

MEMO# 10720

February 11, 1999

DEMOCRATIC LEADERSHIP FILES COMPREHENSIVE PENSION REFORM BILL; ADMINISTRATION BUDGET INCLUDES PENSION REFORM PROPOSALS

1 Co-sponsors include Senators Rockefeller (D-WV), Breaux (D-LA), Feinstein (D-CA), Murray (D-WA), Boxer (D-CA), Durbin (D-IL), Wellstone (D-MN), Kerry (D-MA), Moynihan (D-NY) and Lautenberg (D-NJ). 2 [10720] February 11, 1999 TO: PENSION COMMITTEE No. 8-99 RE: DEMOCRATIC LEADERSHIP FILES COMPREHENSIVE PENSION REFORM BILL; ADMINISTRATION BUDGET INCLUDES PENSION REFORM PROPOSALS

Senator
Daschle (D-SD) and co-sponsors¹ have filed S. 8, titled the "Income Security Enhancement Act of 1999," a bill that includes numerous pension reform proposals described below. Many of these provisions have appeared previously in bills filed last year. In addition to pension provisions, the bill also would prohibit any changes to the "pay-as-you-go" budgetary rules until Congress "saves Social Security first," increase the federal minimum wage, repeal the marriage tax penalty and address remedies for wage discrimination on the basis of sex. Additionally, the Clinton Administration has released its fiscal-year 2000 budget proposal, which includes a series of provisions relating to retirement security, private pension plan coverage, many of which appear in S. 8. A "fact sheet" released by the Administration, which described the pension items in the budget package, and a copy of S. 8 are attached. S. 8 – Income Security Enhancement Act of 1999 I. Proposals Regarding Pension Access and Coverage 1. Small Employer Startup Tax Credit. Small employers would be permitted to obtain a tax credit for up to 50 percent of startup costs incurred when establishing a retirement plan. The credit would be available in amounts up to \$1,000 for the first year in which the credit is claimed and up to \$500 in each of the following two years for expenses related to plan establishment and administration and retirement education. Section 411 of the bill. 2. Exclusion for Payroll Deduction IRA Contributions. Employers would be able to establish a "qualified payroll deduction arrangement" under Code section 408 pursuant to which employees may elect to have the employer make payments up to \$2,000 to a traditional IRA (offset against amounts an individual makes to an IRA outside of this arrangement) on their behalf rather than receive cash compensation. The employer would be required to deposit the elective employer contributions to the IRAs no later than 30 days after the last day of the month with respect to which contributions are withheld from 3employee pay. Additionally, an employer would be permitted to establish a qualified payroll deduction arrangement and make contributions on behalf of

employees without obtaining an election from them, in which case the employer contributions would be tax deductible under Code section 404. Section 412 of the bill. 3. Nonrefundable Tax Credit For IRA Contributions. Individuals whose adjusted gross income is less than \$30,000 would be eligible to receive an annual tax credit of up to \$450 for contributions to a traditional IRA in lieu of taking a deduction for the contribution. Section 413 of the bill. 4. New Exception to Section 72)(t) Penalty. The bill would permit early distributions from IRAs, 401(k) plans and 403(b) arrangements to be used without penalty during periods of unemployment. Section 414 of the bill. 5. Simplified Small Employer Defined Benefit Plan. The bill would establish a simplified defined benefit plan program for small employers, called the "Secure Money Annuity or Retirement (SMART) Trust." Section 415 of the bill. 6. Revision of SIMPLE Plan and 401(k) Safe Harbor Contribution Formulas. The bill would change the SIMPLE plan contribution formulas. First, the matching formula would be increased, requiring employers to match 100% of the first 3% of compensation an employee elects to contribute to the plan and 50% of additional amounts the employee elects to contribute to the extent the amount exceeds 3% of compensation, but does not exceed 5%. The employer also would be required to make a nonelective contribution of 1% of compensation for all employees eligible to participate in the plan. Second, the nonelective contribution formula would be increased from 2% to 3% of compensation. Third, employers would be permitted to make additional nonelective contributions to the plan for all employees (in excess of the proposed requirements) up to 5% of compensation. Section 421 of the bill. The bill similarly would revise 401(k) plan safe harbor formulas. Section 422 of the bill. 7. Amendment of HCE Definition. The bill would amend Code section 414(q)(1)(B) by eliminating the top-paid group election available to employers. Section 423 of the bill. 8. Exemption of Mirror Plans From Section 457 Limits. The bill would amend Code section 457(e) so that amounts of compensation deferred under a "mirror plan" would not be taken into account in applying section 457. A mirror plan is defined as a plan, program or arrangement maintained solely for the purpose of providing benefits in excess of the limitations imposed by Code section 401(a)(17) or 415. Section 425 of the bill. II. Proposals Regarding Benefit Security and Enforcement 1. Periodic Benefit Statement Requirement. ERISA section 105 would be amended to require that participants in defined contribution plans be provided annually a statement of their benefits under the plan. With respect to defined benefit plans, such statements would be required to be furnished at least once every 3 years to participants who have attained age 35. Defined benefit plan statements could be based on "reasonable estimates" pursuant to regulations to be prescribed by the Department of Labor. Section 431 of the bill. 2. Annual 401(k) Plan Investment Report. Plan administrators of 401(k) plans covering less than 100 participants would be required to furnish within 60 days after the end of a plan year to each participant and beneficiary an annual investment report detailing information prescribed by the Department of Labor in regulations. In developing regulations, the Department is directed to consider requiring that the report identify (i) total plan assets and liabilities; (ii) transactions between the plan, employer, any fiduciary, or any 10-percent owner; and (iii) noncash contributions to or purchases of nonpublicly traded securities made by the plan during the plan year. Plan administrators would not be required to provide this report to participants described in section 404(c). Section 432 of the bill. 3. Information Provided to 401(k) Plan Investment Managers. The administrator of a 401(k) plan would be required to provide to the plan's investment managers information sufficient to enable them to separately account at any time for benefits accrued with respect to each plan participant and beneficiary. Section 433 of the bill. 4. Prohibition of Credit Card Loans. The bill would prohibit the provision of plan loans to participants via credit card. Section 434 of the bill. 5. Reporting of Irregularities With Respect To Plans. Section 442 of the bill would require plan administrators to report evidence of any "irregularity" that may have occurred to the Department of Labor and to

the plan's accountant within 5 business days of the discovery. Similarly, an accountant auditing a plan would be required to notify the plan administrator in writing if he has determined there is an irregularity with respect to the plan. If the accountant believes the irregularity involves the plan administrator, the accountant would be required to notify the Department of Labor. Irregularities would include theft, embezzlement, extortion, bribery, kickbacks involving at least \$1,000 and other crimes enumerated in the bill.

6. New Requirements for Qualified Public Accountants. Section 443 of the bill would require an accountant engaged to audit a retirement plan have (1) an "appropriate internal quality control system" (to be defined in Department of Labor regulations), (2) undergone a qualified external quality review of relevant accounting and auditing practices during the 3-year period preceding the engagement, and (3) completed within the 2 years preceding the engagement continuing education courses.

III. Portability

1. Faster Vesting of Employer Matches. Employer matching contributions (as defined in Code section 401(m)) would be vested on a 3-year cliff or 2-to-6 year graded vesting schedule. Section 451 of the bill.

2. Revision of Same Desk Rule. The bill would amend Code section 401(k)(2)(B)(i) by permitting distributions upon "severance from employment," rather than "separation from service" and by deleting the "business sale requirement." Section 452 of the bill.

3. Relief From Anticutback Rule for Transfers Between Defined Contribution Plans. Code section 411(d)(6) would be amended to enable plan transfers between defined contribution plans even where the same distribution options are not available under the transferee plan. Section 453 of the bill.

4. Expansion of Missing Participants Program. The Pension Benefit Guaranty Corporation's missing participant's program for terminating defined benefit plans would be expanded to include multiemployer plans. Defined contribution plan sponsors would be able to participate in the program on a voluntary basis. Section 454 of the bill.

5. Rollovers To and From 403(b), 457, 401(k)s and IRAs. The bill would permit rollovers between and among 401(k), 403(b), 457 plans and IRAs. Sections 455 and 456 of the bill.

IV. Comprehensive Women's Pension Protection

1. Spousal Right To Know Proposal. Code section 417(a) minimum survivor annuity requirements would be amended to require a plan to provide a copy of the written explanation of the right to a qualified joint and survivor annuity (QJSA) and a qualified preretirement survivor annuity (QPSA) form of benefit to a participant's spouse by mailing to the last known address of the spouse. The requirement could be satisfied by a single mailing addressed to both the participant and spouse. Section 461 of the bill.

2. Inclusion of FMLA Leave In Hours of Service Calculation. The bill would require that leave taken under the Family and Medical Leave Act be counted toward plan participation and vesting. Section 464 of the bill.

3. Repeal of Integration Rules. Section 465 of the bill would (1) apply nondiscrimination rules to integrated plan benefits attributable to pre-1989 plan years; (2) disallow application of integration rules to SEPs; and (3) completely repeal integration rules effective for plan years beginning on or after January 1, 2005.

4. Revision of QDRO Rules. Section 466 of the bill would create a specified division of pension assets that would apply in cases where a domestic relations order (with respect to the dissolution of a marriage of at least 5 years duration) does not specifically provide that the parties considered pension benefits in the division of property. In such cases the former spouse would be entitled to claim 50% of the accrued benefit. Additionally, the bill would require plan participants to notify the plan administrator of their divorce within 60 days after the divorce and to provide the plan administrator with a copy of the order and the last known address of the former spouse. The plan administrator, in turn, would be required to notify the former spouse of the right to claim a benefit under the plan.

V. Modification of Joint and Survivor Annuity Requirements

1. Modification of QJSA Benefit. The bill would modify ERISA section 205(a)(1) and Code sections 401(a)(11) and 417 to require that plans subject to the qualified joint and survivor annuity requirement offer an annuity in the form of a "qualified joint and 2/3 survivor annuity" under which the survivor annuity for the life of

the surviving spouse is equal to at least 2/3 the amount of the annuity which is payable during the joint lives of the participant and spouse. The bill also would add an "illustration requirement" pursuant to which the terms and conditions of all joint and survivor annuity forms of benefit offered in a plan would be explained and accompanied by an illustration of the benefits for the particular participant and spouse. The participant and spouse would be required to sign an acknowledgement form indicating that they have read and considered the illustration before choosing any form of benefit under the plan. Section 475 of the bill.

2. Spousal Consent And Annuity Requirement for Defined Contribution Plan Distributions. The bill would make Code sections 401(a)(11) and 417 applicable to defined contribution plans, except in the case of hardship distributions from 401(k) plans. Additionally, defined contribution plans would be permitted to distribute up to 50% of an account balance without spousal consent if the present value of the qualified joint and survivor annuity does not exceed \$10,000. Section 476 of the bill.

Clinton Administration Budget Proposals As described in the attachment, among the President's budget proposals related to pensions include proposals that would (1) facilitate the rollover of assets between and among 401(k), 403(b) and 457 plans and permit the rollover of after-tax dollars to plans and IRAs if the receiving plan administrator or IRA provider separately track and report these amounts; (2) encourage payroll deduction IRAs by excluding from taxable income employee contributions of up to \$2,000 made to an IRA through payroll deduction; (3) provide a small business retirement plan startup tax credit; (4) create a simplified small employer defined benefit plan; (5) provide for faster vesting of 401(k) plan matching contributions; (6) require spouses to be provided notice and explanation of their right to receive a joint and survivor annuity form of distribution; (7) increase the Code section 3405 elective withholding rate for non-periodic distributions (e.g., lump-sum distributions) from deferred compensation plans 10 percent to 15 percent; and (8) increase the excise tax on excess IRA contributions from 6 percent to 10 percent. Finally, the budget proposal indicates the Administration's intent to introduce legislation to improve the audits of private pension plans; at this time, it is unclear whether the Administration will again propose to repeal the limited scope audit, or will take a different approach to addressing these issues than in recent, prior years.

Russell G. Galer Senior Counsel Attachments