agreed to receive ASPA's comments on this issue and to look into the matter.
- A question as to why the proposed rules require the use of section 415(c) compensation rather than section 414(s) compensation. Treasury officials explained that they used the broader section 415(c) definition of compensation to prevent plans from using a much narrower compensation – one that would undercut the protections of the minimum allocation gateways. Furthermore, they indicated that this use of section 415(c) compensation was consistent with existing top-heavy minimum allocation rules.
- Confirmation that only participants who "benefited" under a plan's allocation formula were entitled to a gateway allocation. Therefore, it would be acceptable for a new comparability plan to contain a "last day" requirement for an allocation. ▲

Jeffrey C. Chang, APM, is a shareholder in the law firm of Chang, Ruthenberg & Long Law Corporation. Mr. Chang specializes in profit sharing and pension plans, as well as various deferred compensation and employee benefits matters. He is the founder of the Sacramento Employee Benefits Roundtable, has taught deferred compensation and qualified retirement plans courses in the Masters of Law program at McGeorge School of Law, and is a former member of the executive committee of the State Bar's Taxation Section. Mr. Chang currently serves as the chair of the IRS subcommittee of ASPA's Administration Relations Committee. Recently, he co-authored the Business Owner's Retirement Plan Survival Guide, *along with his partner, Ken Ruthenberg, and the principals of Foord, Van Druggen & Ebersole Financial Services. Mr. Chang received a B.A. in Economics from U.C. Berkeley in 1976, and a J.D. from U.C. Davis School of Law in 1979.*

Department of Labor

by R. Bradford Huss, APM

Representatives of ASPA's Government Affairs Committee met on October 31, 2000 with senior officials of the Pension and Welfare Benefits Administration (PWBA) of the United States Department of Labor. Attendees at the meeting from the DOL included Leslie Kramerich, Acting Assistant Secretary of Labor for the PWBA; Alan Lebowitz, Deputy Assistant Secretary for Program Operations; Ian Dingwall, Chief Accountant; and Virginia Smith, Director of Enforcement. The first topic of discussion was the difficulty experienced by many practitioners in the Form 5500 filing process this year in light of the changeover to filing with the Department of Labor. The DOL officials expressed their sensitivity to the problems experienced during the current filing season and they noted that, although the initial 1999 forms were out by February of 2000, the software necessary for the new filing process was not available until later. The DOL officials indicated that they are trying very hard to get the 2000 forms out as soon as possible. There will be some changes in the 2000 forms which are required by changes in the law, but the DOL does not expect any major changes. Accordingly, DOL believes there will be less preparation required by software developers for the next filing cycle because the changes to the form will not be extensive and the developers are not starting from scratch, as was the case for the 1999 forms. In addition, the DOL expects that the e-filing option should be more widely available.

The DOL hopes to provide the final version of the 2000 form to developers in November or shortly thereafter. At that time, the layout of the Form 5500 and updated instructions will be posted on the DOL's website. The posting, however, will be for information purposes only and this version of the form will not available for downloading and filing. The DOL is making some adjustments in the instructions for the 2000 Form 5500, based upon comments received and actual filing problems noted, with respect to the 1999 form. The DOL, at this point, needs input on the filing process with a goal toward improvement rather than detailed comments on revision of the 2000 forms, as that process is already well underway.

ASPA representatives emphasized the need to also issue the 2001 version of Form 5500 as soon as possible. The DOL officials indicated their understanding of the need to issue new forms quickly but stated that potential changes in the law, with the pension reform legislation pending in Congress, limit the DOL's ability to put the 2001 form out as early as desired by practitioners.

There will be some changes in the 2000 forms [5500] which are required by changes in the law, but the DOL doesn't expect any major changes.

The portion of the discussion with the DOL concerning the recent Form 5500 filing difficulties was led by Theresa Lensander, Chair of the GAC Administration Relations Committee, and Valeri Stevens, Chair of the GAC Reporting and Disclosure Sub-Committee. Both Theresa and Valeri are service providers who personally endured the problems of the 1999 Form 5500 filing process, and they were able to relay their firsthand experiences to the DOL officials.

ASPA stressed to the DOL that there should be no penalties assessed for the late filing of a Form 5500 where the plan administrator and its service providers were unable to meet the October 16, 2000 extended deadline because of the very late issuance of the forms and the necessary software. ASPA reiterated its prior request that no penalties be assessed with respect to any 1999 Form 5500 properly filed by December 31, 2000. The DOL officials responded by saying that no penalty will be assessed for late filing of a 1999 Form 5500 if an appropriate showing of reasonable cause for the late filing is made. In general, the DOL will not respond immediately if a Form 5500 is filed late accompanied by a statement of reasonable cause for the late filing. The DOL will review the reasonable cause statement in due course and will, in all cases, make an analysis of the reasonable cause prior to sending out any letter assessing penalties for the late filing. The DOL also indicated that, if a satisfactory showing of reasonable cause has been made, there generally will be no response by the DOL to either the reasonable cause letter or the late Form 5500. The DOL recommends that plan sponsors and practitioners file any currently overdue Forms 5500 as soon as possible. The DOL does not intend to make any further statements, beyond its prior announcements, with respect to the late filing penalty issue.

The DOL officials reviewed with ASPA the actual results to date of the 1999 filing season. At this point, DOL has received about 900,000 Forms 5500. This amount, however, is about 300,000 forms less than the number usually received at this point in the cycle, representing about one quarter of the filing population. For the 1999 filing season, approximately 15,000 e-filed forms were received. The mechanics for electronic filing are still being worked out and one problem has been a delay in the ability to issue PINs. The DOL believes that this bottleneck in the system has been resolved and notes that a number of practitioners were able to e-file the 1999 Form 5500 for their clients.

On another subject, the ASPA representatives complimented the DOL on the recently issued final Small Plan Asset Security regulations. ASPA believes that the DOL tried hard to achieve a balance between providing greater security for the assets of small plans and minimizing the additional administrative burdens imposed by the new requirements for a small plan to be eligible for waiver of the annual audit requirement. ASPA stated its appreciation that many of the comments by ASPA GAC in response to the DOL's initial proposed regulations were incorporated by the DOL into the final set of regulations, including a provision for a delayed effective date for the new requirements.

At the meeting, the GAC representatives delivered to the DOL a comment letter calling for a revision of the DOL's Delinquent Filer Voluntary Compliance Program (DFVC), which permits the filing of delinquent Form 5500s without imposition of the entire statutory penalty. ASPA stated its belief that most failures to file a timely Form 5500 are due to inadvertent error and that the current penalties under the DFVC program, although reduced from the maximum possible amount, are still too high to effectively encourage voluntary compliance to correct late filings. The letter delivered by the ASPA representatives requests that the penalties for submission of a late Form 5500 under DFVC be significantly lower in order to increase the correction of delinquent filings. ASPA also requests that DFVC be revised to include a procedure under which no penalties would be imposed if a plan administrator were to make an adequate showing of reasonable cause for the late filing. ASPA further requests that the DOL coordinate the DFVC program with the Internal Revenue Service so that a DFVC filing also resolves any potential imposition of late filing penalties by the IRS. The DOL officials indicated that the PWBA has recently been looking at a revision of the DFVC program. The DOL agrees with ASPA that a revision of the DFVC program is appropriate and that a new development with respect to DFVC could be anticipated shortly. The DOL is concerned about a lack of deterrence for late filing if the DFVC penalties were to be lowered too much. In addition, the DOL indicated that its DFVC program will not be able to impact how the IRS administers its penalty program for late Forms 5500.

The ASPA representatives also discussed the DOL's recently issued Voluntary Fiduciary Correction program (VFC), the concept for which was originated and first proposed to the DOL by ASPA GAC. After the submission to the DOL of several detailed proposals by GAC and several years of discussion between the DOL and ASPA, the initial version of VFC was

Chartered Financial Consultants Now Eligible for APM Designation

The ASPA Board of Directors voted at their October 2000 meeting to grant those individuals with the prerequisite three years of pension practice experience, who have been awarded the designation of Chartered Financial Consultant (ChFC) from the American College, eligibility to become an Associated Professional Member (APM) of ASPA.

ASPA created the APM membership category several years ago to recognize those professionals who are involved in the employee benefits field and have also achieved professional recognition in another field. ASPA's Board of Directors has deemed that the ChFC designation justifies admittance into this same category.

The following professionals are eligible for the APM designation if they meet the additional requirement of three years of experience in pension-related matters:

> (1) attorneys currently admitted to the bar in any jurisdiction in the United States, (2) accountants who have attained the CPA designation, (3) enrolled agents who are enrolled to practice before the IRS, (4) those who have been awarded the MSFS degree from the Graduate School of Financial Sciences of the American College, Bryn Mawr, Pennsylvania, (5) those who have been awarded the designation of Chartered Life Underwriter or Chartered Financial Consultant from The American College, Bryn Mawr, Pennsylvania, and (6) other professional designations as follows: Member of the Academy of Actuaries; Associate, Member, and Fellow of the Conference of Consulting Actuaries; Associate and Fellow of the Society of Actuaries; and Accredited Pension Administrator of the National Institute of Pension Administrators.

For more information, or to receive a designated membership application, contact ASPA's membership department at (703) 516-9300 or visit our web site at **www.aspa.org**.

issued in March of 2000. The DOL discussed its experience in the months since the release of the VFC program. DOL has received a number of VFC applications from all over the country but would not discuss the specific number. Many of the VFC applications received so far concern the correction of the late deposit of 401(k) salary deferrals. In addition to the receipt of actual applications, the DOL is encouraged by the number of phone calls being made to DOL regional offices inquiring about the VFC program and the possible eligibility of certain plans for the program.

The ASPA representatives noted that GAC has filed detailed comments with the DOL on the initial version of VFC and has recommended a number of changes be made in the final version of the program. In particular, ASPA stressed its belief that the DOL should eliminate the current requirement under VFC that notice of a VFC application to the DOL be provided to all plan participants. ASPA's GAC believes that the VFC program provides adequate safeguards for plan participants without the blanket requirement for notice to all plan participants in every case. ASPA is concerned that the notice requirement may discourage eligible plan sponsors and fiduciaries from utilizing VFC. The ASPA representatives also reiterated GAC's comments that the VFC program should provide for a waiver of excise taxes on prohibited transactions corrected under VFC and that a successful VFC program will need to include an ability to discuss violations and correction methodology with the DOL on an anonymous basis.

The meeting also included a discussion of the status of legislative proposals to allow mutual fund companies and other providers of investments for plans to provide investment advice to plan participants even in plans where the investment providers' own funds were offered as participant-directed choices. Both the DOL and ASPA have opposed such proposals because they would weaken the prohibited transaction rules of ERISA that were designed to protect plan participants from self-dealing and would create potentially difficult conflicts of interest on the part of the investment providers. While it was acknowledged that such legislative proposals are apparently dead for the current session of Congress, it was agreed that the DOL and ASPA would continue to work together to monitor and review any new proposals of this sort.

The ASPA representatives also discussed the increasing use of so-called "life-style funds" within participant-directed plans. The DOL agreed that the use of such funds provides an important and helpful alternative to the traditional menu of mutual funds or other investment options offered under most ERISA Section 404(c) arrangements. ASPA suggested that the DOL consider a clarification of its Section 404(c) regulation to recognize that the offering of different life-style funds could meet the diverse offering requirement of the Section 404(c) rules.

The DOL representatives discussed the next Saver Summit and asked for input from ASPA on ways to make it more productive. ASPA agreed that it would work with the DOL and other summit participants to identify areas of consensus.

The meeting closed with a discussion of the need to find additional ways to educate both plan participants and plan sponsors on the importance of ERISA's requirements concerning disclosures to participants. ASPA agreed that it would provide assistance to the DOL in this area. ▲

R. Bradford Huss, APM, is a partner in the San Francisco, California law firm of Trucker Huss which specializes in ERISA and employee benefits. Mr. Huss concentrates his practice on qualified pension and profit sharing plans, ERISA litigation, and IRS and DOL audits of employee benefit plans. He serves on ASPA's Board of Directors, is a cochair of ASPA's Government Affairs Committee, is a past president of the San Francisco Chapter of the Western Pension & Benefits Conference, and is a member of the American Bar Association, the Bar Association of San Francisco, and the International Foundation of Employee Benefit Plans.

Pension Benefit Guaranty Corporation

by Kurt F. Piper, MSPA

Representatives of ASPA's Government Affairs Committee met on October 31, 2000 with representatives of the Pension Benefit Guaranty Corporation (PBGC). This was our semiannual conference to discuss a range of issues of importance to ASPA members.

The first item of discussion was cash balance plans. The PBGC has been trying to cope with the termination (and anticipated termination) of underfunded cash balance plans. As part of the termination process, it is necessary to estimate the present value of benefit liabilities. This calculation does not just affect the money that a sponsor owes the PBGC; it can also affect what the other participants get under ERISA 4044.

One specific calculation that is problematic is the determination of the accrued benefit that is payable as a qualified joint and survivor life annuity. In a cash balance plan, the actual value of the index (e.g., 30-year

Treasury rates) determines the accrued annuity benefit payable at normal retirement age from the current cash balance. Ongoing plans do not have a problem, as it is simple to determine the actual index at the point in time that a benefit is actually paid. However, a terminating plan can only estimate the accrued annuity benefit since the actual value of the index can only be estimated. When a plan does not have language in the document to adequately describe the procedure after plan termination, the burden falls on the Plan Administrator or, in the case of a distress termination, the PBGC to fix the accrued annuity benefit.

One might think that since the PBGC only has to pay deminimus lump sums (under $5,000) under a distress termination, the problem is minimal. This issue is not so simple due to complications concerning how the PBGC regulations say to pay deminimis lump sums. First, you apply the variable rate index to get a benefit at NRA; next, you use PBGC lump sum assumptions to get the prevent value. If the value is less than $5,000, then the PBGC can pay a lump sum; if not, then the PBGC can't. Note that this value will be different than the cash balance account balance. The PBGC might have to change their regulations to resolve this situation.

The determination of the estimated index in the calculation of the accrued annuity benefit can also have a large effect on benefit liabilities, on the allocation of assets at plan termination, and finally, on amounts participants are allocated under ERISA 4044. Furthermore, without any certainty, it is impossible to give participants a firm idea of their accrued annuity benefit until actual retirement.

Ed Burrows suggested that one way to manage the problem is to have the IRS require adequate Plan language to spell out what happens to a variable index upon plan termination and, perhaps, to remove the 411(d)(6) protection so as to fix the variable rate. The IRS could entice plans to use this approach if the IRS could ensure plans with such language a swifter determination letter process at plan termination. (Or, perhaps to give plans without such language a harder time.) This does require IRS and Treasury to be willing to allow terminating plans to deal with the issues of 411(d)(6) protection, definitely determinable benefits, and back-loading concerns. The politics of this are not helpful at the moment. Ed Burrows also reminded the group that cash balance plans that allow Participants to elect which index to use for their cash balance account are coming. These plans will present special problems.

The second item of discussion included proposals to foster defined benefit pension plans. The current tax bill has a host of items, including the cap on the variable premium for small plans, paying interest on premium overpayments, the missing participant program for defined contribution plans and professional defined benefit pension plans, extending the guaranty on substantial owner benefits, the eventual elimination of the OBRA '87 full funding limit, and the "topping off rule" to allow Title IV plan sponsors to deduct a contribution needed to fully fund benefit liabilities. It is hoped that if the tax bill fails this year, these provisions would find their way into a tax bill in early 2001.

The third item of discussion was to request more examples of how to calculate the amount to send to the PBGC for missing participants. There is a real need for a calculator program to calculate the PBGC annuity values, since many industry software programs do not do so. Such a program is actually in the works and hopefully will be available soon.

The fourth item of discussion was the PBGC-1 and Schedule A for 2001. ASPA was hoping for an early release. The PBGC informed us that they cannot issue the premium form package until it is clear whether the provisions in the tax bill will be enacted this year, since many of the provisions would go into effect in 2001. The PBGC is therefore working on two sets of instructions, one set if the bill is enacted and another if it is not.

ASPA thanked the PBGC again for extending the filing date for form PBGC-1 until the Form 5500 due date. This helped Service Providers tremendously with respect to meeting the October 16, 2000 filing deadline. Interestingly the PBGC did not believe that the delay in the release of the Form 5500 software affected the timing of the filing of the PBGC-1 forms for Calendar year 2000.

Conclusion

The meeting with the PBGC was very constructive. It is encouraging to see the PBGC very anxious to promote the growth of defined benefit pension plans and prevent politics from destroying the incentive for employers to implement and continue defined benefit pension plans. ▲

Kurt F. Piper, MSPA, is owner and Chief Actuary of Piper Pension & Profit Sharing in Los Angeles. Mr. Piper serves on ASPA's Board of Directors, is a member of the American Academy of Actuaries, an associate of the Society of Actuaries, a Member of ASPA, and an Enrolled Actuary. He is a frequent speaker and currently serves as chair of GAC's Regulations Committee.

Welcome New Members

Welcome and congratulations to ASPA's new members and recent designees.

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Focus on The Pension Actuary

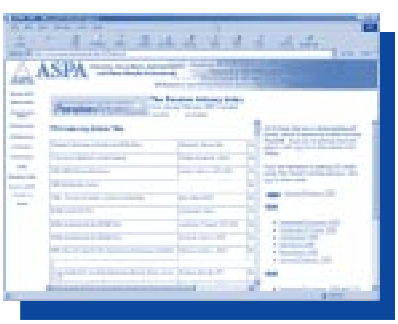
We Value Your Opinions

by Chris Stroud, MSPA

As the year 2000 comes to a close, we would like to review our past year in print. Even more importantly, we'd like to **solicit your suggestions** on how we can continue to enhance and improve the newsletter by asking you to **complete and fax back the enclosed survey**.

Over the past year, we've updated the look of the newsletter, and we've begun to include more graphics and photographs. You will continue to see progress in these areas over the coming year. The Calendar and the Bulletin Board are now permanently located on the back page, making it easy for you to find and refer to for your scheduling needs. We took the opportunity in this special "millennium" year to include some retrospective articles, as we felt it was important not just to look at where we are today, but also to revisit how far we've come over the years.

Early in the year, we added an Index on the ASPA website, **www.aspa.org**, which can be sorted alphabetically by Article Title or by Author's Name. To access the Index, select the "Members Only" section and click on *The Pension Actuary* at the top of the Members Only page. The Index includes articles from January/February 1997 to the present, and the issues containing each of these articles can be viewed and/or printed (in .pdf format) from the same site.



One of the challenges we face today with *The Pension Actuary* is that in today's fast-pace electronic world, our members have many opportunities to get the "latest update" on regulations, pending legislation, etc. Many of you already subscribe to the *ASPA ASAP's*, which do a great job of keeping you abreast of current issues. Due to the nature of our newsletter and the time it takes to get it produced, printed, and mailed (usually by bulk mail, which often can be slow), we are seldom able to include time-sensitive topics. However, we do occasionally provide additional details to an *ASPA ASAP* through a more expansive article. We've tried to slowly shift the focus of the newsletter to the type of topics that provide in-depth discussion on issues of interest and industry trends, including more practical articles that help you run your business. We will continue to expand the type of topics we include to reflect the changes taking place in our industry, and this area is especially where we need your help. As we begin planning our newsletter calendar for 2001, we'd like to know what issues are of most interest to you. We have included a survey for you to fax back to us, which will allow you to let us know what types of articles you'd like to see over the coming year.

I'd like to express my sincere thanks to *The Pension Actuary* newsletter committee and to our contributing authors. The volunteer time that these people have contributed over the past year was vital to the success of the newsletter. I would also like to thank the ASPA Staff for their hard work and dedication over the year to make each issue of the newsletter come to reality.

Let's all work together to make next year's newsletter even better! ▲

Chris Stroud, MSPA, MAAA, EA, is the President of Stroud Consulting Services, Inc. in Miami, FL, providing consulting services to various companies including SunGard Corbel and FDP Corporation. Ms. Stroud is also a Principal of Benefits Consortium, which offers employee benefit education services, marketing and sales force training, review of plan administration operations, etc. for service providers and financial institutions. Ms. Stroud currently serves on the Board of Directors for ASPA and is the Editor of The Pension Actuary.

PIX Digest

The Pension Information eXchange (PIX) is an online service for pension practitioners. ASPA has co-sponsored the PIX Pension Forum for many years. For more information about PIX, call (805) 683-4334.

401(k) Deposits – How Bright a Line?

[Thread #90579]

The new 5500 Schedules H and I ask specifically if the employer did not deposit deferrals on a timely basis, with a specific reference to the plan asset regulations. These regulations specify the well-known "15th business day" rule as well as the less well-known "as soon as administratively feasible" standard.

This thread starts out with a user asking how to complete this question on Schedule H, as well as the companion question about the plan engaging in any non-exempt transactions with a party-in-interest and the "amount involved."

Initially there was a significant discussion about whether the "amount involved" is the entire amount of the late deferral deposit, or just the interest for the use of the late deposit for the time it was being improperly held by the employer. Compelling arguments were made that it is just the interest, quoting from Section 2560.502i-1 of the DOL regulations:

> "(ii) Where the use of money or other property is involved, the amount involved shall be the greater of the amount paid for such use or the fair market value of such use for the period for which the money or other property is used."

Participants then began a discussion about how, as a practical matter, a TPA firm can properly advise clients of the "as soon as feasible" requirements, and on an ongoing basis, properly answer the 5500 question. It is well beyond the scope of engagement of most TPA firms to know their clients' internal procedures in a way that the TPA can make a judgement about whether or not deposits were made as soon as feasible. Furthermore, many clients forget this requirement, instead focusing on the 15th business day standard. One user pointed out that even if the TPA tries to communicate this to the client, they are often contradicted by clients' other advisors.

The thread also discussed DOL enforcement activities in this area, where some extreme positions are being taken by the regulators. One PIX user summed up the issue nicely as follows:

> "I think we must identify the issue relative to the more subjective test. Among other things it provides us with an opportunity to point out to clients that we do NOT know their internal procedures and can't really say what "as soon as feasible" is. But since DOL thinks it CAN look and CAN say, and since apparently DOL DOES look and DOES say, the client should approach this whole issue "defensively."

This thread should be reviewed by anyone offering advice to 401(k) sponsors. Download the file kdepos2.fsg.

The late 415(e) and Post-Retirement Medical Benefits

[Thread #90181]

Those of us who are old enough might remember the pre-1984 use of post-retirement medical benefit accounts in small-employer defined benefit plans. These accounts were funded by additional contributions to the plan, subject to an incidental test, and were intended to provide funds for post-retirement medical benefits. The code was amended to include these contributions in the definition of annual additions effective for plan years beginning after March 31, 1984. This change effectively killed the use of these accounts for small employers, as the defined benefit plan fraction was usually 1.0, precluding any annual additions.

With the expiration of 415(e), this thread explores the use of post-retirement medical account again. This would increase plan contributions and provide for distribution of benefits as "accident and health coverage" by a employer plan to retirees, which is not taxed as income to the retiree. The thread also discusses whether or not such accounts could be used to fund the purchase of a qualified long-term care contract. Since Section 7702B(a)(3) provides that qualified long-term

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PIX Digest

care contracts are treated as an accident or health plan, this could work.

To read the entire thread, download the file newprmb2.fsg.

What is the Minimum "Minimum Required Distribution?"

[Thread #90040]

This thread started with a question from a user regarding an Individual Retirement Account. The account holder had died after age 70 1/2 and had previously been taking minimum distributions based on a single life expectancy with recalculation. The user asked what options the beneficiary might have as to the continued payout of the IRA.

The initial responses pointed out that since the life expectancy was being recalculated, upon death the life expectancy goes to zero, so the account would have to be fully distributed by the end of the following year.

Another user pointed out IRS Private Letter rulings 199951053 and 200018057. These rulings held that a beneficiary could continue the distributions based on the beneficiary's life expectancy, assuming the beneficiary was properly designated for purposes of the minimum distribution rules.

This ruling holds that since the code requires a "minimum" required distribution to be made, and since this minimum can be determined with the joint life of a beneficiary, even if the account owner is taking the account on a single-life basis, this does not increase the statutory "minimum" amount required. It just means that the account owner was taking a distribution greater than the minimum required amount.

To read the entire thread, download mindist3.fsg. ▲

2000 Calendar of Events

		ASPA CE Credit
December 6	C-1, C-3, C-4 and A-4 exams	*
December 7	C-2(DC) exam	*
December 7	Atlanta ABC Meeting Cross-testing Workshop: Where do we go from here? Speaker: Cynthia Groszkiewicz, MSPA, QPA	
December 7	Chicago ABC Meeting Cross-Testing Under Proposed Regulations Speaker: Ken Balinski, MSPA	
December 7	Cleveland ABC Meeting Internet Impact on the Industry Speaker: John Consilio	
December 8	C-2(DB) exam	*
December 31	Daily Valuation Exam submission deadline	**

2001 Calendar of Events

February 15	Cleveland ABC Meeting Mergers, Acquisitions, and Spinoffs	
February 20-22	Central, North, and South Florida ABC Meetings 125 Plans Speaker: Robyn Morris	
April 15 - May 30	C-1, C-2(DC), and C-2(DB) exams	*
April 30 - May 1	Great Lakes TEGE Conference (formerly Midstates Benefits Conference), Chicago, IL	16
May 6-9	Business Leadership Conference, Naples, FL	10
July 22-25	ASPA Summer Conference, San Francisco, CA	20
Oct. 15 - Nov. 30	C-1, C-2(DC), and C-2(DB) exams	*
October 28-31	Annual Conference, Washington, D.C.	20

2002 Calendar of Events

October 27-30	Annual Conference, Washington, D.C.	20

* Exam candidates earn 20 hours of ASPA continuing education credit for passing exams, 15 hours of credit for failing an exam with a score of 5 or 6, and no credit for failing with a score lower than 5.

** The Daily Valuation exam earns 10 hours of ASPA continuing education credit for a passing grade.