Plan Sponsor Voice
A Publication of Nationwide® Retirement Solutions – a Nationwide® Financial company
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Nationwide produces this publication to provide public defined contribution plan sponsors with information about federal legislative and regulatory activity that may be relevant to plan administration and/or design.

Federal Legislative and Regulatory Report

March 2004

I. Washington Update

In early March, Bridget Flynn from Nationwide's Government Relations Office and Mary Willett of Willett Consulting met with several key legislative staffers to discuss the issues that are important to public sector plan sponsors and their employees who are participating in supplemental defined contribution plans. These issues included:

- making EGTRRA provisions permanent,
- protecting the ability of individuals to invest through their employer sponsored plans,
- allowing contributions of sick and vacation leave cash-outs into 457 plans after a termination date, and
- providing exceptions to trustee requirements for government employer-sponsored deemed IRAs.

Representatives Portman and Cardin continue to work on retirement legislation to be introduced this year. They are exploring an expansion of the Saver's Credit to provide additional incentives for low- and moderate-income workers to save and invest for retirement. One approach being discussed would provide a fully refundable credit (no income taxes need to be paid by the individual to receive this credit) to eligible employees. The credit would be directly deposited into a retirement-savings account, such as an employer plan or individual retirement account.

The House-Senate conference on the Pension Funding Equity Act (H.R. 3108) has been working out the differences in the two versions of this bill. Although both bills provide a replacement of the 30-year Treasury bond for pension calculations, the main point of contention pertains to the inclusion of a deficit reduction contribution holiday in the Senate's version. The conference committee is chaired by Representative John Boehner (R-Ohio).

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Government Pension Offset Exemption Requirements Change

Chart: Impact of Last-Day Exemption Change On the GPO

W-2 changes to show employer HSA contributions

 NRS-0943 (03/2004)

The Health Savings Accounts for the Uninsured Act of 2004 (H.R. 3901) was introduced in the House of Representatives. This legislation would allow health savings account (HSA) holders to deduct premiums required under their high deductible plans. Currently, only their employer contributions made to HSAs are deductible. If enacted, this would apply to taxable years beginning after December 31, 2003.

II. Government Pension Offset Exemption Requirements Change

The Social Security Protection Act (HR 743) enacted on March 2, 2004, will change the exemption requirements for the Government Pension Offset (GPO). The GPO affects public employees who are entitled to spouse/surviving spouse benefits from Social Security, and who receive pensions from federal, state and local government retirement systems that do not cover their employment under Social Security. The GPO could reduce the spouse/surviving spouse benefit by two-thirds of the amount of the pension they receive from the government retirement system.

> **Example**: Joe receives a monthly pension of $600 from a state retirement system, which does not cover employees under Social Security. He is also potentially eligible for a $500 monthly widower's benefit from Social Security. The GPO will reduce his monthly widower's benefit by two-thirds of the amount of his state pension ($600 x .6666) or $400. Instead of total monthly benefits of $1,100 (full Social Security benefit plus his state pension), because of the GPO he will actually receive total monthly benefits of $700 ($100 monthly Social Security widower's benefit plus his $600 monthly pension from the state retirement system).

Until the enactment of the Social Security Protection Act, state and local government employees who are subject to the GPO were exempt if their last day of state/local government employment was in a job covered by both Social Security **and** the state or local government retirement system. The Act:

- changes the GPO exemption requirements,
- adds disclosure requirements for public employers not participating in Social Security and
- includes additional account statement requirements for the Social Security Administration.

GPO Exemption Changes - Effective July 1, 2004, state and local government employees who are not covered under Social Security will be exempt from GPO reduction if they work at least 60 consecutive months, including the last day of employment, in Social Security covered employment under the same public retirement system that provides their pension. Individuals within 5 years of retirement after enactment of this new law will be subject to transition rules.

Disclosure Requirements - Effective on or after January 1, 2005, state and local government employers who do not cover employees under Social Security will be required to provide written notice to newly hired employees. This notice must explain the maximum effect to their potential Social Security benefits that may result from public employment that is not covered under Social Security. Newly hired employees will be required to sign a statement acknowledging that they have received this information.

Social Security Account Statements - After January 1, 2007, non-covered employees will receive account statements from the Social Security Administration that will include an explanation of the maximum potential benefit reductions that may result from the receipt of a state or local government pension that is based on employment not covered by Social Security.

This Act also includes a provision that permits Kentucky and Louisiana to operate divided retirement systems, effective January 1, 2003. Divided systems cover some groups of employees under Social Security while other groups, such as police, fire and teachers, are not covered. Employees in these systems who are not covered under Social Security will be subject to the GPO unless they meet the exemption requirements.

The following Q and A [page 4 of this document] is from the Social Security Administration and reflects the impact the change in the last-day employment exemption will have on the GPO.

III. W-2 Modified for Employer Health Savings Account Contributions

The IRS recently released Announcement 2004-2 that adds a new reporting code for employer contributions to Health Savings Accounts (HSA). For tax years beginning January 1, 2004, employer contributions to employee HSAs will be reported on the employees' W-2 forms in Box 12, Code W.

The revised 2004 W-2 Instructions state that:

- Employer contributions to an employee's HSA are not subject to federal income tax withholding or FICA taxes if the employer believes at the time of payment that it would be excludable from these requirements.
- Employee contributions to an HSA that are not made through pre-tax contributions to an employer sponsored cafeteria plan (Section 125 plan) will be included in the employee's wages and subject to income tax withholding and applicable FICA taxes.
- Employee HSA contributions made with after tax dollars are deductible on the employee's federal income tax return and must be reported on IRS Form 8889 which will be attached to employee's federal income tax return.

For more information about the features and requirements of HSAs, see Federal Legislative and Regulatory Reports for December 2003 and January 2004.

Find it online

A complete list of Social Security Q&As may be found on the Social Security Administration's Web site at http://ssa-custhelp.ssa.gov/cgi-bin/ssa.cfg/php/enduser/std_adp.php?p_sid=Oknee-Rg&p_lva=&p_faqid=1265

For more information on IRS Announcement 2004-2 and the new reporting code for employer contributions to Health Savings Accounts, please refer to www.irs.gov/pub-pdf/fw.2.pdf and www.irs.gov/pub/irs-pdf/iw2w3.pdf

IV. Keeping watch

Nationwide continues to monitor investigations into mutual-fund trading practices and related issues. The most recent information on these issues is on the Employer page of your plan Web site.

In addition, we report guidance on legislative and regulatory activity that is relevant to government sector defined contribution plans through our quarterly *Plan Sponsor Voice* newsletter, monthly *Federal Legislative and Regulatory Reports* and e-mail alerts distributed as needed.

Impact of Last-Day Exemption Change on the GPO

When will the new 60-month (5-year)/last day exemption requirement to GPO become effective?	Generally, the changes will be effective for Social Security benefit applications that are filed in April 2004 or later. This change will not apply for anyone whose last day of government employment occurs before July 1, 2004, even if the application for Social Security benefits is filed in April 2004 or later.
Will the change in the law affect anyone already receiving Social Security benefits and who was able to use the more liberal last day requirement?	No, anyone receiving full Social Security spouse or surviving spouse benefits because of the previous last day exemption rule will continue to receive their full Social Security benefit.
Will this change affect the future Social Security benefits of anyone who worked in non-covered employment and recently retired after working their final day of government employment in a job that was covered under Social Security?	No. Any state or local government employee whose last day of employment was covered both by Social Security and their state/local pension system would not have the GPO applied to their future claim for Social Security spouse/surviving spouse's benefits.
How will this change affect employees who will either retire soon, but are not yet eligible for Social Security, if they switch to Social Security-covered employment before retiring ?	As long as their last day of employment occurs before July 1, 2004 and that last day of employment is covered both by Social Security and their pension system, they will meet the last day exemption to the GPO. In this case, it does not matter if they would not be eligible for Social Security benefits for several years.
If someone is eligible for Social Security benefits and files before the change to the GPO exemption becomes effective, but delays retirement, will (s)he still be able to use the more liberal last day exemption?	Yes. Anyone eligible for Social Security spouse/surviving spouse's benefits who files for those benefits on or before March 2004 can work his/her last day in a position covered under both Social Security and their pension system and qualify for the last-day exemption regardless of how far in the future their retirement occurs.
Would this change affect someone who is going to retire in the next few years?	Probably. This individual could avoid the GPO if: - (S)he files for benefits before April 1, 2004 or retires before July 1, 2004 with the last day of work covered under both Social Security and the public retirement system. - Otherwise the new 60-month/last-day rule would be the only way to avoid the GPO.
Could the GPO eliminate the spouse or surviving spouse benefit?	Yes.
Will either the new or the old GPO last-day exemption affect the Windfall Elimination Provision (WEP) on a public employee's own Social Security benefits?	No. WEP will continue to apply to public employees entitled to Social security benefits based on work covered under Social Security and who receive pensions from a public retirement system that does not participate in Social Security. The WEP will reduce their Security benefits because their benefits are calculated under a different benefit formula, which reduces but does not eliminate their Social Security benefit.

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