The Retirement Plan Simplification and Enhancement Act of 2013

Expanding Coverage and Increasing Retirement Savings

Modify the Current Automatic Enrollment Safe Harbor - The bill would revise the automatic enrollment safe harbor to remove the cap that required automatic escalation of employee deferrals go no higher than 10 percent of employee pay.

Establish a New Automatic Enrollment Safe Harbor. Under the current law automatic enrollment safe harbor, the automatic deferral must be at least three percent of salary during the first year. Some have argued that this provision has resulted in employers setting the deferral amount at three percent in the first year (even though they could set it higher), when most Americans should be saving more to ensure a financially secure retirement. Therefore, the legislation would establish a new automatic enrollment safe harbor - ***in addition to*** the existing the existing automatic enrollment safe harbor. Some of the features of the new safe harbor include:

- The minimum default level of contribution would be 6% in the first year, 8% in the second year, and 10 % in all subsequent years.
- The employer would be required to make matching contributions equal to 50 cents on the dollar for the first 2% of pay and 30 cents on the dollar for the next 8% of pay.
- A special tax credit would apply to small employers (i.e., employers with 100 or fewer employees) that adopt this safe harbor equal to 10% of the total amount of employer and employee contributions under the safe harbor on behalf of all eligible nonhighly compensated employees, up to a maximum annual credit of $10,000. The credit would apply to the first three full years the arrangement is in effect.
- Similar to the existing safe harbors, this new safe harbor arrangement would be exempt from nondiscrimination and top-heavy testing.

Amend DC Elective Deferral Coverage Rules for Long-term Part-time Workers - Under current law, employers generally may exclude part-time employees (employees who work less than 1,000 hours per year) when providing a defined contribution plan to their employees. As women are more likely than men to work part-time, these rules can be quite harmful for women in preparing for retirement. The bill will require employers maintaining a 401(k) plan to have a dual eligibility requirement under which an employee must complete either a one year of service requirement (with the 1,000-hour rule) or three years of service where the employee completes at least 500 hours of service.

Amendment to Top Heavy Rules to Expand Coverage - In a top heavy plan, any participant that has completed an hour of service must receive a top heavy contribution – even if the employer allows employees to enter the plan before the law would require they be eligible to participate. As a result, small employers are discouraged from allowing early entry into 401(k) plans. The bill would allow employers to test participants that have not met the minimum statutory age and service requirements separately for determining required top heavy contribution requirements.

Enhancements to the Saver's Credit - The bill would:

- Make the Saver's Credit refundable. The bill also would incent taxpayers to pay the credit into the taxpayer's retirement account by doubling the credit for such action. For example, if a taxpayer is eligible for a $400 credit but agrees to pay the credit to his/her retirement account, he or she will instead be eligible for an $800 credit.
- Expand the number of families and individuals who would be able to use the full Saver's Credit of 50 percent by just about doubling the existing income limits for the full credit. The new limits would be set at adjusted gross incomes of $32,500 for individuals and $65,000 for couples. It also creates a phase out range for those earning slightly above those limits.
- Establish the maximum amount of an employee's contribution that is eligible for the Saver's Credit at $500 for an individual and $1,000 for a couple. These contribution limits will increase by $100 and $200, respectively, each year until 2023 and after that time the limits will increase with inflation.

Retirement Readiness Checklist - The bill would require the Social Security Administration to prepare a retirement readiness checklist to be distributed annually to Americans with their Social Security statements. The checklist would include Q&As that individuals should consider in preparing for retirement, such as what annual income the individual will need in retirement and how many years the individual will live in retirement.

Additional Time to Adopt a Qualified Plan - Under current law, Revenue Ruling 81-114 provides that a deduction for qualified plan contributions is not allowed for a prior taxable year if the plan is not established by the end of that taxable year. Accordingly, in order to be able to make deductible contributions for a taxable year, an employer must formally adopt a new qualified retirement plan by the end of such year. However, an employer can establish a Simplified Employee Pension (SEP) plan as late as the due date of the employer's tax filings, including extensions. The proposal would permit an employer to adopt a qualified plan up to the due date (including extensions) for filing its tax return for the employer's taxable year in which the first plan year ends.

Frequently, the employer's profitability for a year will be a major factor in his or her decision to establish a plan, and reliable information on such profitability is often not available until after the close of the employer's taxable year. The proposed change will allow employers to consider the adoption of a qualified plan, or addition of non-elective contributions to an existing plan, when final results for a year are available, thereby expanding coverage and employer-funded retirement benefits. The extension of time to adopt a qualified plan will coordinate with the maximum time that an employer can make a deductible contribution with respect to a plan year. This rule also would place the timing for adopting qualified plans on par with the adoption of SEPs, enabling an employer to opt for an ERISA-covered program to cover its employees in lieu of adopting a non-ERISA covered SEP program.

Encouraging Small Businesses to Enter and Remain in the Employer Retirement Plan System

Enhancement of the Start Up Credit - Current law offers a small business that adopts a new qualified plan a tax credit, which can apply for up to three years, equal to the lesser of (1) 50 percent of the employer's start-up costs, or (2) $500. The bill would increase the $500 amount to $5,000.

Strengthen Multiple Employer Plans - To address the low incidence of qualified plans among small businesses, Congress has authorized employers to band together and offer multiple employer plans. But the risk that a noncompliant employer within the plan will taint the entire plan has stymied the expansion of such plans. The bill directs Treasury and DOL to issue administrative guidance addressing this issue for multiple employer plans.

Preservation of Income

Study of Spousal Consent for Distributions from Defined Contribution Plans – Under the bill, GAO is required to conduct a study of the feasibility and desirability of extending the spousal consent requirements to defined contribution plans and to report the results, with recommendations for legislative changes, to the House Committees on Ways and Means and Education and Workforce and Senate Committees on Finance and Health, Education, Labor and Pensions.

Administration of Joint and Survivor Annuity Rules - One of the reasons that defined contribution plans do not provide guaranteed lifetime income options is that if they do so, the plan must then comply with the statutory requirements relating to joint and survivor annuities. The J & S rules impose administrative requirements involving notifications to spouses, waivers by spouses, and prescribe the form and amount of spousal benefits. The bill provides that where the plan sponsor and the annuity administrator have agreed that the annuity administrator will be a fiduciary responsible for administration of the joint and survivor annuity rules, enforcement actions for failure to comply with the joint and survivor annuity rules may only be maintained against the annuity administrator, provided that the plan sponsor or administrator has prudently selected and retained selection of the annuity administrator. This provision is applicable only to administration of the joint and survivor annuity rules under defined contribution plans.

Clarify the law with respect to the availability of distribution options. Under the bill, Treasury is directed to clarify its regulations with respect to the treatment of investment options that provide employees with rights to distribution options, such as annuity contract investments or guaranteed minimum withdrawal benefits. Under the clarified regulations, such options could be limited to employees who have attained specific age and/or service conditions, in the same manner as it is clearly permissible to apply such conditions with respect to the distribution options themselves.

Rollover of Insurance Contracts to IRAs - Code section 408(a)(3) currently prohibits IRAs from holding life insurance contracts. In contrast, qualified retirement plans under Code section 401(a) and tax-sheltered annuities under Code section 403(b) can hold life insurance contracts, subject to certain limitations on the amount of insurance that can be maintained. The bill amends the Code to provide that, if an eligible rollover distribution from a qualified retirement plan or tax-sheltered annuity includes a life insurance contract that met the incidental death benefit requirements at the time of distribution from the qualified plan, the contract can be rolled over to and held by an IRA. Under no other circumstances would an IRA be permitted to hold life insurance contracts.

In-Plan Lifetime Income Options Portability - One of the concerns plan sponsors have regarding offering a lifetime income option, such as guaranteed minimum withdrawal benefits, in their defined contribution retirement plans relates to portability. To address this issue, the bill would treat a defined contribution plan's discontinuance of a lifetime income option as a distributable event, allowing affected participants to rollover the entire amount invested in the lifetime income-related investment to an IRA that provides the same or similar lifetime income protection. By allowing participants to rollover their accounts if a lifetime income option is discontinued, (for example, by change of plan provider or otherwise), the participants are generally able to preserve their guarantee feature. Otherwise, the participants will have paid the guarantee fee and potentially will receive no protection.

Creation of a Lost Pension Plan Registry - The bill would create a Lost Pension Plan Registry, an online listing of ongoing private retirement plans and sponsors that have changed their name or address, or have been merged, acquired, divested or otherwise changed their corporate structure. The Lost Pension Plan Registry would be established by the PBGC to supplement its "Missing Participants Program." The MPP locates lost participants in terminated plans who the PBGC has been unable to locate, usually because they were not found by plan sponsors prior to termination. The Registry would be added to the MPP's "Internet Missing Participant List." Plan administrators would be required to include information about changes in names, addresses, and corporate structure during a year on a new schedule to the annual Form 5500 that would be forwarded by the IRS to the PBGC. The requirement would be mandatory only for future changes but plan sponsors and administrators would be encouraged to voluntarily provide this information to the PBGC.

The PBGC would post a list of "lost plans" with current contact information on its website. This would make it possible for retirees who left their former employers many years ago to locate their lost plans and apply for their benefits. It would also be helpful to employers who now have to hire firms to find "lost participants" to meet the requirement that they start paying benefits at age 70 1/2.

Simplification and Clarification of Qualified Retirement Plan Rules

Exception from RMD Rules when Retirement Savings Does Not Exceed $100,000. Under current law, participants are generally required to begin taking distributions from their retirement plan at age 70 1/2. The policy behind this rule is to ensure that individuals use their retirement savings during their lifetime - and not use their retirement plans for estate planning purposes to transfer wealth to beneficiaries. However, for most Americans, unfortunately, they do not have large retirement account balances and will need their retirement savings during their lifetimes. Furthermore, the age 70 1/2 was never indexed and so with Americans living longer, it doesn't seem to make good policy sense to require most people to begin spending down their retirement savings at age 70 1/2 when they could live another 20 years or more. The bill would provide that participants with a balance in their retirement plans of less than $100,000 on their 70 1/2 birthday are not required to comply with the RMD rules.

Expand EPCRS - Because of the ever growing complexity of plan administration due to continued Internal Revenue Code changes, the bill would expand the correction system to allow more types of errors to be corrected internally through self correction and a simplified IRS Voluntary Correction Program (VCP) submission program with reduced VCP fees. For example, the bill would allow for correction of many plan loan errors through self correction. These are a frequent area for error and it can be burdensome to go to the IRS to correct a single loan error. Typically, correcting a loan error for a loan amount would be less than the cost of the VCP fee.

Clarify that Forfeitures Can Fund Safe Harbor Contributions - Under Code section 401(k), safe harbor contributions must be nonforfeitable. Forfeitures can be used to reduce employer contributions and/or to pay for a plan's administrative expenses. The bill clarifies that safe harbor contributions must be nonforfeitable only at the time they are designated as safe harbor contributions, and therefore, forfeitures can fund safe harbor contributions.

PBGC - ERISA 4062(e) proposal – Under the bill, a 4062(e) "event" would only occur if an employer maintaining a defined benefit plan has both (1) a facility shutdown whereby activities at a facility actually cease (and are not simply moved to a different facility, for example), and (2) a layoff of over 20% of the employer's workforce, determined on a controlled group basis. The bill would also direct the PBGC to enforce the law in accordance with the new facility shutdown rule as of the date of enactment of this bill.

Church Plans Clarification - Several recent legislative and regulatory enactments have resulted in uncertainty on a number of issues impacting church pension plans and the bill would clarify the treatment of church plans on these issues. The legislation: (1) clarifies that certain non-church controlled organizations (e.g. universities and nursing homes) may be disaggregated for control group purposes; (2) provides that defined contribution limits do not apply to 403(b) grandfathered defined benefit plans; (3) allows church plans offering auto-enrollment have the benefit of preemption of certain state laws; (4) provides for church plan transfers and mergers; and (5) clarifies that tax-exempt status is not impacted in the case that a collective investment vehicle includes commingled non-plan assets.

Frozen DBs Proposal - In the last several years, many companies have frozen their defined benefit pension plans. Although this bill contains proposals that are intended to reverse that disturbing trend, it is also important to address the issues that arise with respect to existing frozen plans and the plans that freeze in the future. Such freezes have the greatest adverse effect on older employees, who generally have the largest accruals under defined benefit plans and have the least amount of time to adjust to a change in the plan. For that reason, many companies either (1) do a "soft freeze" under which accruals continue for existing employees, or (2) provide higher company contributions to a grandfathered group of older employees under the company defined contribution plan. The problem with both of these approaches is that, over time, they will in many cases violate the Treasury rules prohibiting discrimination in favor of highly compensated employees. This is true because at many companies turnover is higher among lower paid employees, so that over time the grandfathered group becomes disproportionately higher paid. This is an inappropriate result that precludes many companies from protecting and helping older workers. Under the bill, if a grandfathered group of employees is a nondiscriminatory group when it is first formed, it will be treated as a nondiscriminatory group permanently (unless, of course, the group is modified by plan amendment). This would allow companies to protect older workers.

Review by Treasury and Labor of Reporting and Disclosure Requirements - The bill would direct Treasury, DOL and PBGC to review the current ERISA and PPA reporting and disclosure requirements and make recommendations to consolidate, simplify, standardize and improve such requirements.

Consolidation of Employee Notices - Over the years, Congress has created a number of notices that must be provided to participants in 401(k) and similar defined contribution plans. These notices must be provided upon enrollment and annually thereafter, with the precise timing requirements varying slightly in the implementing regulations. These notices include:

- Qualified default investment alternative notice. *(ERISA §§ 404(c)(5)(B), 514(e)(3))*: Explains how a participant's account will be invested in the absence of an affirmative election.
- Participant fee and investment disclosure. *(DOL Reg. § 2550.404a-5)*: Informs participants who have the right to direct investment of their account about the plan's fees and the investments on the plan menu.
- Safe harbor notice. *(Code § 401(k)(12)(D))*: Informs participants that the employer will make matching or nonelective contributions to satisfy the Code's nondiscrimination testing safe harbor.
- Auto enrollment safe harbor notice. *(Code § 401(k)(13)(E))*: Informs participants that the employer will utilize auto enrollment, auto escalation and matching or nonelective contributions to satisfy the nondiscrimination testing safe harbor and about the employer contributions and the auto enrollment features.
- Permissive withdrawal notice. *(Code § 414(w)(4))*: Informs participants in auto enrollment plans about their right to stop automatic contributions and withdraw them within 90 days.

The bill would:

- Direct the Secretaries of Labor and the Treasury to adopt final regulations within 18 months of enactment providing that a plan may, but is not required to, consolidate two or more of the notices required under ERISA §§ 404(c)(5)(B) and 514(e)(3), Internal Revenue Code §§ 401(k)(12)(D), 401(k)(13)(E), and 414(w)(4), and 29 C.F.R. § 2550.404a-5 into a single notice and/or consolidate such notices with the summary plan description or summary of material modifications described in ERISA § 104(b), so long as the combined notice, SPD, or SMM includes the required content, clearly identifies the issues addressed therein, and is provided within the time required by law.

- Amend ERISA §§ 404(c)(5)(B) and 514(e)(3) and Internal Revenue Code §§ 401(k)(12)(D), 401(k)(13)(E), and 414(w)(4) to provide that the annual notices must be furnished at least annually within any 12-month period without regard to the plan year

Making Target Date Disclosure More Effective - The Department of Labor's new participant disclosure regulation requires that each designated investment alternative's historical performance be compared to an appropriate broad-based securities market index. Thus, for example, if the plan offers an equity fund on its menu, the plan will show participants the 1-, 5-, and 10-year returns of the equity fund and the returns of an appropriate index like the S&P 500, because the S&P 500 represents an index of the same asset class. Unfortunately, the rule does not adequately address increasingly popular investments like target date funds that include a *mix* of asset classes.

Target date funds offer a long-term investment strategy based on holding a mix of stocks, bonds and other investments that automatically changes over time. Comparing a target date fund to an index consisting solely of equities or bonds is *inherently* misleading because neither of these accurately reflects the risk/return profile of a target date fund. In fact, DOL has acknowledged that benchmarks that do not reflect the proportional holdings of the investment will mislead 401(k) savers. Further, the rule as written would allow a comparison solely against an index like a bond index that will make the target date fund appear to significantly beat its benchmark over time. DOL's benchmarking rule is based on a longstanding similar requirement under the securities laws for mutual fund prospectuses, which generally works well—but not in this circumstance.

In the preamble to the final regulation and a related Field Assistance Bulletin, DOL has indicated that a plan could provide the required benchmark and *additional* benchmarks in the disclosure, but this simply serves to further confuse participants and unnecessarily lengthen the disclosure.

Under the bill, DOL is directed to modify its regulations so that an investment that uses a mix of asset classes can be benchmarked against a blend of broad-based securities market indices, provided (a) the index blend reasonably matches the fund's asset allocation over time, (b) the index blend is reset at least once a year, and (c) the underlying indices are appropriate for the investment's component asset classes and otherwise meet the rule's conditions for index benchmarks. (These conditions are important to prevent the blended benchmark from being manipulated.) This change in the disclosure rule will allow better comparisons and aid participant decision-making. This change, including the conditions, would also apply to balanced funds and other asset allocation investments.

Permit Non-Spousal Beneficiaries to Roll Assets to 457, 401(k) and 403(b) Plans - The Pension Protection Act of 2006 (PPA) permitted non-spousal beneficiaries to roll assets they obtain as a beneficiary to an IRA but not to their 457(b), 401(k) or 403(b) accounts. EGTRRA acknowledged that the consolidation of retirement assets is valuable to those with multiple retirement savings accounts. It would be very beneficial to permit non-spousal beneficiaries to consolidate their beneficiary assets in their 457(b), 401(k) or 403(b) accounts rather than forcing them to open an IRA and maintain multiple retirement savings accounts.

Eliminate the "first day of the month" requirement - Participants in a 457(b) plan must request changes in their deferral rate prior to the beginning of the month in which the deferral will be made. This rule does not exist for other defined contribution plans. This rule has a negative impact on participants and is no longer necessary to carry out the purposes of a 457(b) plan.

Providing Equity in Divorce

- **Railroad Retirement Reforms**
  - With respect to railroad retirement, the bill will:
    - Eliminate the current-connection requirement for widows to collect Tier II benefits (under current law, if an employee leaves his or her railroad employer and goes to work for another employer and then dies, the surviving spouse receives a Social Security equivalent benefit but does not receive the Tier II benefits).
    - Permit both widows and divorced spouses/widows to remarry at age 60 without penalty.

- **Military Retirement Reforms**
  - The bill would eliminate the special jurisdictional requirement to treat military retirement pay as property of the military member and spouse. Under current law, there is a special jurisdictional requirement that applies to the division of a military pension between a service member and spouse that does not apply to the court's jurisdiction over the member's divorce generally or to the court's jurisdiction to divide any other property. This additional jurisdictional requirement can impose a hardship on a spouse who cannot afford to travel to file for divorce (and other laws already protect the member from having to litigate in a faraway forum). The bill would repeal the jurisdictional requirement.

- **Preservation of Assets** – During the "reasonable" period that plans are given to determine whether domestic relations orders are Qualified Domestic Relations Orders (QDROs), plans are required to segregate and preserve plan assets that would otherwise be payable to an alternate payee for up to 18 months from when the benefit first becomes payable. However, there is nothing to prevent plans from distributing assets *prior* to receipt of a proposed QDRO, even if the plan has received notice of an impending domestic relations proceeding (although in this situation some plans place a "hold" on funds voluntarily). The bill would require plans to segregate and preserve half of the participant's assets upon receipt of written notice that a separation or divorce proceeding is in process.

- **Plan Disclosure Obligations** – Current regulations require plans to furnish pertinent information about the plan and a participant's benefits thereunder to beneficiaries upon written request, and it is DOL's view that this duty applies to prospective alternate payees before receipt of a QDRO. However, if a plan administrator fails to furnish requested information, it appears that the requestor's only recourse is to rely on DOL to request the information on the beneficiary's behalf, which could take a long time. The bill would impose a meaningful financial penalty on plans that fail to respond within a reasonable time to the informational requests of prospective alternate payees, their representatives, or DOL.

- **QDRO Expenses** - Until 2003, it was DOL's view that any expenses attendant to providing information to a beneficiary or making a QDRO determination must be allocated to the plan as a whole. However, in 2003, DOL reversed this longstanding position and allowed defined contribution plans to charge the participant and alternate payee for any QDRO-related expenses. The bill would require all types of plans to allocate QDRO-related expenses to the plan as a whole.

- **Civil Service Survivor Annuities Protected -** The bill would ensure that surviving spouses of former federal employees under the Civil Service Retirement System (CSRS) would receive their survivor benefits regardless of when the worker left employment. Under current law widows and widowers of federal employees under CSRS receive survivor annuities if the employee dies while still employed or if the employee had retired and commenced receiving pension benefits. However surviving spouses do not receive survivor benefits in situations where a CSRS employee leaves work with the government and then dies before collecting pension benefits. The current law applies the same rules to both surviving spouses and to divorced widows and widowers who have been awarded survivor annuities by courts. The bill would require that both surviving spouses and surviving former spouses receive their survivor benefits even if the employee died after leaving employment and before taking pension benefits.

- **Commencement of Former Spouse Benefits** - The bill would allow former spouses of federal employees to begin collecting their court awarded share of the pension benefits when the employees become eligible to retire. Under current law both federal pension systems CSRS and Federal Employees Retirement System (FERS) allow for the division of pension benefits at divorce. However, neither plan allows a former spouse to collect the benefit until the employee actually retires. The bill would allow the former spouse to begin taking his or her court awarded share of the benefit once the employee becomes eligible to retire, regardless of whether the employee actually retires.

***Creation of IRS Office of Participant and Plan Sponsor Advocate* -** The bill would create an Office of Participant and Plan Sponsor Advocate at the IRS, similar to the current PBGC advocate.