AMERICAN RETIREMENT ASSOCIATION
Working for America's Retirement

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American Retirement Association
Comments to the
United States Senate
Committee on Finance

July 17, 2017

The Honorable Orrin G. Hatch
Chairman
United States Senate Committee on Finance
Washington, DC 20515-6200

Dear Chairman Hatch:

On behalf of the over 20,000 members of the American Retirement Association, we respectfully submit the following comments regarding the critically important tax incentives for retirement savings and we thank the Senate Finance Committee for its willingness to receive our insights as the Committee works to overhaul the tax code.

The American Retirement Association is a non-profit professional organization comprised of four premier retirement industry associations - the American Society of Pension Professionals & Actuaries (ASPPA), the ASPPA College of Pension Actuaries (ACOPA), the National Association of Plan Advisors (NAPA), and the National Tax-deferred Savings Association (NTSA). These associations include every type of retirement plan professional – from business owners, actuaries, consultants and administrators, to insurance professionals, financial advisers, accountants, attorneys and human resource managers. While our members come from all corners of the country, and represent every part of the industry, they are all united by their belief in and commitment to the private employer-provided retirement system.

The Incentives for Workplace Retirement Savings are Efficient, Fair, and Unique

The goals of achieving a tax code that is efficient, fair, and increases the financial and retirement security of American families, are goals that the American Retirement Association shares with the Committee. The primary message that we want to convey to the Committee is that the current tax incentives work well to promote good savings behavior for tens of millions of working Americans. If anything, these incentives – for both employers and employees – should be enhanced. At a minimum, any modifications to the current incentives should be evaluated based on whether or not the changes will encourage more businesses to sponsor retirement plans for their employees.

The most important factor in determining whether or not workers across the income spectrum save for retirement is whether or not there is a workplace retirement plan. Over 70% of workers earning $30,000 to $50,000 participate in a plan at work, but less than 5% will save through an IRA on their own.[1] Employer-provided retirement plans – like the 401(k) and similar defined contributions plans – primarily benefit middle class families. Eighty percent of the participants in these plans have an adjusted gross income (AGI) of less than $100,000 per year. 43% of participants have an AGI of less than $50,000.[2]

The tax incentives for retirement savings are unique in that the tax incentive is a deferral, not a permanent exclusion – so every dollar that is excluded from income this year will be included in income in a future year. In fact, one study shows the current methodology overstates the true present value cost by over 50%.[3] The tax incentives for employer-sponsored retirement plans are also unique in that the nondiscrimination rules, coupled with dollar limits on contributions and a limit on the amount of compensation that can be included in determining benefits, assure that the plans do not unduly favor highly compensated employees.

The American Retirement Association supports an improved Saver's Credit because it will help lower paid workers to be able to afford to save. We urge the Committee to modify the 1040 EZ individual income tax form to allow the moderate income individuals who predominantly use that form to claim the Saver's Credit. Additionally, if the credit is directly deposited to retirement savings accounts instead of refunded to the saver, it should also help supplement savings. However, an improved Saver's Credit would not be as impactful without also increasing the availability of workplace retirement plans.

Expanding Workplace Savings Increases Financial and Retirement Security

If increasing the financial and retirement security of American families is the goal, increasing the availability of workplace savings plans is the way to get there. The American Retirement Association was encouraged when the Committee took action in September 2016 on a unanimous bipartisan basis to report the *Retirement Enhancement and Savings Act* (RESA) to the full Senate. RESA proposes many critical changes to the tax code that will both enhance the incentives for and simplify the administration of workplace based retirement savings plans.

By making it easier and more meaningful for a small business to adopt a workplace retirement savings plan, access to saving through payroll deduction will increase. This in turn will help build a secure retirement for the rank and file workers who are 15 times more likely to save through work than on their own in an IRA. The bill expands the current law tax credit for sponsoring a qualified retirement plan and it adds an additional credit to encourage the automatic enrollment of those workers into both new and existing plans. Enhancing these tax credits will expand retirement plans and the number of workers saving.

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[1]Employee Benefit Research Institute (2010) estimate using 2008 Panel of SIPP (Covered by an Employer Plan) and EBRI estimate (Not Covered by an Employer Plan – IRA only)
[2]Estimate of Internal Revenue Service (IRS) Statistics of Income Division (SOI) data for the 2010 tax year extrapolated to 2012 tax year.
[3]Judy Xanthopoulos and Mary Schmidt, *Retirement Savings and Tax Expenditure Estimates* (September 2016) available at: http://www.asppa.org/Portals/2/Comm_2016/16.09%20ARA%20Report%20-%20Retirement%20Savings%20and%20Tax%20Expenditure%20Estimates%20FINAL.pdf

RESA also gives a small business owner more time to make a decision about whether to adopt a qualified retirement plan for the year, since many small business owners do not know their true profits until their tax returns are filed. Another provision would give a small business owner with an existing plan the flexibility to choose a safe harbor plan with generous employer contributions after the beginning of the year. These provisions recognize the real challenges that small business owners face when deciding to provide retirement benefits for their workers and will help business owners make that important decision with more certainty and confidence.

RESA expands retirement plan coverage by allowing two or more unrelated private employers to join a pooled employer retirement plan. Importantly, the legislation requires the provider of such an arrangement to take responsibility for the proper operation of the plan. The clear lines of responsibility prescribed in the legislation give adopting employers – many of which could be small business owners – more security. Additionally, adopting employers will not have to worry about the actions of one participating employer disqualifying the plan for all the other employers. Furthermore, RESA allows retirement plan providers to offer a payroll deduction IRA program with automatic enrollment through a pooled employer plan to small business owners. Pooling unrelated employers together into one plan creates economies of scale that lowers both employer and plan participant cost which will ultimately boost retirement plan coverage in the private sector.

In addition to the provisions in RESA, the American Retirement Association strongly supports a proposal in Chairman Hatch's retirement policy reform legislation introduced in the 113th Congress – *the Secure Annuities for Employee (SAFE) Retirement Act of 2013* – that would further increase access to workplace based retirement plans. The proposal would create a new safe harbor plan design called the Starter 401(k) plan. The Starter 401(k) plan is designed for a small or start-up business that is not currently in a position help fund a retirement plan but wants to help its employees save. The safe harbor would allow workers to save up to $8,000 per year in the plan – currently $2,500 more than individuals can save through an IRA on their own – but $10,000 less than workers can save in a full blown 401(k) plan. Under the new Starter 401(k) plan, the business owner is only required to automatically enroll his or her workers at 3% of pay to be exempted from any employer contribution or nondiscrimination testing requirements.

The American Retirement Association supports proposals that would expand retirement plan access to temporary or self-employed contract workers that make up an ever greater share of the workforce in the so-called modern "gig economy". The tax code should be changed to encourage retirement plan sponsors to open their plans to these workers who would otherwise not be eligible to participate in the retirement plan without jeopardizing the tax qualified status of their plan. It should also be made clear that voluntary participation in the retirement plan by contract workers should not, by itself, change the employment classification of the contract worker.

Increasing the Financial Security and Savings of Millennial Workers

One of the most challenging issues for millennial workers and their families is the heavy student loan debt they carry for many years into their work lives. There is as much as $4 trillion in outstanding student loan debt according to some estimates. Not only does this burden impede their ability to achieve a basic level of financial wellness, it often precludes their participation in their workplace retirement plan, and the matching employer contributions that they would otherwise receive. Those employees miss out on essentially "free money" by not taking advantage of those matching employer contributions.

The American Retirement Association strongly supports a provision included in Ranking Member Wyden's *Retirement Improvements and Savings Enhancements* (RISE) Act discussion draft that addresses this critical issue. The provision would allow employers to make matching contributions to their 401(k) plans on behalf of their employees who made student loan payments, but as a result were unable to afford to also contribute to their 401(k) plan. This provision would encourage everyone to participate in the 401(k) plan and receive meaningful employer contributions to help build up a secure retirement nest egg.

Simplification Not Consolidation

A discussion of simplification often leads to talk of retirement plan "consolidation". The American Retirement Association would caution against tax reform proposals that would consolidate all the different types of defined contribution plans into a single type of plan. That would not be a simplification in our view. It would cause serious disruption since it would force state and local governments and nonprofit organizations to terminate their existing retirement savings plans and procedures and adopt a new program that would be foreign to millions of workers. The distinctions in defined contribution plans for public and non-profit workplace workers were designed to protect traditionally lower paid workers who feel called to serve society. Improved retirement security, and meaningful simplification, will be accomplished through thoughtful modifications to the existing structure – like the above proposals – without wasting resources on cosmetic overhauls that produce pain rather than savings gain.

Pass-Through Income Tax Rates Could Eliminate Incentives for Small Business Retirement Plans

We applaud your committee's work on tax reform. It is long overdue and we offer our support and help. As you formulate your proposal, we bring to your attention a House Republican Blueprint proposal capping the maximum tax rate on active business income at 25% and wage income at 33%. We expect small business owners to characterize most of their income as active business income to take advantage of the 25% tax rate and forgo contributions to a retirement plan which will be eventually taxed at 33% as deferred wages. We estimate that over 300,000 retirement plans (about 50% of the retirement plans in the United States) sponsored by small business pass-through entities affecting 24 million non-owner employees will terminate their retirement plans to take advantage of the 25% tax rate on active business income. Deferring wages in the form of contributions to a retirement plan which will be taxed eventually at 33% under the House Republican Blueprint results in a 10% penalty on the small business owners for saving in a retirement plan rather than paying out profits currently. We look forward to working with the Committee to solve this problem and continue promoting retirement plan sponsorship by small businesses.

Integrating Health and Retirement Savings

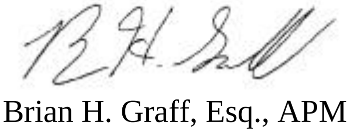
As the Committee expands health savings accounts (HSAs), we propose a simple legislative fix that will boost adoption of HSAs, lower participant's investing costs and coordinate health and retirement savings decisions. Today, health savings accounts are largely treated separately from retirement savings accounts and hence employees do not receive holistic financial advice and access to lower cost retirement plan investments. Health experts tell us a healthy Medicare eligible couple age 65 will need at least $260,000 in savings for health care in retirement.

To address this need, we propose modifying the health savings account rules to give plan sponsors the option of offering a health savings account in their 401(k) plan. We call it the "HSA side car" proposal. A similar provision allowing plan sponsors to add an IRA to their 401(k) plan was passed by Congress in 2001.

Integrating HSAs into the 401(k) helps employees in three major ways. First, participants will get access to lower cost investment options offered in their 401(k) plan. Second, the proposal will give employees access to holistic financial education and planning tools so they can allocate their savings across their health and retirement accounts to best meet their family needs. Third, the HSA side car proposal will create more HSA accounts because opening an HSA will now be linked to retirement plan enrollment. A significant percentage of high deductible health plan users neglect to open a health savings account after enrolling in their health plan. And last, the HSA side car proposal preserves all the unique characteristics of HSAs under current law to keep things simple.

The American Retirement Association looks forward to working with the Committee to simplify the rules and regulations surrounding the tax incentives to save for retirement through workplace based retirement plans. Thank you for this opportunity to participate in this important effort.

Sincerely,



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