

**CLEAR VISION,
POWERFUL RESULTS**

The Watkins, Meegan, Drury & Company, L.L.C. Tax & Financial Source welcomes feedback and suggestions for articles to assist business leaders and other professionals in meeting their organizations' objectives. If you wish to submit an idea, request use of any information in this issue, or be added to our mailing list, please contact Kevin Jones at (301) 664-8164 or Jason Quinn at (301) 664-8185. Or e-mail us at Kevin.Jones@WatkinsMeegan.com or Jason.Quinn@WatkinsMeegan.com

LOCATIONS

Bethesda, MD
 Vienna, VA
 Annapolis, MD

www.WatkinsMeegan.com

Contents of the **Tax & Financial Source** are general in nature and based on sources which are believed to be authoritative. Specific applications require consideration of all facts and circumstances by qualified professionals. Watkins Meegan will be pleased to provide additional details upon request. No part of this newsletter may be reproduced or utilized in any form or by any means without written permission from Watkins, Meegan, Drury & Company, L.L.C.



Watkins, Meegan, Drury
 & Company, L.L.C.
 Certified Public Accountants
 Business and Financial Advisors

401(k) Automatic Enrollment Plans Boost Participation

When most investments are declining in value, as they have over the last 18 months, many employees understandably do not save for retirement with the same urgency that they would during boom years.

Indeed, employees may delay enrolling in an employer-provided 401(k) plan or stop saving for retirement entirely when the value of their current retirement savings decreases. Nevertheless, investing when asset prices are low, as well as during boom years, is sure to provide a stronger retirement fund than investing only during boom years. To help their employees secure their financial futures and to counteract their natural inclinations to pull back from saving when the stock market is declining, many employers have inserted automatic enrollment and automatic escalation features into their 401(k) plans.

With an automatic enrollment feature, a portion of a new employee's salary is automatically contributed to a 401(k) plan, without the employee needing to elect to participate. While 401(k) automatic enrollment programs allow employees to withdraw from the plan, this option has not decreased enrollment. In addition, many 401(k) plans with an automatic enrollment feature also include an escalation feature,



which gradually increases an employee's contribution the longer the employee remains with the company. Many companies set the initial contribution rate as low as 3 percent of an employee's salary, with 35 percent of companies offering an escalation feature. Thanks to the convenience and ease of automatic enrollment and escalation

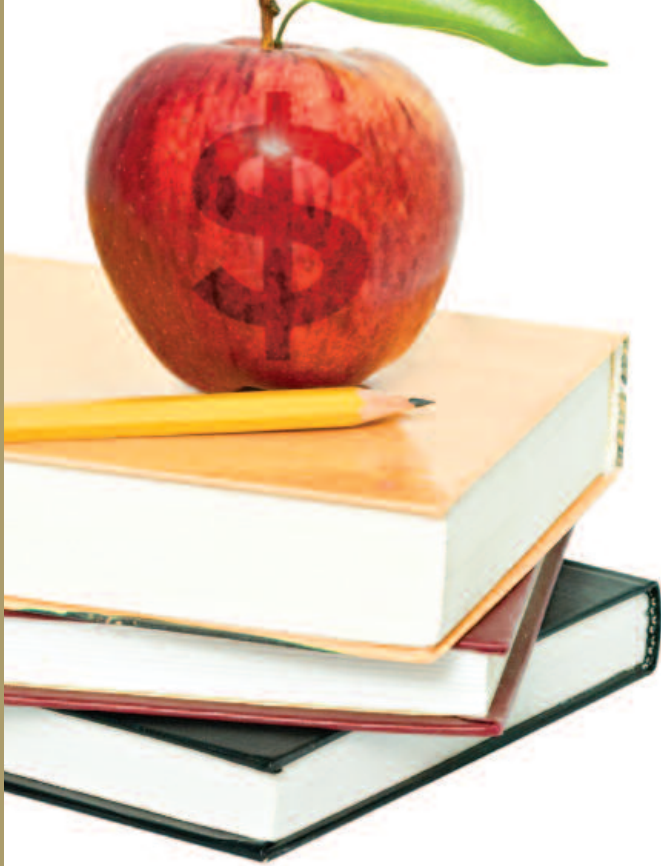
features, many people who ordinarily would not have enrolled in a 401(k) plan are now participating. Research also shows that few people withdraw from their 401(k) plan once enrolled.

Automatic enrollment 401(k) plans not only benefit the employees, but also assist employers with compliance and recruitment efforts,

Automatic enrollment 401(k) plans not only benefit the employees, but also assist employers with compliance and recruitment efforts, among other things.

among other things. For example, every 401(k) plan must pass non-discrimination compliance tests set forth by the IRS. These tests investigate the percentage of salaries deferred into a 401(k) plan for employees at various income levels. To avoid significant penalties, companies must meet certain non-discrimination re-

Continued on page 4



Providing Tax-Free Educational Benefits To Employees

For many companies, a large portion of the total compensation package they offer employees is made up of noncash benefits. Generally, when an employer provides noncash benefits to an employee, the employee is taxed on the fair market value of those benefits, unless an exception to taxation applies.

A common example is employer-provided or subsidized health insurance. Under general tax rules, an employee is required to pay taxes on the value of the health benefits he receives, but the tax law carves out an exception to taxability for employer-provided health benefits, allowing the employee to receive health insurance benefits without increasing his or her tax liability.

economy. When business activity is slow, employees likely have more time to devote to acquiring new skills and have a greater need to enhance their value to their employer. As employees acquire new skills, an employer can use those skills to achieve the goals of the organization and retool as it adjusts to changing market conditions. An employer can provide tax-free education benefits by

in his or her employment. To qualify for the exclusion, an educational assistance program must meet the following requirements:

- * The program must be set forth in a written plan and must be designed to provide educational assistance for the employer's employees exclusively;
- * The program must benefit qualified employees under a classification de-

Tax-free education benefits in particular may be more valuable to both employers and employees in a slowing economy.

An employer also gains from compensating its employees with the use of tax-free benefits instead of additional cash compensation. With the use of tax-free benefits, the employer can provide similar after-tax value to the employee with less out-of-pocket cost to the employer. There are exceptions to taxation similar to the exception for employer-provided benefits throughout the tax law, some of which may be underutilized or may be more relevant under current economic conditions.

Tax-free education benefits in particular may be more valuable to both employers and employees in a slowing

developing and maintaining an educational assistance program or by taking advantage of the tax exclusion for working condition fringe benefits. Both of these approaches have distinct advantages, disadvantages, and requirements for tax-free qualification.

Educational Assistance Program

Under an educational assistance program, an employer can provide tax-free payments for education expenses. These tax-free payments are limited to \$5,250, but they can be provided regardless of whether the program is designed to improve the skills needed by the employee

defined by the employer, provided that classification does not discriminate in favor of highly compensated employees or their dependents;

- * No more than five percent of payments under the plan may be made to shareholders or owners who own more than five percent of the employer;
- * The program may not offer eligible employees a choice between educational assistance and other benefits; and
- * The employer must provide reasonable notification to the employees of the availability and terms of the program.

Education Benefits Provided as a Working Condition Fringe Benefit

An employer is not limited in the value of the educational benefits it can provide to an employee as a working condition fringe benefit. In addition, an employer does not need to meet the documentation, non-discrimination, and notice requirements of an educational assistance program. However, education expenses reimbursed to an employee as a working condition fringe benefit are non-taxable to the employee only if the education expenses incurred by the employee qualify as deductible trade or

business expenses. To qualify as trade or business expenses, education expenses must be paid for an education program that meets the following requirements:

- ✦ It maintains or improves skills required by the individual in his or her employment; or
- ✦ It meets the express requirements of the individual's employer, imposed as a condition of the employer to the retention of the employee in his or her established employment position.

Even if an education program meets one of the above requirements, reimbursed educational expenses do not qualify for

tax-free treatment if the education program either:

- ✦ Is necessary for the employee to meet the minimum requirements for qualification in his or her employment; or
- ✦ Qualifies the employee for a new trade or business.

If your company is considering providing education benefits to its employees, carefully structuring the education benefits program as an educational assistance program or a working condition fringe benefit can provide value to your company and its employees.

TAX CALENDAR

JUNE

Monday, June 15, is the due date for the second quarterly installment of your estimated individual income tax (including any self-employment and alternative minimum tax).

Monday, June 15, is the due date for the second quarterly installment of the 2009 estimated tax for calendar year corporations. For fiscal year corporations, estimated

payments are due on the fifteenth day of the fourth, sixth, ninth, and twelfth months of the taxable year.

Monday, June 15, is the deadline for employers to deposit income, Medicare, and social security taxes withheld from their employees' salaries in May if the monthly depositor rules apply.

JULY

Wednesday, July 15, is the deadline for employers to deposit income, Medicare, and social security taxes withheld from their employees' salaries in June if the monthly depositor rules apply.

Friday, July 31, is the deadline for employers to file quarterly Form 941 for income, Medicare, and social security taxes withheld from their employees' salaries in April, May, and June. If the tax for the quarter has been deposited in full and on time, employers have until Monday, August 10, to file the return.

Friday, July 31, is the deadline for employers to make the second quarterly deposit of FUTA taxes for April, May, and June. Use the Federal Tax Deposit Coupon. However, you are allowed to skip the deposit provided your cumulative liability (first and second quarters) does not exceed \$500.

Friday, July 31, is also the due date for the required Forms 5500 or 5500-EZ, plus the applicable attachments to be filed by the self-employed or by employers who have set up a pension, annuity, stock bonus, profit sharing, or other funded plan that provides deferred compensation for employees. In the case of a fiscal year plan, file these information forms before the last day of the seventh month following the end of the plan year.

To receive a filing extension of two and one-half months, submit Form 5558, Application for Extension of Time to File Certain Employee Plan Returns.

Friday, July 31, is the due date to file Form 720, Quarterly Federal Excise Tax Return, for the second quarter of 2009.





Watkins, Meegan, Drury & Company, L.L.C.

Certified Public Accountants
Business and Financial Advisors

7700 Wisconsin Avenue, Suite 500
Bethesda, MD 20814-3556

PRSRT STD
U.S. POSTAGE
PAID
PERMIT NO. 2375
Southern, MD

IN THIS ISSUE:

- 1 401(k) Automatic Enrollment Plans Boost Participation**
- 2 Providing Tax-Free Educational Benefits To Employees**
- 3 June/July 2009 Tax Calendar**



Printed on recycled paper

WATKINSMEEGAN.COM

401(k) Automatic Enrollment Plans Boost Participation

Continued from page 1

quirements by ensuring that a certain percentage of non-high salaried employees are enrolled in a 401(k) plan. On the other hand, companies that comply with non-discrimination standards reap yearly tax-preferred benefits. By implementing an automatic enrollment feature, companies are likely to have greater success retaining lower salaried employees as participants in a 401(k) plan and therefore have an easier time complying with the applicable regulations.

In addition, adopting automatic enrollment for their 401(k) plans gives companies the opportunity to show that they are interested in the futures of their staff. This is especially useful for recruiting skilled employees and retaining valued staff members. Employees feeling the loss of defined-benefit plans can also breathe a little easier about their retirement accounts, as 401(k) plans with automatic enrollment have similar features as defined-benefit plans, such as professional investment management.

Nonetheless, some employers are concerned about whether the benefits of automatic enrollment are outweighed by additional costs. This is especially true for companies that offer a matching contribution to employees who participate in a 401(k) plan. Companies should keep in mind that employer matching

contributions are tax deductible and therefore can lower their overall tax bill. In addition, the majority of newly participating members of a 401(k) plan are those with low to moderate income levels, so the amount paid in matching contributions is considerably less.

Employers can also reduce costs by carefully choosing the features of an automatic enrollment plan. Many employers set a default contribution percentage that is lower than what the average employee would choose without an automatic enrollment feature, reducing the employer's matching costs. Employers can also reduce their matching costs by automatically enrolling only new employees, not current employees who did not opt into the plan before the implementation of an automatic enrollment feature, allowing the employers to exercise greater control over their matching costs.

Overall, 401(k) plans with automatic enrollment and escalation features provide an opportunity for employers to offer a more attractive compensation package and help employees take the initial step toward a stable retirement. In addition, both employers and employees stand to benefit from the tax benefits of 401(k) plans: employers by more easily meeting non-discrimination requirements and employees by deferring taxation of their income. With many companies reevaluating their compensation packages, now may be the time to consider updating your 401(k) plan features.