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WEB's ***Benefits Insider*** is a member exclusive publication providing the latest developments from the Nation's Capital on matters of interest to benefits professionals. The content of this newsletter is being provided as a result of a partnership with the American Benefits Council, a premier benefits advocacy organization, which provides much of its core content.

Articles in this Edition

RECENT REGULATORY ACTIVITY

IRS Provides Sample Roth Amendment
On April 24, the Internal Revenue Service (Service) released Notice 2006-44, Sample Amendment for Roth Elective Deferrals, (Notice) that may be used by plan sponsors wanting to allow employees to elect designated Roth contributions (those made with after-tax dollars but whose qualified distributions, including earnings, are tax-free). The Notice was published in Internal Revenue Bulletin 2006-20 on May 15. The Notice provides that an amendment (either the sample or another individually drafted amendment) must be adopted and signed by the end of the first plan year in which participants are permitted to elect designated Roth deferrals.

The sample amendment contained in the Notice is drafted in a form often used by pre-approved plans (such as master and prototype and volume submitter plans), but the Service indicated it could also be used by individually designed plans. Further, plan sponsors who have adopted master and prototype plans can add the amendment without causing the plan to fail to be a master or prototype plan.

One issue not addressed in the sample amendment is the extent to which an employee can elect to have a distribution (other than a corrective distribution of excess distributions) made from either the designated Roth account or any other account of the employee's under the plan. The Service seems to recommend that the plan sponsor revise the amendment to conform it to the plan's operation in this area. The amendment indicates that highly compensated employees can designate the extent to which an excess distribution is composed of pre-tax deferrals or Roth elective deferrals made during the year (an option not required under the proposed regulations).

The amendment also spells out that the $200 minimum rollover amount will be calculated separately for the Roth elective deferral account, but not the $1,000 amount for purposes of mandatory rollover distributions.

DOL Finalizes Regulations for Abandoned Plans
On April 21, the Department of Labor's (DOL's) Employee Benefits Security Administration (EBSA) released final regulations governing the termination of abandoned or orphaned plans along with an updated class exemption for services provided in connection with the termination. The final regulations were very similar to the proposed regulations, but a few changes were made.

Plan sponsors may have a concern about the ability of qualified termination administrators (QTAs) to find institutions that would set up IRA accounts for small amounts owed to missing participants. For such amounts, the QTA could set up an interest-bearing federally insured bank account in the name of the missing participant or transfer missing participants' account balances to state unclaimed property funds. The final regulations permit this treatment for missing participants with small account balances of $1,000 or less. In addition, the final rule allows for forfeiture of any amount that is less than the costs anticipated in closing out the account.

The final regulations do not reflect suggestions to broaden the definition of QTAs so that others involved in plan administration such as recordkeepers could serve as the QTA.

However, the final regulations clearly indicate that a QTA may engage, on behalf of the plan, any necessary service providers.

DOL Provides Guidance on Allocating Settlement Proceeds

On April 19, the DOL released Field Assistance Bulletin (FAB) 2006-1, which addresses the duties and responsibilities of plans and service providers under the Employee Retirement Income Security Act of 1974 (ERISA) in connection with the distribution and allocation of mutual fund settlement proceeds to retirement plan participants. "Settlement proceeds" generally refer to payments mutual fund companies agree to pay to their investors to settle matters (often without conceding liability) raised by the Securities and Exchange Commission (SEC) and in which the SEC alleges the funds' conducts violates various securities laws (e.g., late trading and market timing).

The FAB includes an extensive discussion of the fiduciary issues that arise in connection with mutual fund settlement proceeds and reaches the following conclusions:

- Independent Distribution Consultants (IDCs) are appointed by the SEC and are responsible for developing a plan for distributing settlement proceeds (a "distribution plan"). The FAB indicates that IDCs are generally not ERISA fiduciaries;
- Mutual fund settlement proceeds will be considered plan assets once distributed from the settlement fund. As a result, an intermediary that receives settlement proceeds on behalf of employee benefit plan clients will generally be considered a plan fiduciary (even if the intermediary is not otherwise a plan fiduciary);
- Intermediaries will be required to hold settlement fund proceeds attributable to employee benefit plan clients in trust and manage the proceeds in accordance with ERISA's fiduciary responsibility rules pending distribution of the proceeds to clients;
- If the distribution plan does not specify a method for distributing the settlement proceeds among omnibus account clients, then the intermediary will have to develop a method of distribution. This method will be subject to ERISA fiduciary responsibilities and will generally require allocating the proceeds among clients in relation to how the late trading and market timing activities may have affected the individual clients. DOL notes that if it is cost effective to do so, an intermediary can allocate the settlement proceeds among clients in an omnibus account according to the average share or dollar balance of the clients' investments in the mutual fund during the relevant period; and
- If the distribution plan provides a specific methodology for allocating proceeds among participants (on either a mandatory or elective basis), DOL will view the plan fiduciary's application of this methodology as satisfying the requirements of ERISA. If the distribution plan does not contain a method for allocating the proceeds among participants, then the fiduciary should select a method for allocating the proceeds, which is in relation to the impact the market timing and late trading activities may have had on the particular account. The plan fiduciary would also have to weigh the costs to the plan or participant accounts and ultimate benefit to the plan or participants when trying to determine the impact of the trading activities on the individual participant accounts. The FAB suggests that it may be permissible to allocate the proceeds to current participants (rather than participants who may have been in the plan at the time of the alleged activity) in some circumstances.

Portman Tapped to Lead Office of Management and Budget
President Bush has nominated former Ohio Representative and U.S. Trade Representative Rob Portman as the director of the White House's Office of Management and Budget (OMB), replacing Josh Bolten, who has assumed the position of Bush's chief of staff. In Portman's 12 years as a congressman, he authored a series of bipartisan pension reform proposals, most notably included in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). His work with Congressman Ben Cardin (D-MD) on these issues set the standard for developing sound bipartisan retirement policy. In his tenure as trade representative, Portman won praise for brokering passage of the Central American Free Trade Agreement (CAFTA) with six Latin American nations.

In his new role, Portman will oversee the composition of the President's annual budget. In recent years, the President has used his budget proposal to introduce proposals for new retirement savings vehicles such as Employer Retirement Savings Accounts (ERSAs), Retirement Savings Accounts (RSAs) and Lifetime Savings Accounts (LSAs), as well as Health Savings Accounts (HSAs). The Director of OMB is a cabinet position and requires Senate confirmation.

DOL Updates Voluntary Fiduciary Correction Program
On April 18, the DOL updated its Voluntary Fiduciary Correction Program (VFCP) program that helps employers and their professional advisors voluntarily correct violations of fiduciary law for employee benefit plans under ERISA. The new standards were effective 30 days after publication in the April 19 Federal Register. This update incorporates several changes, including expansion and simplification of eligible transactions and streamlined documentation and clarified eligibility requirements.

FASB Releases Exposure Draft on Pension and Other Postretirement Obligations
On March 31, the Financial Accounting Standards Board (FASB) issued a draft of proposed rules requiring employers to recognize the overfunding or underfunding of their defined benefit pension plans and other post-employment benefits such as a retiree health plan. The proposal would require that plan assets and liabilities be measured as of the date of the financial statements. For a pension plan, the obligation would be the projected benefit obligation and for other post-retirement benefit plans (like retiree health) the benefit would be the accumulated post-retirement benefit obligation.

Current accounting standards allow employers to report the funded status of the pension plan in the notes to the company's financial statements. For public companies, the new reporting requirement would be effective for fiscal years beginning after December 15, 2006, and for non-public companies it is effective for fiscal years after December 15, 2007. The proposed rules are the first step in a process to reconsider existing accounting rules; FASB has indicated that the second phase will be more comprehensive, and analysts suggest that FASB will likely attempt to introduce more of a "mark-to-market" approach to pension accounting, potentially causing more volatility in the financial reporting of companies that sponsor defined benefit plans.

RECENT LEGISLATIVE ACTIVITY

Pension Reform Legislation Conference Update
The congressional conference for retirement savings legislation – charged with resolving the differences between the House of Representatives-passed Pension Protection Act (H.R. 2830) and the Senate-passed Pension Security and Transparency Act (S. 1783) –

has passed the two-month mark, and progress remained slow at the end of April. Lawmakers were pushing for a final bill by Memorial Day (May 29), but that deadline appears unlikely.

With respect to the retirement savings legislation, many plan sponsors continue to lobby vigorously for a final bill that will foster continued employer sponsorship of health and retirement savings programs, including making recommendations for improving the funding provisions of the bills, while also advocating support for issues such as EGTRRA permanence, hybrid plan clarification and several health plan related provisions.

Senate conferees recently offered a formal compromise to their colleagues in the House of Representatives, but House conferees have indicated that they will not accept it. The proposal reportedly included:

- Liabilities and asset values will be smoothed/averaged over 15 months instead of 12 months;
- Acceptance of additional limits on credit balances by underfunded plans;
- Nonqualified deferred compensation limits would be enforced for a company's top five executives and managers subject to certain security law restrictions;
- Adoption of the House bill's 100 percent funding target for currently underfunded plans;
- Increased the deductible limit to 175 percent of current liability over the value of the assets (The Senate bill currently uses 180 percent); and
- Adoption of House bill's required notification to participants related to a 4010 filing.

On April 6, the House approved a Motion to Instruct the Conferees (Motion), proposed by Representatives George Miller (D-CA) and Nancy Pelosi (D-CA), that directed pension bill conferees to accept the Senate bill’s (S. 1783) provisions on hybrid pension plans. The Senate provisions were prospective only and proposed onerous new mandates. Despite extensive communications from numerous sources, the Motion passed the House by a vote of 248-178, with 51 Republicans voting in favor. The Motion was non-binding and the House conferees are not required to follow it.

Recent face-to-face meetings with Representatives Robert Andrews (D-NJ) and Donald Payne (D-NJ) furthered efforts to advocate on many aspects of the retirement legislation including retirement and health provisions. During this meeting, several companies made recommendations for improving the funding provisions of the bills, while also advocating support for issues such as EGTRRA permanence, hybrid plan clarification, investment advice and several health plan related provisions.

Meanwhile, efforts continue to achieve passage of the EGTRRA permanence provisions of the legislation. A campaign of "Retirement Savings Permanence Bulletins," a series of fact sheets on the EGTRRA provisions' simplification measures for plan sponsors was circulated to Hill offices including:

- Retirement Savings Permanence Bulletin No. 1: Simplification for Plan Administration
- Retirement Savings Permanence Bulletin No. 2: Increased Limits
- Retirement Savings Permanence Bulletin No. 3: Matching Contribution Vesting

Defined Benefits Pension Plan Funding Reform: A series of "Pension Pointers," developed jointly by various business organizations, was sent to the full House and Senate to educate lawmakers and their staffs on the basics of pension funding reform:

- PENSION POINTERS No. 1: Funding Rules
- PENSION POINTERS No. 2: Credit Rating
- PENSION POINTERS No. 3: Calculation of At-Risk Liability
- PENSION POINTERS No. 4: Myths and Facts Regarding Press Coverage of Pension Reform

Also, a "dear colleague" letter from Senators Carl Levin (D-MI) and George Voinovich (R-OH) regarding pension funding reform garnered support from 33 of their fellow Senators. The "dear colleague" letter requests adequate transition time for companies to conform to new funding rules.

Hybrid Plan Provisions: The differences in the hybrid plan provisions of the two bills remain particularly controversial. On March 27, Senators Kit Bond (R-MO) and Jim Talent (R-MO) sent a letter to conferees urging them to confirm the legality of existing and future hybrid pension plans. On March 31, Senator Richard Burr (R-NC), along with Senators Elizabeth Dole (R-NC), Jim DeMint (R-SC) and Wayne Allard (R-CO), sent a similar letter to conferees.

Health Plan Provisions: Discussions with conferees on the health plan provisions of the pension bill are also on-going. Additionally, letters have been sent to conferees urging support for the provisions clarifying subrogation rights under ERISA – the ability of an insurer to recover funds from liable third-parties – and allowing participants to carry forward up to $500 for use in their FSA the following year or to roll over these amounts into a health savings account (HSA).

In related news, on March 27 the Government Accountability Office (GAO) released a report entitled Private Pensions: Opportunities Exist to Further Improve the Transparency of PBGC's Financial Disclosures. The report finds that while PBGC has recently taken steps to include more information about its methodology for determining probable claims in its annual reports and make more detailed information on its financial condition available on its Web site, there are still concerns about the lack of transparency regarding the methodology PBGC uses to determine the interest rate used to calculate its liabilities.

HSA Working Group Hosts Briefing by Employers on Capitol Hill
A panel of small, medium and large employers discussed their experiences offering HSAs to their employees at a briefing held in April for congressional staff. The briefing was sponsored by the HSA Working Group, a broad coalition composed of companies and trade associations representing employers, health plans, financial institutions and others supporting HSAs and other forms of consumer-directed health benefits. The briefing was organized by members of the Working Group's steering committee as part of a continuing series of forums aimed at informing congressional staff about recent marketplace developments on HSAs.

Representatives on the briefing panel came from Wendy's International, Inc., whose health benefit plan covers 20,000 lives; Lutheran Social Services, an Ohio-based nonprofit organization with 2,100 employees; and All-Flow Plumbing, a family-owned business located in Michigan with eight full-time employees. All the companies had at least one year of experience offering employees HSAs with compatible high deductible health plans (HDHPs) on a full-replacement basis.

The panelists cited recent double-digit increases in insurance premiums or health care claims costs as a key factor in their decisions to offer HSAs and lower-premium HDHPs to their employees. A desire to engage employees more directly in health care spending decisions also motivated their decisions.

All of the companies contributed to the HSAs of their eligible employees. Panelists also reported that employee contributions to HSAs were generally high and many had year-end balances. However, panelists also called for changes to HSA rules to (1) allow employers to contribute more to their lower-paid workers as opposed to higher-paid workers, (2) allow both employer and employee contributions to exceed the amount of the deductible for the HDHP, and (3) permit more flexibility in covering prescription drugs outside of the high deductible. These proposals are also included among the recommended improvements to HSAs supported by the HSA Working Group. The HSA Working Group's policy agenda is intended to encourage more employers to offer HSAs and encourage more employees to elect these new plan designs when available to them in the workplace.

RECENT JUDICIAL ACTIVITY

Richards v. FleetBoston Cash Balance Ruling Finds Hybrid Plans Illegal
On March 31, the U.S. District Court for the District of Connecticut rejected a motion by FleetBoston to dismiss the age discrimination suit brought by a former employee against the sponsor of a cash balance pension plan. In the case of Richards v. FleetBoston, U.S. District Judge Janet Hall did not directly render judgment against the plan but clearly adhered to the analysis that all cash balance plans are inherently age discriminatory, as suggested by the Cooper v. IBM case (which is currently pending in the Seventh Circuit Court of Appeals).

In July 2003, the U.S. District Court for the Southern District of Illinois ruled in favor of the plaintiffs in Cooper, et al v. IBM, contrary to the legislative history of ERISA, U.S. Treasury Department regulations and several other federal court cases. The American Benefits Council and the ERISA Industry Committee recently filed an amicus (friend of the court) brief with the Seventh Circuit Court of Appeals. Oral arguments were made by the parties on February 16, 2006.

The *FleetBoston* ruling underscores the need to actively weigh in with conferees to the pending pension legislation on the distinctions between the design and conversion issues and the practical consequences of court decisions that require employers to make up for the "time value of money" by contributing excessive amounts on behalf of older workers in order to make rational contributions for younger workers.