



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

Highlights

1. Administration's Defined Benefit Pension Plan Reform Proposal
2. HIPAA Regulations
3. Automatic Rollover Rules are Coming
4. PBGC Proposal Mandates Electronic Filing of Actuarial and Financial Information by Troubled Control Groups
5. Veterans Benefits Improvement Act of 2004
6. Advisory Opinion Holds that an Insurer's or Banker's Incentive Cash Contribution to an Individual's New HSA is not a Prohibited Transaction
7. IRS PLR Holds that a Rollover Maneuver by a 5% Owner Defers Required Minimum Distributions

Administration's Defined Benefit Pension Plan Reform Proposal

Secretary of Labor Chao introduced the Administration's Defined Benefit Reform Proposal. Secretary Chao stated that the administration's proposal has three prongs:

1. Reforming the funding rules for private defined benefit plans to ensure that employers fully fund their retirement promises. This proposal includes:
 - a. Replacing multiple measures of pension liabilities with one measure that is adjusted to reflect the plan's risk of termination.
 - b. One basic method of calculating the minimum required and maximum allowable contributions rather than the current multiple approaches.
 - c. Plan funding targets that are based on the plan sponsor's financial health.
 - d. Measurement of pension liabilities using a current duration-matched yield curve of corporate bond rates.
 - e. Shortening of the period in which plan sponsors can make up funding shortfalls, e.g. seven years.
 - f. Prohibiting employers from promising additional benefits or pay for them immediately, if the plan sponsor is financially weak or the pension plan is significantly underfunded.
 - g. Permitting plan sponsors to make additional deductible contributions during good economic times.



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

2. Changing the pension premium structure. The current structure does not reflect the true risk of a plan terminating with insufficient assets to pay benefits and can be manipulated to avoid payment of risk-based premiums.
 - a. Flat rate premiums. The flat rate premium would be adjusted to reflect the growth in worker wages since 1991 when the current rate of \$19 was set. The index-adjusted rate would be \$30 and the premium rate would be indexed to reflect the growth of wages in the future.
 - b. Risk-based premiums. Risk-based premiums would be based on plan underfunding relative to the appropriate funding target. Also, the proposal contains a provision permitting the PBGC board to adjust the risk-based premium periodically so that premium revenue is sufficient to cover expected losses and to improve PBGC's financial condition. All underfunded plans would pay risk-based premiums under the proposal.

3. Increasing the disclosure of information about private defined benefit pension plans to workers, investors and regulators to ensure greater transparency and accountability. Part of the proposal would require a plan sponsor to reveal the plan's funding status earlier in the year than currently along with the plan's funded status in recent years.

HIPAA Regulations

IRS, DOL, and the Department of Health and Human Services (HHS) have issued final regulations under HIPAA that essentially follow the interim regulations on portability that were issued in 1997. At the same time, the agencies issued proposed regulations that, among other things, further refine the 63-day break-in-coverage and special enrollment rules to provide the tolling of the period in certain circumstances when a proper HIPAA notice has not been given. Other items included in the preambles to the final and proposed rules include updated model certificates of group health plan coverage that can be used by health plans and health insurance providers to satisfy HIPAA's coverage information requirement.

The final HIPAA regulations accomplish the following:

- Requires group health plans and group health insurance issuers to include, concurrently with the certificate of creditable coverage provided to individuals when they lose coverage under the plan, an educational statement on their HIPAA rights.
- Includes model language that group health plans and group health insurance issuers can use for the new educational statement.



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

- Recognizes health plans maintained by foreign governments, and by the U.S. government, e.g., Veterans Administration coverage, as creditable coverage that can be used to reduce the length of or eliminate preexisting condition exclusion.
- Offers sample language that plans and issuers can use to satisfy their obligations to provide participants notices of preexisting condition exclusions.
- Clarifies that certain plan benefit restrictions are in fact preexisting condition exclusions that must comply with HIPAA's limitations on such exclusions.

The corresponding proposed regulations contain the following changes:

- Provides an extension of time for individuals to exercise HIPAA portability rights, in situations where the individual must exercise those rights within a certain number of days after losing coverage, but the individual is not promptly notified through a certificate of creditable coverage that he/she has lost coverage.
- Specifies that group health plans and group health insurers must provide a certificate of creditable coverage when an individual leaves a group health plan while taking leave under the Family and Medical Leave Act, and that any period of time during which a person does not have coverage while under such leave does not count against him/her with regard to HIPAA's protections.
- Sets forth a mathematical formula for counting the average number of employees employed by an employer during a year (various HIPAA insurance reform provisions require the determination of such an average number).

Automatic Rollover Rules are Coming

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) amended the automatic rollover rules to provide that involuntary distributions greater than \$1000 but less than \$5000 must be rolled over to an IRA (in the absence of specific participant directions). The IRS and DOL have issued regulations dealing with the automatic rollover rules.

The final rules are generally effective for involuntary distributions made on or after March 28, 2005. The IRS recently issued IRS Notice 2005-5 to clarify the following issues:

- ***Covered Distributions.*** An involuntary distribution is defined as a distribution that is made without the participant's consent and prior to the participant's attainment of age 62 or normal retirement age under the plan. A distribution that is made as a participant loan offset is not an eligible



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

rollover distribution. In addition, distributions to surviving spouses and alternate payees are eligible rollover distributions. The notice also confirms that rollover contributions are eligible rollover distributions even if the rollover contributions are not considered in determining whether the present value of the distribution exceeds \$5000.

- ***Administrative Delay.*** A plan with an involuntary distribution provision that has not established sufficient procedures, including the designation of an IRA provider, for distributions on or after March 28, 2005 will not be considered to be in violation of the new rollover rules as long as such distributions are made by December 31, 2005.
- ***Anti-cutback rules.*** The notice clarifies the plan will not violate the anti-cutback rules if it is amended to either eliminate involuntary distributions or to limit the amount of the involuntary distributions to \$1000 or less.
- ***Joint and survivor rules.*** Plans subject to the joint and survivor and pre-retirement rules that permit voluntary distributions greater than \$1000 but less than \$5000 do not have to get spousal consent before the annuity starting date.
- ***Participant Disclosures.*** The notice reiterates the disclosure requirements set forth in the DOL safe harbor. The IRS further provides that the plan sponsor can provide the disclosure requirements electronically as long as the requirements of IRC section 401(f) are met. In addition, if the notice is returned as undeliverable by the U.S. Postal Service and the plan has used the participant's most recent mailing address, the disclosure requirements will be met.
- ***Plan Amendments.*** Plans that currently have involuntary distributions that do not contain automatic rollover provisions must adopt good faith plan amendments by the end of the first plan year ending on or after March 28, 2005. The notice contains sample language for the good faith amendment that can be used by individually designed plans as well as pre-approved master or prototype plans.
- ***Government Plans.*** The automatic rollover rules apply to governmental plans, including Section 457(b) plans and non-electing church plans. The delayed effective date for these plans is as follows:
 - Governmental plans. Plan must comply with the automatic rollover rules with respect to all distributions occurring on or after the close of the first legislative session of the legislative authority to amend the plan that begins on or after January 1, 2006.
 - Non-electing church plan. These plans are considered compliant as long as the rules are applied to all distributions on or after the 60th day following the first church convention that begins on or after January 1, 2006.



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

PBGC Proposal Mandates Electronic Filing of Actuarial and Financial Information by Troubled Control Groups

PBGC has issued a proposed rule that requires the electronic filing of annual financial and actuarial information by controlled groups of corporations with pension plans that have significant funding problems.

Currently, plan sponsors have been able to provide the identifying, financial, and actuarial information required by ERISA section 4010 in a non-standardized format. This information is utilized by PBGC to anticipate possible major demands on the pension insurance system and to focus PBGC resources on situations that pose the greatest risks to the system. Because the information is provided in a non-standardized format it has been difficult for the PBGC to use the information for its intended purposes and also restricts PBGC's ability to perform electronic data analysis.

Under the proposed rule, certain identifying, financial, and actuarial information must be filed electronically in a standardized format, except as otherwise provided by PBGC. PBGC will provide instructions on how to file the information on its website.

Through the instructions on its website, PBGC would be able to modify the format of the information as needed, and to require the submission of additional information relating to the specific information described in the regulations.

These regulations also permit PBGC to simplify the reporting process; improve the accuracy, completeness, and timeliness of the information that it receives, and access the information quickly and in a complete manner from its data base. PBGC states that these changes will impose very little additional burden on required filers, most of whom are large corporations accustomed to submitting electronic filings with other government agencies.

Under the proposed rule, additional items of supporting information that are not currently required by PBGC, but are readily available to the filer, would have to be filed. The additional required items are:

1. The requirement to breakdown benefit liabilities (currently reported in the aggregate) and report both the amount of benefit liabilities and number of participants in each of the following categories:
 - a. Retired participants and beneficiaries receiving payments.
 - b. Terminated vested participants.
 - c. Active participants.



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

2. The requirement to provide, in addition to the items of supplementary information required to be provided with the actuarial valuation report that are already listed in PBGC Regs. 4010.8(a)(3):
 - a. The current liability, vested and non-vested, calculated under IRC section 412 (separated into information for retired participants and beneficiaries receiving payments, terminated vested participants, and active participants).
 - b. The expected increase in current liabilities due to benefits accruing during the plan year.
 - c. The expected plan disbursements for the plan year.
3. Filers will have to specify the actuarial assumptions for interest, i.e., the specific rate of interest, mortality, retirement age, and loading for administrative expenses used to calculate benefit liabilities for purposes of preparing the report.
4. Inclusion of identifying information about certain small entities that are contributing sponsors (defined as exempt entities because they are not required to file ERISA section 4010 reports and were not previously included in the ERISA section 4010 reports of other members of the controlled group).
5. Upon written request by PBGC, filers would be required to submit additional information about certain small or fully funded plans that are currently required only to be identified in the filing.
6. Filers would be required to report revenue, operating income, and net assets for each contributing sponsor as well as for all other nonexempt entities that are included in the consolidated financial statements.
7. Filers would be required to identify any controlled group members and plans that joined or left the controlled group during the information year.
8. Filers would be required to identify which plans are frozen as well as the nature of the freeze (e.g., service is frozen but pay is not).

The proposal also eliminates the current optional assumptions method for determining whether a contributing sponsor must file an ERISA section 4010 report if the aggregate unfunded vested benefits of all plans of a contributing sponsor's controlled group exceed \$50 million.

When the proposed rule is finalized, the new rules would apply to reporting under ERISA section 4010 for any information year ending on or after December 31, 2004.



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

Veterans Benefits Improvement Act of 2004

Congress passed the Veterans Benefits Improvement Act of 2004 which makes certain enhancements to the benefits and rights provided by the Uniform Services Employment and Reemployment Rights Act (USERRA) to an employee on active military duty. The bill is awaiting the President's signature.

The bill extends the period during which employers must make health coverage available to an employee in active military service from 18 months to two years. Under the bill the employers are required to provide notice to individuals, entitled to benefits under USERRA, of their rights, benefits and obligations. The notice obligation may be satisfied by posting the notice where employers customarily place notices for employees. The contents of the notice will be specified by the Secretary of Labor.

Advisory Opinion Holds that an Insurer's or Banker's Incentive Cash Contribution to an Individual's New HSA is not a Prohibited Transaction

In an advisory opinion, DOL's Employee Benefits Security Administration (EBSA) has ruled that the contribution of a \$100 cash credit by an insurer or bank to an individual's newly created health savings account (HSA) as a means of encouraging him/her to participate in their HSAs, is not a prohibited transaction. (ERISA Opinion Letter No 2004-09A, 2004)

The two scenarios presented in the letter were as follows:

1. Individual plans. In this scenario, only persons insured under high deductible health plans (HDHPs) issued by an insurance company in the individual market are able to establish HSAs with the insurer. However, a person does not have to establish an HSA with the insurer to participate in the HDHP. If the HSA is established with the insurer, the insurer serves as both a custodian or trustee and recordkeeper of the HSA.

To encourage participation in its own HSA program, the insurer will offer an incentive to a person who establishes an HSA when he/she first enters into the HDHP with the insurer. This incentive will be in the form of a \$100 cash credit by the insurer, as trustee or custodian, directly to the individual's HSA. The credit to the HSA is automatic, i.e., the individual does not need to make any contribution to the HSA in order to receive the credit. The account holder cannot divert the money to himself/herself before it is credited to the HSA.



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

The premiums payable under the HDHP does not vary based on the individual's choice of HSA custodian or trustee. In addition, the administrative fees charged on the HSA will not change as a result of the credit to the HSA.

2. Group plans. In this scenario, the insurer and its affiliates offer various health benefit plans in the group market, including HDHPs. In this situation, the insurer enters into a contractual relationship with a specified bank to provide HSAs for individuals covered by HDHPs issued by the insurer. However, the individual does not have to establish an HSA with the bank to participate in the HDHPs offered by the insurer. The bank serves as recordkeeper and custodian or trustee for the HSAs and receives compensation from the insurer for its services in that regard. Neither the bank nor the vendor is a member of the same controlled group as the insurer.

To encourage establishment of HSAs with the bank in connection with group HDHPs issued by the insurer, the bank offers an incentive to a person who establishes an HSA with the bank when the insurer first covers that person under a group HDHP. The incentive is in the form of a \$100 cash credit from the bank directly to the individual's HSA. As in the individual scenario, the premiums charged for the individual's coverage under the group will not vary based on the individual's choice of HSA custodian or trustee and the administrative fees charged on the HSA will not change.

The HSA is a plan. The insurer in scenario 1 and the bank in scenario 2 are disqualified persons. The prohibited transaction rules of ERISA prohibit several types of per se transactions between a plan and disqualified persons, including the transfer of assets between a plan and a disqualified person.

EBSA held that the \$100 cash contribution to the individual's HSA. Under IRS Notice 2004-50, 2004-IRB, Q&A-28, any person can make contributions to an HSA on behalf of an eligible individual.

Generally, HSAs are not employee welfare benefit plans within the meaning of ERISA, if the employer involvement with the HSA is limited.



Let us help you manage your benefits cost and risk.

Weekly Newsletter – Volume 1, No. 2 – January 21, 2005

IRS PLR Holds that a Rollover Maneuver by a 5% Owner Defers Required Minimum Distributions

IRS recently approved a deferral maneuver by a taxpayer who was employed by two different companies. In one company, he was a 5% owner and in the second company he did not have a 5% ownership interest. In the PLR the IRS said that the individual could defer required minimum distributions past age 70 ½ from the plan sponsored by the company in which he was a 5% owner by rolling over his account balance to the plan maintained by the company in which he did not have 5% ownership interest.

In reaching its conclusion the IRS looked for guidance in Treasury Regulations Section 1.401(a)(9)-7, Q&A 2, which provides that where amounts are distributed by one plan and rolled over to a receiving plan, “the benefit of the employee under the receiving plan is increased by the amount rolled over for purposes of determining the required minimum distribution” for the year following the year in which the amount rolled over is distributed. Based on this rule, the IRS held that the amount rolled over is subject to the required minimum distribution rules of the receiving the plan. Since in this situation, the individual is not a 5% owner of the company sponsoring the receiving plan he does not have to receive distributions until he reaches his required beginning date under the receiving plan.