

Federal Update 2005-32

Report to Attendees at 2005 NCTR Convention on Federal Developments

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Tampa, Florida
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Introduction

I'll be covering three areas today:

- Where do we stand on federal issues?
- A five-minute summary of 18 years of NCTR's lobbying
- Linguistics?

Where Do We Stand on Federal Issues?

Accomplishments Thus Far in 2005

We've accomplished several items thus far in 2005. First, legislation was enacted in April that expands pension protections if a plan participant goes into bankruptcy. The protections are in the Bankruptcy Abuse Prevention and Consumer Protection Act (Public Law 109-8). What's key for us is that the legislative history accompanying the bill makes clear that the new law doesn't overturn prior case law. For more information, go to Federal Update 2005-15.

Another area of accomplishment relates to legislation about the use of Social Security Numbers (SSN). We worked to ensure that NCTR members can continue to use SSNs in H.R. 1745, legislation about SSN privacy. Unlike previous versions of the bill, it now includes an exemption for submitting an SSN as part of the administration of, or providing benefits under an employee benefit plan, including those of state and local governments. The bill is still in committee. Federal Update 2005-16 contains details.

Social Security Privatization

Let's move on to Social Security privatization. The President made it a top priority for 2005. He largely failed, however, to attract the support of the public. Congress, for its part, is backing away from the issue, but, at least on the Senate side, not for lack of trying. Sen. Charles Grassley (R-IA), Chairman of the Finance Committee, issued a press release on July 14 saying that the Committee had 15 meetings since February and three hearings. The implication was that despite the high level of activity,

no agreement could be reached. Rep. John Boehner (R-OH) was blunter. He said on September 27 that enacting Social Security reform is “like asking Congress to eat a bowl of cold, green peas – they don’t want to do it.”

Pension Legislation

Also stalled is S. 1783, Pension Security and Transparency Act. The legislation represents a compromise between a Senate Finance Committee bill and the Defined Benefit Security Act of the Senate Health, Education, Labor, and Pension (HELP) Committee. The bill includes the following provisions of interest to NCTR members:

- Clarification of Purchase of Service Credit
- After-Tax Rollovers into DB Plans
- Relief from Minimum Distribution Rules
- Exemption for Public Safety Workers from 10% Early Withdrawal Tax

The bill also addresses cash balance plans. The language of the provision has created concern, as described in the memo by David Powell, the Groom Law Group, attached at the end of this update.

The entire bill has bogged down over funding provisions that don’t affect NCTR members. Whether the Senate will get to it before the end of the year is questionable.

Other Federal Issues

Several other issues are percolating:

- Proposed Repeal of Pick Ups
- Section 415 Proposed Regs
- Retiree Health Care (9/27/05 Court Ruling)

Proposed Repeal of Pick Ups

Earlier this year, the Joint Committee on Taxation proposed the repeal of pick ups. If enacted, it would have two results:

- Eliminate state and local governments’ right to pay employee (EE) pension contributions, known as the “pick up,” and
- Make employee pension contributions includable in income and treated as wages for FICA purposes. In other words, workers would be subject to a new tax and they would have to pay Social Security payroll taxes on the contributions if they are in jurisdictions that participate in Social Security.

NASRA and NCTR worked on a survey in September to assess the number of plan participants who would be affected by the repeal. The survey shows that over **80%**

of participants in large state and local government plans would be affected. See Federal Update 2005-30 for the survey results.

Section 415 Proposed Regs

In May, the U.S. Department of the Treasury issued proposed regulations on Section 415 of the Internal Revenue Code. Section 415 limits the size of an annual payout from a defined benefit plan and the annual contribution to a DC plan.

The proposed regs raise many issues, including treatment of COLAs, return to work provisions, and post-termination pay, such as sick leave and other forms of payment at retirement. Federal Update 2005-26 has further information.

Retiree Health Care (9/27/05 Court Ruling)

In the area of retiree health care, a recent court decision makes clear that employers may reduce or eliminate retiree health care benefits when beneficiaries reach Medicare age without violating the Age Discrimination in Employment Act (ADEA) (Erie County Retirees Assn. v. Erie County, September 27). The decision allows the Equal Employment Opportunity Commission (EEOC) to go forward with a rule that permits employers to take such actions. NCTR, NASRA, and NCPERS favor this position as do public employee unions who provided the court with an Amicus Brief in support of the EEOC rule.

Two final points relate to changes that your legislatures may make in the future. If your legislature is contemplating:

- a change in your plan's COLA, be sure to check the federal minimum distribution rules, summarized in Federal Update 2004-32, or
- a program of interstate pension portability, be sure to review NCTR's model language, at http://www.nctr.org/pdf/ecs_portability_teachers.pdf

Summary of 18 Years of Lobbying Activity for NCTR

As most of you know, I'll be retiring at the end of 2005 from my position as Washington Counsel for NCTR. I've been working with the organization for 18 years and from that vantage point I can summarize our lobbying efforts under two categories:

- Protective
- Proactive

Protective Lobbying

"Protective lobbying" preserves the well-established distinction between federal regulation and state/local government (SLG) regulation of NCTR members. In the late

1980's through early 1990's, various Members of Congress promoted a mini-ERISA for NCTR members. The bills would have established federal reporting, accounting, and fiduciary duties, even though such rules already exist on the state level. The new regulation would have been carried out by U.S. Department of Labor and would have been in addition to IRS oversight. The bills were known as PEPPRA (the Public Employee Pension Plan Reporting and Accounting Act) and PERISA (the Public Retirement Employee Income Security Act).

NCTR's response to the threat of additional federal regulation was twofold. First, it conducted grassroots lobbying and published studies showing the breadth of protective state laws. (The publication continues to exist. Called Protecting Retirees' Money, the most recent version came out earlier this year.)

Challenges remain in NCTR's effort to hold off further federal regulation. In 2002, legislation was introduced in response to the Enron situation. It would have imposed federal reporting rules on defined contribution plans including those in the public sector. The reporting would have been similar to that in the PEPPRA/PERISA bills. The bill is now stalled in committee, but illustrates that the threat continues.

Another problem arose in the same year. IRS issued temporary regulations on the minimum distribution rules. Such rules specify how and when pensions must be paid. The temporary regulations interfered with COLAs of NCTR members. After effective lobbying by NCTR members and others, IRS changed its approach in the final regulations.

Proactive Lobbying

The second category of lobbying is proactive. Such lobbying:

- Enhances state and local government defined benefit plans, and
- Addresses federal pension laws that conflict with the structures of NCTR members.

Enhancing Defined Benefit Plans' Portability

When the opponents of defined benefit (DB) plans began their campaign in the middle-1990's, they cited lack of portability as one of their arguments. We recognized the argument and sought ways to address portability. An obvious area was the elimination of federal barriers created by the Section 415 limits that impeded the full use of purchases of service credit (PSC). State legislatures authorize PSC to make DB plans portable. We worked with Congress to harmonize PSC with the Section 415 limits. The changes we secured were included in the Taxpayer Relief Act of 1997.

With that change accomplished, we moved to make more sources of funds available for PSC. Over the years, NCTR members told me that their plan participants wanted to use 403(b) and 457 funds on a pre-tax basis for PSC. We worked with

Congress on this change and it was made part of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA).

Addressing Conflicting Federal Law

Both federal and state pension laws govern NCTR members. It seems logical that conflicts between the two bodies of law would occur and they do. Thus, we need to be proactive in either eliminating conflicting federal law or harmonizing it with relevant state laws.

We worked with Congress in two areas. First, the Section 415 limits have always created conflicts and we secured the elimination of a problem between the Section 415 definition of compensation and that of the states in the Small Business Job Protection Act of 1996. Second, the nondiscrimination rules under Section 401(a)(4) threatened to interfere with the historical structure of state and local government retirement plans. Congress implemented the rules to address an abuse in the private sector. We pointed out that the abuse did not relate to the public sector. Congress agreed and exempted state and local government plans from the rules in the Taxpayer Relief Act of 1997.

Key to Lobbying Success

Two factors contribute to NCTR's lobbying success. First, pension issues have a "motherhood and apple pie" reputation in Congress. Members of Congress, both Republicans and Democrats, view pensions as necessary to helping Americans live in dignity during their retirement. This bipartisan support has helped move our issues forward.

Second and complementary to the first factor is NCTR members' strong grassroots involvement in federal lobbying. They are the **engine that fuels successful efforts**. Legislative Committee members convene in Washington yearly and meet with their Congressional delegations. Throughout the year the entire membership has always been available to lobby Congress through letters, emails, calls, lunches with staff in district, and even spur-of-the-moment trips to Washington.

Linguistics? [Lɪŋ'gwɪstəks]¹

So what will I be doing after I retire? I plan to take some time off and study Spanish in Mexico. I'll then go to graduate school for a master's in linguistics. After I finish the degree, I should be able to answer such puzzling questions as:

- Why we park in the driveway and drive in the parkway
- Why we pronounce "Buick" and "quick" differently even though they are spelled alike
- Why we say something is out of whack (what is a whack?)
- Why "abbreviation" is such a long word

¹ I've written the word phonetically, which, as you see, includes symbols not used in our alphabet.

- Why a “wise man” and a “wise guy” are opposites
- Why “phonics” is not spelled the way it sounds
- And the most puzzling of all: doesn’t “expecting the unexpected” make the unexpected expected?

Final Thoughts

Thanks for the great ride! I’ll miss all of you.

Attachment relating to Cash Balance Provision in S. 1783

TO: Cynthia L. Moore, NCTR Washington Counsel

FROM: David Powell, Attorney at Law, The Groom Law Group Chartered

RE: Cash Balance Provision in S. 1783

You asked that I send you a short explanation of the governmental plan problems with the current Senate bill dealing with hybrid plans.

As you know, until recently, the cash balance plan (also known as hybrid plan) changes in various pension bills only modified sections of the Internal Revenue Code and ERISA that did not apply to public plans. However, the Senate pension bill language (S. 1783) is now worded in a way that could adversely affect governmental plans - potentially not just governmental cash balance/hybrid plans, but cash-balance-like features common in traditional governmental defined benefit plans, such as refunds of pay-based contributions with interest.

The problem is caused by a combination of (1) language adding cash balance plan requirements to the Age Discrimination in Employment Act (ADEA), and (2) the broad definition of "cash balance plan" in the bill. ADEA already applies to governmental plans, although, at least in the case of state-level plans, only the Equal Employment Opportunity Commission (EEOC) and not individual plaintiffs can sue to enforce it. The current language in the Senate bill would state that any defined benefit plan which is a "cash balance plan" shall not fail to meet ADEA if it is a "qualified cash balance plan for purposes of section 204(b)(5) of [ERISA]". And a cash balance plan is essentially defined as any defined benefit plan with a hypothetical account with pay and interest credits. The result would be that governmental defined benefit plans with such notional accounts would be precluded from meeting the requirements of ADEA, because they are not subject to ERISA, or they would be required to meet certain private sector ERISA rules, including minimum vesting requirements and minimum and maximum interest rates, in order to comply with ADEA—conflicting with the state and local statutes currently governing these plans in this area and state constitutional limits on changing

benefit formulas for active governmental employees. This would not only apply ill-fitting requirements on these programs, but would jeopardize the ability of public sector employees to directly influence these plan design provisions at the state and local level.

There are several large governmental cash balance plans with pay and interest credits. In addition, though, it is not only what people tend to think of as "cash balance plans" that are at risk. The definition of "qualified cash balance plan" in the bill is essentially any notional account in a defined benefit plan that has pay and interest-based credits. It will be hard to argue, for example, that a typical governmental plan refund feature is not exactly that.

All the proposed "fix" would say is that a governmental defined benefit plan would not violate ADEA merely because it has notional accounts based on pay and interest-based credits. Such plans would not also have to meet ERISA requirements such as vesting and interest rate rules. The provision does not promote cash balance plans or conversions to cash balance plans. Governmental plans would remain subject to ADEA generally, of course, and could not, for example, decrease interest or pay crediting rates, or any other benefit features, on account of age.

Please let me know if you have any questions.