

Rosen Seymour Shapss Martin & Company LLP
Certified Public Accountants & Profitability Consultants

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BENEFITS BLAST

Greetings!

Welcome to the Employee Benefits & Executive Compensation Service Group's Benefits Blast! (a publication of Rosen Seymour Shapss Martin & Company LLP). Here is where you will receive periodic updates on all your employee benefits and executive compensation needs.

Employee benefits programs and executive compensation issues are more complex than ever - tax laws and the applicable statutory schemes are continually changing, and increasingly employers must consider international implications. These issues also are critical to maintaining continuity in your workplace and retaining key employees.

We welcome your questions or comments about the topics discussed or related ones. Please feel free to contact us at 212-303-1806 or e-mail us at aneumark@rssmcpa.com and let us know how we can be of assistance.

Sincerely,

Avery E. Neumark, CPA, JD
 Partner-in-Charge of Employee Benefits & Executive Compensation

Net Unrealized Appreciation - Can It Work For You?

When an individual receives a distribution from his or her qualified plan (e.g. 401(k), profit sharing plan) the distribution is usually taxed at ordinary income tax rates. It

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may, however, be possible to reduce taxes if the retirement account is in a qualified plan that (1) includes employer stock and (2) that stock has net unrealized appreciation ("NUA").

NUA is the difference between the market value of the stock at the time of distribution and its original cost to the plan.

The NUA rules allow an individual who is retiring or changing jobs to take a lump sum distribution of company stock, and immediately pay income tax on the distribution at ordinary tax rates. The tax is calculated, however, on the COST basis of the stock and not the market value of the stock at date of distribution. Remaining assets in the qualified account can be rolled over into another qualified plan or IRA. If the recipient receives a distribution prior to age 55, there is usually an additional 10% penalty added to the tax.

The NUA election is **not** all inclusive. You may elect to include only a portion of the stock. You could, for example, choose to use only those shares with a lower cost basis. Once the stock is segregated from the qualified plan, the recipient is able to sell it and pay tax on the gain, including the NUA, at lower (capital gains) tax rates. The recipient might choose not to sell the stock, but to include same in his or her estate, which might yield additional tax savings.

In order to qualify for such treatment,

- the individual must be eligible to take a lump sum distribution,
- the distribution must include all of his or her benefits in all plans sponsored by the same employer,
- at least part of the distribution must be in company stock, and
- the stock must have been purchased with either employer contributions or employee **pretax** contributions.

If you are near retirement, contemplate changing jobs, or will receive a qualified plan distribution because of death or disability, and your qualified plan includes company stock, it would be prudent to check with your tax advisor about various alternatives available to you. All situations will be different, depending on various items such as your length of employment, your age and future employment goals, the percentage of plan assets held as company stock, and the current net unrealized appreciation of the stock. We are here to assist you in making the right choices.

IRS To Investigate Delinquent Filers

The IRS has recently initiated a program to investigate employers who have failed to file the requisite Form 5500 or 5500-EZ for their pension, benefit or welfare plans for plan years ending December 31, 2004 or later. The current program is aimed at employers who have not filed a required return, rather than those who have either filed an incomplete return or were late in filing the return. The IRS has started to send notices to employers, who they believe to be delinquent, 15 months after the original due date of the return in question. Realizing that their records may not be accurate, the IRS will permit employers who have fully met their reporting requirement to respond to the notice in such a way as to allow the IRS to correct its records.

This program is separate and apart from notices generated by the Employee Benefit Security Administration ("EBSA") of the Department of Labor who regularly requests clarification of information on Form 5500.

Failure to file a return can result in substantial penalties for each day the return is late. There is a delinquent filer voluntary compliance ("DFVC") program that caps the penalty on both a "per filing" and "per plan" basis.

If you receive a notice from the IRS regarding your failure to file a Form 5500, you should contact us regarding how to respond. If you, in fact, are delinquent in your filings we can help you to take advantage of the DFVC program in order to reduce your exposure at a reasonable cost to you.

401(k) Safe Harbor Choice - Automatic Enrollment Arrangements - It's Great If You Do It Right

Effective for 2008, 401(k) plans that adopt an **appropriate** automatic enrollment feature **may** be able to avoid annual non-discrimination testing and top-heavy rules. The benefit of avoiding the top-heavy rules is that highly compensated employees can contribute the maximum amount permitted by law to their plan accounts, without consideration of any disparity with the contributions made by non-highly compensated employees.

With an automatic enrollment feature, eligible employees,

who do not elect otherwise, are automatically enrolled in the plan. In effect the employee must "opt out" of deferring income, rather than electing to participate. If the plan sponsor initially invests those deferrals in qualified default investment alternatives ("QDIA"), until the participant makes an affirmative investment choice, the plan sponsor is protected against fiduciary liability arising from its investment choices.

It is commonly believed that by adopting an automatic enrollment feature the plan will eliminate the need for annual testing. But that is not the case. In order to avoid non-discrimination testing and top-heavy rules, the plan must adopt certain **minimum** deferral percentages, which increase over time, and the sponsor is required to make a matching or non-elective contribution to the plan. In addition, employees must be notified within a reasonable time (usually 30 to 90 days) prior to the adoption of an automatic enrollment feature by the plan and annually thereafter. The adoption must be made prior to the beginning of the plan year and remain in force for the entire year, for the plan to avoid the annual non-discrimination testing for that plan year.

The rules for setting up an automatic enrollment mechanism are complex. If you are considering such a plan feature, we can help you amend the plan, investigate QDIAs and notify your employees of the plan amendment on a timely basis.

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