The Asset Management Industry
SERVING INDIVIDUAL INVESTORS

INVESTMENT COMPANY INSTITUTE

MEMO# 3550

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PENSION PROVISIONS OF H.R. 4210, THE TAX FAIRNESS AND ECONOMIC GROWTH ACT OF 1992

- 1 - February 27, 1992 TO: PENSION MEMBERS NO. 3-92 RE: PENSION PROVISIONS OF H.R. 4210, THE TAX FAIRNESS AND ECONOMIC GROWTH ACT OF 1992 ____ H.R. 4210, The Tax Fairness and Economic Growth Act of 1992, approved today by the House of Representatives, contains several pension provisions of interest to investment companies. Relevant portions of the bill and the accompanying Technical Explanation are attached. Penalty-Free Withdrawals from IRAs (Attachment A) Under the bill, first-time homebuyers would be allowed to withdraw up to $10,000 from an IRA without paying the 10 percent early withdrawal penalty if the funds are used within 60 days of the withdrawal to purchase or construct a home. A first-time homebuyer would be any person (and, if married, his or her spouse) who had not owned a home in the last three years and was not in an extended period for rolling over gain from the sale of a principal residence. The bill also would allow the penalty- free withdrawal by a parent on behalf of a child if the child (and the child's spouse) were first-time homebuyers. The waiver would not apply to an inherited IRA or amounts rolled over from qualified plans. The bill also provides for penalty-free withdrawals for qualified educational expenses (post-secondary education) of a taxpayer and his or her spouse and children. As with first-time homebuyers, the waiver is unavailable for withdrawals from an inherited IRA or with respect to rolled over distributions from qualified plans. Finally, the bill would extend to IRAs the exemption from the 10 percent penalty currently available for distributions from qualified plans for medical expenses and expand the persons for whose benefit the withdrawal could be made to children, grandchildren and ancestors of the taxpayer. Rollovers (Attachment B) - 2 - The bill would expand the circumstances in which a distribution could be rolled over tax free to an IRA or another qualified plan. Any distribution to an employee or the surviving spouse of an employee (other than a minimum required distribution), could be rolled over into an individual retirement account (IRA) or a qualified plan or annuity unless the distribution is one of a series of substantially equal payments made (1) over the life or life expectancy of the participant or the joint life or life expectancies of the participant and his or her beneficiary or (2) over a period of ten or more years. Employee contributions, as under current law, could not be rolled over. In addition, the bill would require plans to permit participants to elect to have any rollover distribution transferred directly to a qualified defined contribution plan or annuity (but not to a defined benefit plan) if the transferee plan accepts such contributions. Master and Prototype Plans (Attachment C) Under the bill, the Internal Revenue Service (IRS) would be authorized to prescribe regulations defining the responsibilities of master and prototype plan sponsors. These responsibilities would include maintenance of current lists of adopting employers and the provision of certain (unspecified) annual notices to adopting employers and the IRS. The Technical Explanation to the bill also states that sponsors will be required to (1) notify adopting employers that the failure to adequately support the plan with administrative services risks plan disqualification and (2) furnish employers with the names of firms that are familiar with the prototype plan and can provide professional administrative services. The Technical Explanation notes that these requirements are not intended to create fiduciary relationships under Title I of ERISA that would not exist in the absence to the requirement. Nondiscrimination Rules for 401(k) Plans (Attachment D) The bill would modify the nondiscrimination test applicable to elective deferrals and employer matching to base the permitted average deferral percentage for highly compensated employees in the current year on the actual average deferral percentage for nonhighly compensated employees for the prior year. SARSEPs (Attachment E) The bill also would extend salary reduction simplified employee pensions or "SARSEPs" to employers with 100 or fewer employees and eliminate the antidiscrimination rules in favor of design-based safe harbors. To be qualified, the SEP would need to meet the following requirements. First, the employer must contribute 1 percent of each employee's compensation, up to - 3 - $100,000, for the year. Second, each employee must be allowed to make elective deferrals of up to $3,000 annually. Finally, the employer must match all employee contributions at a 100 percent rate on the first 3 percent of compensation and at a 50 percent rate on the next 2 percent of compensation. We will keep you informed of further developments. David J. Mangefrida Jr. Assistant Counsel - Tax Attachments

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