

# BENEFIT BYLINES

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## Washington Update

### Background

Recent issues of *Benefit ByLines* have included articles informing readers about potential threats to the retirement security of American workers. Various proposals have been issued by members of Congress and the Administration that would reduce or cap the amount of contributions that could be made by workers and their employers to tax-deferred retirement/savings arrangements. The goal of many of these proposals is to reduce the up-front tax deductions for retirement savings by individuals and employers and apply those savings to reduce the Federal debt and yearly deficits.

### Various Proposals Have Surfaced

Several tax reform/debt reduction proposals directly target all workers by reducing future contribution opportunities for everyone. Other proposals focus on business owners and wealthier tax payers. Some argue that it is only fair to expect more affluent taxpayers to shoulder more of the financial burden to help solve our Nation's fiscal crisis. Without debating the merits of that issue, there is a practical counter argument: business owners and executives will be much less inclined to deal with the complexity and expenses associated with maintaining retirement programs for their workers if their own tax-deferred savings opportunities are curtailed or eliminated. So, restricting the opportunities for business owners and executives to save for their own retirement has a high probability of eliminating those opportunities for their employees as well.

To date, no specific proposal negatively impacting retirement savings has gained traction. The Administration's recent budget proposal included two highly controversial pension recommendations, one would result in double taxation on amounts contributed by higher income individuals and the other would restrict future tax-deferred contributions once an individual had accumulated just over \$3 million in all IRA and employer-sponsored savings accounts combined. The Administration's budget proposal was generally perceived as being "dead on arrival" at Congress. However, that does not mean that the recommendations that are part of it (including those affecting retirement savings) will not resurface as the debate continues. (*Continued on Page 4*)

## Save My 401k Campaign Continues

Thanks to all of our readers who sent emails to their Federal representatives as part of last year's Save My 401k Campaign. Also, thanks to plan sponsors who encouraged their employees to email their representatives too.

### Update

ASPPA Executive Director, Brian Graff, reports that Phase I of the Save My 401k Campaign was highly successful. More than 100,000 emails were sent to representatives of Congress by plan sponsors, participants and service providers. According to Graff, more people in Washington now have an appreciation of the importance of 401(k) and other employer-sponsored retirement plans but there is more work to do.

### More than Just 401(k) Plans at Risk

It is important to recognize that Federal policy makers are looking at cut-backs in more than just 401(k) plans as sources of revenue for deficit reduction. The name 401(k) is often used to refer to all types of employer-sponsored savings plans, including 403(b) and SIMPLE plans as well as 457 arrangements. Further, some deficit reduction/tax reform proposals, e.g., the Administration's proposed budget, would impact virtually all types of tax-deferred savings arrangements, including IRAs as well as employer-sponsored pension, profit sharing and 401(k) type plans.

### Why is ASPPA Focusing on Just 401(k) Plans?

ASPPA, the Small Business Council of America, and other organizations representing small businesses and the private retirement system are NOT limiting their education and lobbying efforts to just 401(k) arrangements. They have issued position papers and met with public officials and their aides on issues related to all types of tax-favored retirement arrangements. (*Continued on Page 2*)

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Nonetheless, ASPPA believes that their basic message to protect workers' retirement security will gain more attention and support by capitalizing on the name recognition of 401(k) plans. To that point, almost everyone inside and outside the Washington beltway has heard of 401(k) plans and there is a general impression among most constituents that 401(k) plans are a good thing.

### **Individual Taxpayers Have the Most Impact**

According to ASPPA, Congress does take notice when they receive emails and letters from retirement plan professionals on particular issues. However, they tend to pay greatest attention when they hear from thousands of **individual taxpayers**. This is why it is so important to continue to involve employees in grassroots campaigns like Save My 401k.

### **Save My 401k Video**

Please browse to the link below to view ASPPA's award-winning "Save My 401k" video. It is brief, to the point, and somewhat amusing. <http://www.youtube.com/embed/nt-JkLigag>

### **Call to Action**

ABP encourages all of our readers to consider sending emails to their House and Senate representatives, even if they have done so previously. It is easy to do this through the Save My 401k website, [www.savemy401k.com](http://www.savemy401k.com).

In addition, we hope that business owners and managers who are part of firms that sponsor 401(k) plans will contact their employees to enlist their support. Please ask them to watch the Save My 401k video, then email their Congressmen. A suggested email memo to employees with links to both the Save My 401k video and website is attached.

ABP will continue to keep our readers informed about further developments in future issues of *Benefit ByLines*. ■

### ***Expanded Roth Conversion and Extended Charitable IRA Rollover Opportunities***

*This article was originally scheduled to be included in the Spring issue of Benefit ByLines but was pre-empted by a discussion of the Obama Administration's 2014 budget proposal that was released just before we went to press.*

The so-called "fiscal cliff" was temporarily avoided when the American Taxpayer Relief Act of 2012 was signed into law by President Obama on January 2, 2013 to become effective as of the beginning of the year. The Taxpayer Relief Act did not include any cutbacks on contributions and compensation limits affecting retirement savings plans as some had originally feared it would. It did, however, include provisions extending

IRA Charitable Rollovers and expanding Roth Conversion opportunities within employer sponsored 401(k) type plans. These are both discussed below.

### **IRA Charitable Rollovers**

Since 2006, IRA account holders who have attained age 70½ have been able to have distributions from their IRA account transferred directly to qualified charities. The annual distribution limit for this purpose is \$100,000. Some taxpayers allocate their post 70½ required IRA minimum distributions under this provision to avoid the tax that would otherwise be imposed if they received the money directly. While taxpayers who chose to make charitable distributions do not pay tax on those distributions, they do not also get to claim a charitable deduction. Since taxes have not been previously paid on non-Roth IRA contributions or accumulated earnings, this additional deduction would be considered "double dipping". On the other hand, taxpayers do have the option to take distributions from their IRA, pay tax on those distributions, and then make a tax-deductible charitable contribution. However, various Federal and state tax law requirements sometimes prevent the deduction from fully offsetting taxable income.

Charitable IRA rollover provisions were first available for the 2006 tax year and have been extended several times. The American Taxpayer Relief Act of 2012 provides a further extension covering charitable distributions made in 2013. Unless Congress takes further action, the opportunity to make direct charitable rollovers from an IRA expires on December 31, 2013.

### **Roth Conversions**

For a number of years, sponsors of 401(k) type plans have been able to offer participants the opportunity to contribute elective deferrals on either a traditional pre-tax or a Roth after-tax basis. In 2010, Congress enacted additional legislation permitting participants to convert existing pre-tax balances to Roth accounts within 401(k) type plans. Under this conversion, participants would pay Federal income tax at the time they file their personal tax returns for the tax year containing the conversion. However, the 2010 tax act allowed in-plan Roth conversions only for amounts that were otherwise eligible for distribution from the employer's plan. This generally meant that conversions were permitted by participants who had attained age 59½ or otherwise satisfied the plan's in-service withdrawal provisions.

The American Taxpayer Relief Act of 2012 liberalizes the rules for making in-plan conversions by eliminating the "distribution eligible" requirement. Beginning in 2013, any plan participant can convert all or a portion of his/her account from pre-tax to Roth, irrespective of age or other conditions, provided that the employer's plan is amended to allow this option.

Please contact your ABP administrator if this is a plan design feature that appeals to you. *(Continued on Page 3)*

*(Expanded Roth Conversion - Continued from Page 2)*

### **Observations**

1. A relatively small percentage of workers are in a position to take advantage of either IRA charitable rollovers or Roth in-plan conversions. However, the potential benefits of each of these options can be substantial to those who elect them.
2. Government projections indicate that the expansion of the Roth conversion opportunity will increase federal revenues by \$5.099 billion dollars over the next 10 years. In arriving at this financial projection, the Treasury Department has assumed that a substantial number of individuals will be willing to pay taxes currently in exchange for the opportunity to avoid paying them or having them paid by their estates down the road.
3. While historically supporting the inclusion of Roth provisions in clients' plans, ABP has maintained neutrality with respect to promoting their advantages to individual participants. The decision to make after-tax Roth contributions rather than traditional pre-tax deferrals requires an analysis of both an individual's current and future circumstances and, at least in some circumstances, an educated guess as to what future tax rates will be for the individual. Roth skeptics point out that giving up current tax deductions in exchange for the promise of future tax benefits requires a leap of faith that those in Washington will not change the tax rules down the road in a manner that will take away anticipated benefits. To those who say that could not happen, consider the fact that Social Security benefit payments were received totally tax-free prior to 1984 but no longer are. The pension proposals included as part of the Administration's budget draft do not rise to that level of tax policy reversal. However, these proposals, if enacted into law, would change long standing rules that influenced at least some taxpayers to take actions they might not otherwise have taken. In any event, participants should be encouraged to seek the advice of their personal financial advisers before seriously considering either of the options discussed above. ■

### ***Maximize Contributions While You Can***

The optimistic view is that Federal tax reform and debt reduction will be achieved without any negative impact on the private retirement system. A more realistic assessment is that, despite strong grass roots lobbying, some cutback in future tax-deferred savings opportunities is likely to occur when comprehensive tax legislation eventually becomes law. However, both the timing and specific changes that might happen are anyone's guess at this point in time.

Given this uncertainty, ABP suggests that all individuals who have access to either a personal IRA account or employer-sponsored retirement/savings arrangement take full advantage of the opportunity to maximize their contributions this year, next year and as long as possible thereafter. Specific suggestions (for individuals and plan sponsors) are provided herein.

### **Maximize Elective Deferrals**

Employees participating in 401(k), 403(b) and SIMPLE arrangements should maximize their elective deferral contributions if at all possible. For 2013, the statutory contribution limit for elective deferrals in 401(k) and 403(b) plans is \$17,500 and the limit for SIMPLE IRAs is \$12,000. As a minimum, participants at all income levels should contribute the amount required to earn them the maximum employer matching contribution available, if this is a feature of their employer's plan. Note: Some plans restrict elective deferrals to a stipulated percentage of pay and others may need to restrict contributions by highly-compensated employees due to discrimination testing in non-Safe Harbor plans. Therefore, participants need to check with their plan's internal representative before changing elections.

### **Take Full Advantage of Catch-Up Contribution Opportunity**

To the extent available under your employer's salary reduction plan, individuals who have attained age 50 can make additional "catch-up" contributions. For 2013, the statutory limit on catch-up contributions for 401(k) and 403(b) arrangements is \$5,500 and the limit for SIMPLE IRAs is \$2,500. Catch-up contributions may qualify for an employer match in some plans. Significantly, catch-up contributions are not subject to 401(k) plan ADP discrimination testing.

### **Maximize Profit Sharing Contributions/Allocations**

Profit sharing plans, and the profit sharing component of 401(k) and 403(b) plans, can be designed in different ways. The specific design parameters are determined by the employer as is the amount of each year's discretionary contribution. For 2013, up to \$51,000 can be contributed on behalf of higher paid employees. If a 401(k) arrangement exists within the plan, elective deferrals do count toward this limit, but catch-up contributions can be allocated in addition (\$56,500 total). Using design techniques available through ABP, it is possible to allocate different rates of employer contributions to each participant or class of participants. This provides the opportunity for the employer to allocate limited dollars selectively to key employees and others who they want to recognize without making the same level of contribution for all employees.

### **Implement a Cash Balance Plan**

Firms that have consistently strong profits and are owned or managed by highly compensated individuals may want to consider implementing a cash balance retirement plan. A cash balance plan is a hybrid arrangement --- it is a defined benefit plan that has many of the characteristics of a defined contribution arrangement. The contribution limits for a cash balance plan can be well in excess of the \$51,000 statutory contribution limit applicable to defined contribution plans. In fact, it can be as much as \$100,000 to \$150,000 per participant for higher paid employees. Further, like a class allocation profit sharing plan, cash balance plans can be designed to provide higher contributions for targeted employees. *(Continued on Page 4)*

*(Maximize Contributions While You Can - Continued from Page 3)*

### **Implementation**

Although increasing elective deferrals and catch-up contributions are strategies within each participant's individual control, other strategies may require plan elections and design changes by the employer to provide the opportunity to maximize contributions by or on behalf of some or all participants. Further, some strategies can be implemented for 2013 within existing plan structures or by plan design changes that can take effect this year; other potential design or administrative changes may require decisions/actions this year in order to take effect for 2014.

Feel free to contact a member of ABP's professional staff to discuss plan objectives and opportunities that may be available to increase retirement savings opportunities for some or all participants in your plan or the plan of one of your clients. ■

### ***Washington Update – Continued from Page 1***

### **What To Expect**

At the Mid-Atlantic Benefits Conference in Philadelphia in May, Brian Graff, Executive Director of ASPPA, observed that **while the timing of tax reform legislation is uncertain, it will happen eventually**. Further, Graff warns that cut backs

on retirement savings opportunities, in one form or another, continue to be on the agenda when tax reform and debt reduction are discussed.

Informal tax reform and deficit reduction discussions are on-going, including some that are bi-partisan. However, the Washington insiders that ABP has heard from think it is unlikely for a comprehensive agreement to be reached before Labor Day, at best. They feel that the next best shot for an agreement to be achieved will be toward the end of September when a further extension of the debt ceiling must be addressed as well as the adoption of a Federal budget for the fiscal year beginning 10/1/2013. Of course, this is just speculation in a generally dysfunctional Washington environment.

### **ABP Observation**

While most of us are in favor of reducing the Federal debt, targeting retirement savings in an attempt to do so is short cited. The serious funding problems with Social Security have not yet been addressed and most workers are not saving enough on their own to make up for the probable shortage of funds when they actually retire. Logically, it doesn't make sense to address one financial crisis (the Federal debt) by taking actions that make another rapidly approaching crisis (inadequate retirement savings by millions of families) worse.

It is essential for retirement plan sponsors, participants and service providers to continue their grassroots efforts to urge legislators to implement sensible tax reform that does not put the retirement security of American workers in jeopardy. ■

### ***Associated Benefit Planners, Ltd.***

Associated Benefit Planners, Ltd. (ABP) is an independent consultant and third party administrator (TPA) operating from offices located in Berwyn and King of Prussia, Pennsylvania. We specialize in the design and administration of employer-sponsored retirement/savings plans, including 401(k) arrangements. ABP also provides plan document and compliance support for Section 125 Plans and Employee Welfare Plans, operating on a fee-for-service basis.

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