Washington Update

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BEAM
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Craig P. Hoffman

Craig P. Hoffman of Jacksonville, FL, is the General Counsel and Director of Regulatory Affairs for the American Society of Pension Professionals and Actuaries ("ASPPA"). He previously served ASPPA as President, Co-Chair of the Government Affairs Committee and Co-Chair of the Political Action Committee. Prior to joining ASPPA, Craig served as General Counsel for SunGard Relius. Mr. Hoffman was an expert speaker at the National Summit on Retirement Savings, served as a charter member of the first IRS Advisory Committee on Tax Exempt and Governmental Entities, is a Fellow in the American College of Employee Benefits Counsel and received the 2008 Lifetime Achievement Award from the National Institute of Pension Administrators (NIPA). Mr. Hoffman is a frequent speaker at industry meetings and serves on the editorial boards of several pension journals.

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What We Will Cover

- The Tax Reform in 2015
- The "SAFE" Act of 2013

Tax Reform in 2015

Tax Reform

- During 2014, Max Baucus (D-MT), former Chair of the Senate Finance Committee, and Dave Camp (R-MI), former Chair of the House Ways and Means Committee, lobbied their colleagues on Capitol Hill to consider enacting comprehensive tax reform during the current the last term of Congress (which ended in 2014).

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Tax Reform

- As a result of these retirements and the mid-term elections, there is now new leadership at the committees in Congress that have jurisdiction over the Tax Code:
  - Orrin Hatch (R-UT) is now the Chair of the Senate Finance Committee.
  - Paul Ryan (R-WI) is now chair of the House Ways and Means Committee.

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Tax Reform

- Tax Reform high on the GOP Congressional agenda
- Very LIMITED window of time to pass reform: It would have to be done in early 2015, before the 2016 election year and presidential campaigning begins.
- Many GOP legislators, both conservative and moderate are calling for it
- But tax reform means different things to different people

Tax Reform: House

- Paul Ryan, has already been preparing the way for tax reform in 2015 with a focus on:
  - Lowering the baseline for tax revenues
  - Implementing dynamic scoring for tax legislation.
- "*Typically tax reform in history has been led by presidents, '86 is a perfect example," he said, referring to the 1986 tax overhaul achieved by President Reagan and a Democratic-led House. "That won't be the case this time if we get it in the next two years…. it will have to be led by Congress, and we'll see what we can get."*

Tax Reform: Senate

- *Senator Mitch McConnell , Senate Majority Leader*...
- "We're going to want to see what kind of things we might be able to agree on with the President…I'll give you a couple of examples where there may be areas of agreement: comprehensive tax reform and trade agreements."
- "The president has indicated he's interested in doing tax reform — we all know that having the highest corporate tax rate in the industrialized world is a job killer. He's interested in that issue and we are too."

Tax Reform: Senate

- Senator Orrin Hatch on his work for federal tax reform has sponsored **S. 1270**, the SAFE Retirement Act of 2014, Title II of which adopts ASPPA proposals
- In September 2014: "*One of the major goals of comprehensive reform should be to fundamentally change this system and anything we do in the interim should move us further down that path.*"

Tax Reform: The President

- President Obama has outlined a number of tax reform proposals in conjunction with his State of the Union address last week. Among them:
  - Taxing unrealized capital gains at death;
  - Raising the capital gains tax rate to 28%;
  - Limiting the exclusion for elective deferrals to that provided to those in the 28% tax bracket; and
  - Placing a cap on an individual's total tax favored retirement savings equal to approximately $3,400,000. (The limit is based on the actuarial equivalent of a $210k annuity at age 62 but floats with federal interest rates).

Other Leaders on Tax Reform

- **Sen. Rob Portman**. "*Our onerous and outdated tax code continues to force businesses to leave the U.S., taking American jobs with them. We can and must reform our tax code again so that we keep businesses and jobs here at home and provide relief to all Americans.*" He also said: "*We can't wait for the next president. We can't wait for the next Congress. We need to act and act now.*"

- **Sen. Rand Paul**: Tax reform should lead GOP's 2015 priorities in a Republican-led Senate. "*We could have a boom like we haven't seen in years*," Paul said on CBS's Face the Nation

Vehicle for 2015 Tax Reform

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- Bipartisan bill that the President would sign;
- GOP goes in 100% on a bill and forces President Obama to veto it; or
- Include in "Budget Reconciliation," which only lasts 10-years, but can pass the Senate with just 51 votes, although still subject to a potential Presidential veto.

Threats and Opportunities from Tax Reform

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Tax Reform

- Dave Camp, before leaving Congress, released his the Tax Reform Act of 2014.
- This, and all other legislation that had not been passed by the last Congress when it adjourned in December, lapsed and will need to be reintroduced in the new Congress.
- Although Mr. Camp is now gone, it is possible that some of what he proposed could find its way into a new tax bill as evidenced by President Obama's tax proposal unveiled last week.

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Camp Tax Reform Proposal

- Revenue Raisers in Camp Proposal:
  - Large employers (more than 100 ee's) must add a Roth option and pre-tax elective deferral contributions would be limited to 50% of the IRC § 402(g) limit (including catch-up), remainder must be contributed on a Roth, after-tax basis. (Raises $143.7 billion).
  - 10 year freeze on cost of living increases to qualified plan contribution and benefit limits (Raises $60.1b with respect to the IRC §402(g) freeze and $1.8 with respect to the IRC §415 freeze).

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Camp Tax Reform Proposal

- Revenue Raisers (cont'd):
  - Eliminates the use of the "stretch" IRA as a distribution option at death, instead requiring a total distribution within 5-years of death (expected to be in the President's budget proposal.
  - Exception available for "eligible designated beneficiary," i.e., a spouse, minor child, disabled dependent or anyone else no more than 10 years younger and certain binding annuities in effect on date of enactment.

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Camp Tax Reform Proposal

- Revenue Raisers (cont'd):
  - Pre-tax IRA contributions eliminated; only Roth IRAs would be permitted and there would be a 10-year freeze on cost of living increases. (Raises $16.7B)
  - Prohibits re-characterization of Roth IRA contribution or Roth conversion back into a traditional IRA by due date of individual's tax return. (Raises $.4B)
  - No exclusion for unrealized appreciation on employer securities. (Raises $.9B)

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Camp Tax Reform Proposal

- Revenue Raisers (cont'd):
  - Double Taxation on DC Plan Contributions
    - The bill reduces marginal tax rates to 10% and 25%, but adds a new 10% additional income tax for earnings in excess of $400k ($450k joint) of **modified** adjusted gross income (AGI).
    - AGI for this purpose is modified by INCLUDING various items of compensation that would not otherwise be subject to income tax including all pre-tax contributions to qualified defined contribution plans (both employer and employee) but not defined benefit plans.
    - The net effect is to the to double-tax plan contributions, i.e. at 10% when they go in and again at normal income tax rates when they are distributed. (Revenue not broken out)

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Other Camp Provisions

- "Leakage" provisions:
  - 1st time home purchase and post-secondary education would no longer qualify for an exception to the 10% penalty on early distributions. (Raises $.3B)
  - The 6-month contribution suspension after a 401(k) hardship distribution would be eliminated.
  - Rollover period for loan offset distribution would be extended until the due date of the tax return for the year of the distribution.

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Tax Reform

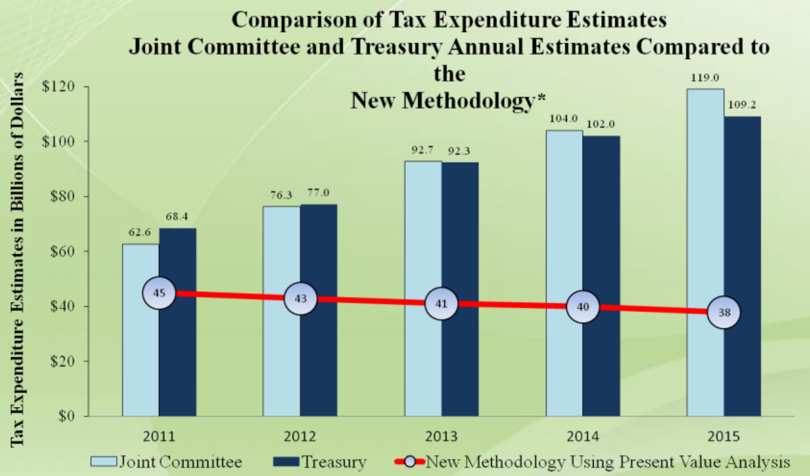
- Other possible tax reform pension revenue raisers:
  - Simpson-Bowles - 20/20 Proposal.
  - Obama - 28% Cap on Tax Benefits of Pre-tax contributions.
  - Obama - $3.4 Million Lifetime Cap on Qualified Retirement Savings.
- Remember, TRA '86 – Cut the 401(k) Limit by 70%.

Tax Expenditures

JCT August 2014 estimates
https://www.jct.gov/publications.html

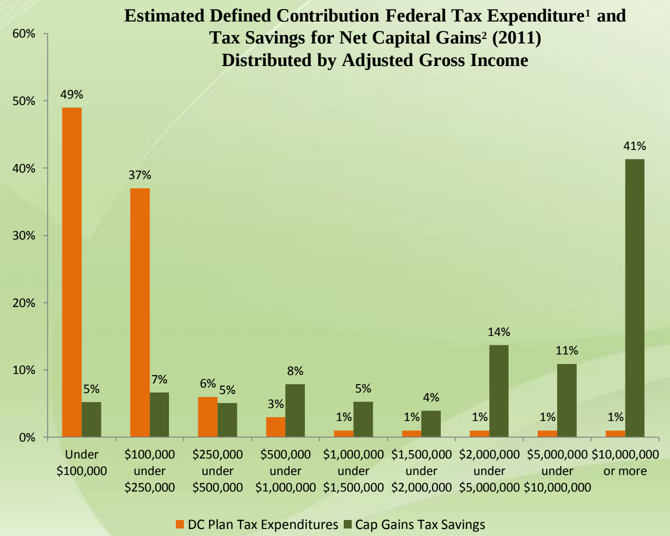
Billions

Tax Expenditure	2015	2016	2017	2018
Employer-provided health exclusion	$150.6	$155.8	$163.6	$172.0
Home mortgage deduction	74.8	81.6	87.8	93.2
Defined contribution plans	62.3	81.2	98.9	111.7
Defined benefit plans	41.3	50.4	61.2	69.4
Self-employed pension plans	8.7	10.0	11.4	16.2
Total ER-provided retirement plans	**112.3**	**141.6**	**171.5**	**197.3**
Traditional IRAs	12.8	13.9	15.0	16.0
Roth IRAs	5.5	6.1	6.6	7.2



* The new methodology estimates the tax benefit of the deferral and inside buildup, in present value terms. The Joint Committee and Treasury estimates rely on cash-flow analysis.

Upside Down?



[1] Estimated - participants with access and retirees with account balances. See ASPPA, "Distributional Analysis and Pension Tax Provisions," (2014)

[2] Tax differential between ordinary Income and capital gains rates. Estimates based on IRS SOI, Individual Income Tax Returns

Retirement Security is What Americans Worry About Most

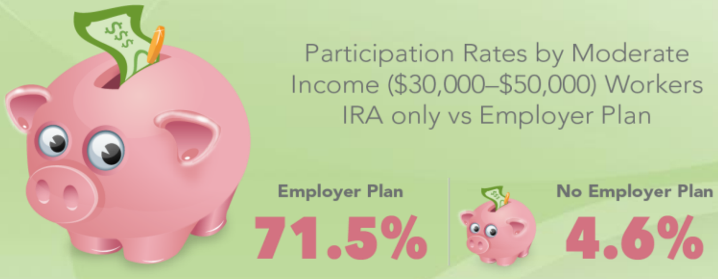
Financial Concerns	18-29	30-49	50-64	65+
Not enough money for retirement	50%	70%	68%	37%
Not paying for children's college	46%	55%	23%	8%
Not affording serious medical	52%	54%	58%	43%
Not paying off debt	47%	45%	42%	20%
Not maintaining living standard	52%	44%	52%	41%
Not paying normal healthcare	35%	37%	46%	33%
Not paying normal monthly bills	40%	33%	38%	29%
Not paying rent or mortgage	40%	30%	31%	20%
Not paying credit card minimums	14%	17%	18%	15%

* Gallop, Economy and Personal Finance Survey, ranked by 30-49 year olds (April 2014)

Tax Reform

Myth – Workers will save for retirement without a workplace plan.

The Middle Class is 15 Times More Likely To Save At Work



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What to Expect

- Reforming the Tax Code still remains a hot issue.
- Despite the President's proposals being "DOA," it still may be one of the few areas that a bipartisan bill could pass Congress.
- Reform of the corporate Tax Code provisions is the main driver.
- If tax reform is going to move forward, the "sweet spot" for doing so will be in 2015 before the 2016 presidential election cycle gets into full swing.
- ASPPA will continue to lobby to ensure that tax reform does no harm to the private pension system.

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Opportunities in Tax Reform

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THE "SAFE" ACT OF 2013

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SAFE Act of 2013

- On July 9, 2013, Senator Orrin Hatch (R-Utah), ranking member on the Senate Finance Committee, introduced the Secure Annuities for Employee Retirement ("SAFE") Act of 2013 (S. 1270).
- The bill is divided into 3 Titles:
  - Public Pension Reform
  - Private Pension Reform
  - Individual Retirement Investment Advice Reform

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PRIVATE PENSION REFORM

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SAFE Act of 2013

- The Act proposes a new "Starter 401(k)" in the form of a deferral-only safe harbor plan.
  - Elective deferrals only, no other contributions.
  - Employer must not have had any other qualified plan during the plan year of initial adoption.
  - Mandatory auto enrollment of between 3%-15%.
  - Maximum contribution of $8,000 (other than catch-up).
  - Normal catch-up limits for those eligible.
  - Exempt from top-heavy requirements.
  - No Form 5500 required.

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SAFE Act of 2013

- "Secure Deferral Arrangement" - new 401(k) automatic enrollment safe harbor alternative.
  - Auto enrollment % would begin between 6%-10%, rise to at least 8% in the second year and go to at least 10% thereafter.
  - NHCE matching contributions required equal to 50% on the first 2% of pay plus 30% match on deferrals between 2% and 10% of pay (for a maximum of 3.4%).
  - Exempt from top-heavy and ADP/ACP testing.
  - Tax credit equal to 10% of the NHCEs' contributions, to a max of $10,000 per year for the first 3 years.

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SAFE Act of 2013

- Multiple Employer Plans ("MEPs") -
  - Repeals the "commonality" requirement for DC MEPs to be treated as a single plan if:
    - Employer retains fiduciary responsibility for selecting and monitoring the MEP's designated provider, the named fiduciary if different from the MEP's designated provider; and the investment and management of plan assets attributable to the their employees if not delegated to another fiduciary.
    - On termination of participation, the participating employer is not subjected to unreasonable fees, penalties or restrictions

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SAFE Act of 2013

- Multiple Employer Plans ("MEPs") cont'd-
  - Repeals the "the one bad apple" rule on plan disqualification for MEPs that satisfy the commonality requirement and other MEPs if:
    - The MEP has "designated plan provider";
    - The "designated plan provider" registers with the IRS and consents to IRS audits; and
    - The "designated plan provider" is designated under the plan as the person responsible to perform the necessary administrative duties (as determined by IRS regulations.

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SAFE Act of 2013

- Other changes in SAFE include:
  - Repeal of the top-heavy requirements.
  - Permits forfeitures to be used to fund safe harbor type contributions such as QNECs and QMACs.
  - Permits direct rollover of insurance contracts to an IRA.
  - Allows Qualified Pre-retirement Survivor Annuity notice to be given ONLY at initial eligibility as part of SPD.
  - Allows DB minimum participation requirements to be satisfied through 7.5% DC plan contribution

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SAFE Act of 2013

- Other retirement plan changes cont'd:
  - 403(b) custodial accounts may be treated as IRA on termination of the plan.
  - Directs the DOL to modify the participant disclosure regulations to permit the use of a "blended" benchmark for DIAs that use a "mix of asset classes" in comparative investment chart.
  - Exempts from RMD rules amounts invested in certain types of commercial annuity contracts which may not exceed 25% of the participant's account.
  - Directs the expansion of EPCRS to IRAs and to allow self-correction of loan errors.

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SAFE Act of 2013

- Other retirement plan changes cont'd:
  - Would permit as the default electronic communication of any IRS or DOL required notice
  - Would tie the deadline for providing updated SPDs to the plan's remedial amendment cycle.
  - For purposes of the small plan exemption from the independent audit requirement, only participants with accrued benefits would be counted.
  - Amends IRC §401(b) to allow "required amendments" to be adopted during the remedial amendment cycle and discretionary amendments by the due date of the applicable year's tax return

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INDIVIDUAL RETIREMENT INVESTMENT ADVICE REFORM

(TITLE III)

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Investment Advice Reform

- In 1978, an Executive Order, that was later codified into law, transferred jurisdiction from the IRS to the DOL over application of the prohibited transaction rules of ERISA.
- Title III of the SAFE Act returns that jurisdiction back to the IRS.
- It would also provide joint jurisdiction for IRS and DOL with respect to the application of the prohibited transaction rules to retirement plans.

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Questions ???