

## Benefits Advisory and Compliance

### Bulletin

October 2010

Passage of the Small Business Jobs and Credit Act, which permits in-plan Roth conversions, was a major development in September. In other news, pending legislation requiring automatic IRAs could affect employers that exclude certain employees from participating in a company's 401(k) plan. In regulatory developments, recent comments from Treasury officials indicate the deadline to amend cash balance plans for the Pension Protection Act (PPA) may be extended. Finally, the President's Economic Recovery Advisory Board (PERAB) report suggests how to simplify qualified retirement plan rules.

### Legislative Developments

#### In-Plan Roth Conversions Now Effective

As part of the recently enacted Small Business Jobs and Credit Act of 2010, sponsors of 401(k), 403(b) and government 457(b) plans may allow participants to directly roll over their account balance to a Roth account within the plan. As reported in the August *BAC Bulletin*

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in-plan conversions are only available for amounts that are otherwise distributable from the plan (e.g., elective deferrals for participants age 59½ or older, or, if provided by the plan document, employer contributions subject to the two-year holding/five-year participation rule).

**Insight:** The legislative history of the bill states that plans may limit new in-service distribution options (e.g., plans that decide to allow withdrawal of employer contributions subject to the two-year holding/five-year participation rule) to plan participants who roll over their account balance directly into a designated Roth account. While this provision would meet the intended goal of the legislation (i.e., preventing plan leakage), specific language permitting such a condition on these rollovers is not included in the Small Business Jobs and Credit Act of 2010. Moreover, Treasury officials have informally suggested that these restrictions would violate the direct rollover rule (which generally does not seem to allow plans to restrict a participant's ability to roll over eligible distributions to any eligible retirement plan). This change is effective immediately for 401(k) and 403(b) plans, and in 2011 for governmental 457(b) plans.

The timing of enactment complicates decision making for plan sponsors. The special income inclusion rule and the uncertainty surrounding extension of the 2001 and 2003 tax cuts may create

pressure for plan sponsors to allow conversions this year. However, meeting this deadline may be difficult, because vendors have different time frames for providing administrative and communication support. In addition, although implementing conversions in 2010 may be optimal for some plan participants, waiting until 2011 or later might also be beneficial, depending on a participant's personal tax situation.

A copy of the Act can be found [here](#).

## **Automatic IRA Bill Could Affect Employers With Qualified Plans**

The Automatic IRA Act (introduced in the Senate and House by Senator Jeff Bingaman [D-NM] and Representative Richard Neal [D-MA], respectively) would require employers that do not offer a qualified retirement plan to automatically enroll workers in IRAs. While employers that offer a qualified retirement plan would generally be exempt from the automatic IRA requirement in both Senate and House bills, there are some differences between the two:

- Under the Senate bill, employers would be required to provide an automatic IRA to employees in a subsidiary, division or major business unit who are not covered by a qualified retirement plan.
- Under the House bill, employers would only be required to offer automatic IRAs if the subsidiary, division or major business unit has at least 50 employees constituting at least 10% of the employer's total workforce.

**Insight:** Under both Senate and House bills, the default contribution would be 3% of compensation, and employees could increase or decrease their contributions, or opt out of the program. The Departments of Treasury and Labor would develop the specific vehicles. Other important differences between the two bills include:

- Whether employees would be defaulted into a Roth or traditional IRA in the absence of an affirmative election
- The default investment options available for automatic IRAs
- The requirements that must be satisfied by automatic IRA providers (i.e., the degree of regulation), among other issues

A copy of the Senate bill can be found [here](#) and the House bill [here](#).

## Regulatory Developments

### Cash Balance Plan PPA Deadline Is Likely to Be Extended

Treasury officials have informally indicated that the plan year-end 2010 deadline to amend a hybrid pension plan to incorporate the requirements of the PPA is likely to be extended.

**Insight:** This extension will likely be coordinated with the release of new final and proposed regulations regarding hybrid plans. The guidance is expected to be released no later than January, and there are indications that it may be out as soon as this week. As a result, plan sponsors will have a reasonable period of time to analyze the new guidance and decide how best to react before they need to amend their plans.

## Publications

### PERAB Report

The PERAB was established in 2009 to discuss the advantages and drawbacks of options to simplify the tax code, increase tax compliance and reform corporate taxes. The PERAB's recently released report contains several proposals aimed at simplifying retirement saving programs, including:

- Harmonizing the eligibility, contribution and withdrawal rules to create greater consistency among 401(k), 403(b) and 457 plans, or consolidating employer-sponsored retirement plans into a 401(k)-like plan that would be available to all employers (i.e., for-profit, not-for-profit and governmental entities)
- Expanding automatic enrollment and improving the saver's tax credit by converting it to a matching contribution and simplifying the eligibility thresholds
- Reducing retirement account leakage by prohibiting the cash-out of small account balances (employers would either have to keep the accounts or roll them over to an IRA or another employer-sponsored plan) and limiting tax-free and penalty-free distributions
- Simplifying the rules for plan sponsors by simplifying nondiscrimination testing or repealing the nondiscrimination rules, and requiring all plans to meet a safe-harbor limit (including a minimum contribution requirement for medium and large employer plans)
- Eliminating minimum required distributions for individuals with account assets below a certain threshold

**Insight:** Although some of the proposals in the PERAB report have received legislative attention or discussion, it seems unlikely that they will receive legislative attention this year. Instead, they may serve as a reference for future retirement or tax reform discussions. For example, Senator Max Baucus (D-MO) listed tax reform as an area for possible legislative action and began setting the stage for a tax reform debate in a September 23 hearing entitled "Tax Reform: Lessons From the Tax Reform Act of 1986."

A copy of the report can be found [here](#).

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