



AMERICAN BENEFITS COUNCIL

January 30, 2015

SUMMARY OF RETIREMENT SECURITY ACT (S. 266/H.R. 557)

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SUMMARY

- (1) **New automatic contribution safe harbor:** The legislation would establish a new automatic contribution safe harbor from the nondiscrimination rules for plans with the following features:
- a. **Minimum levels of default contributions:** The minimum default level of contributions would be 6% in the first year, 8% in the second year, and 10% in all subsequent years. There would be a 10% cap on the default level of contributions in the first year but no cap would apply thereafter.
 - b. **Matching contributions:** The employer would be required to make matching contributions on behalf of all eligible nonhighly compensated employees (“NHCEs”) equal to (a) 100¢ on the dollar on employee or elective contributions up to 1% of pay, (b) 50¢ on the dollar on the next 5% of pay; and (c) 25¢ on the next 4% of pay, so that some level of matching contributions must be provided on employee or elective contributions up to 10% of pay. This structure ensures that the required matching contribution for all NHCEs under the new safe harbor will be at least equal to the required matching contribution for NHCEs under the existing safe harbor. Matching contributions with respect to employee or elective contributions above 10% of pay would not be permitted. For this new safe harbor, the nonelective contribution option available with respect to the existing automatic contribution safe harbor would not apply. The rationale is that employees should have an incentive to contribute up to 10%; if the employer could use the nonelective contribution option, that incentive would not exist.

- c. **Special tax credit:** A special tax credit would apply to small employers (i.e., employers with 100 or fewer employees) that adopt the new safe harbor. (No special tax credit applies solely by reason of an employer adopting the existing safe harbor.) The purpose of the credit is twofold. First, compared to not using automatic enrollment, adopting the new automatic enrollment safe harbor will be expensive, as it will cause a significant increase in matching contribution expense. Second, even compared to the existing safe harbor, the new safe harbor will be expensive, as illustrated below. To address both of these additional costs, the tax credit would equal the matching contributions made on behalf of NHCEs, subject to two limits: (a) the credit with respect to any NHCE would be limited to 2% of pay, and (b) the credit with respect to any NHCE would only apply for the NHCE's first five years of participation in the plan.
- i. Here is an illustration of how the new safe harbor is more expensive than the existing one, and how the tax credit addresses that issue. *Matching contribution required under the existing and new safe harbors (assuming that the plan's default contribution rate is the minimum level required):* year 1: 2% of pay under the existing safe harbor and 3.5% of pay under the new safe harbor, for a difference of 1.5% of pay; year 2: 2.5% of pay under the existing safe harbor and 4% of pay under the new safe harbor, for a difference again of 1.5% of pay; year 3: 3% of pay under the existing safe harbor and 4.5% of pay under the new safe harbor, for a difference again of 1.5% of pay; year 4 and all subsequent years: 3.5% of pay under the existing safe harbor and 4.5% of pay under the new safe harbor, for a difference of 1%. Thus, the new safe harbor costs an additional 1.5% of pay in the first three years, and an additional 1% of pay in all subsequent years. The proposed credit equal to matching contributions up to 2% of pay covers this additional cost, and also covers some of the costs of adopting any automatic contribution arrangement, which are often substantial.
- d. **Nondiscrimination safe harbor:** A plan that fits within the existing safe harbor is exempt from (1) top-heavy testing and (2) nondiscrimination testing with respect to pre-tax elective contributions and matching contributions, but not with respect to after-tax employee contributions. The new safe harbor arrangement would have the same exemptions as the existing safe harbor; in addition, to enhance the attractiveness and workability of the new safe harbor, the nondiscrimination exemption would also apply to after-tax employee contributions. Without the applicability to after-tax employee contributions, there is a very good chance that, unlike under the existing safe harbor, company owners and

other principals would not be able to receive the maximum match available under the plan, which would make it less likely that such principals would decide to adopt the new safe harbor. Thus, this change is needed to ensure that the company principals can receive the maximum matching contributions available.

- e. **Notices:** Generally, employees must receive a notice explaining their rights and obligations under the existing safe harbor (1) prior to eligibility to contribute so that the employee has a reasonable period of time after receipt of the notice to elect out of automatic enrollment or to elect a non-default investment, and (2) annually thereafter. Under the legislation, Treasury would be directed to simplify and clarify the rules regarding the timing of participant notices regarding the existing and new safe harbors in the context of (1) plans that allow employees to be eligible immediately, and (2) companies with multiple payroll and administrative systems. Treasury would also be directed to simplify and clarify the automatic escalation timing rules in the context of companies with multiple payroll and administrative systems. In these situations, for example, the notices and the automatic escalation increases often, as a practical matter, have to happen at different times for different employees. This has raised uncertainties for plan sponsors and has thus caused hesitation to use the existing safe harbor; practical difficulties in meeting the notice timing rules in the case of plans providing immediate eligibility have also caused similar concerns and hesitation.
 - f. **Other aspects:** Generally, in all other respects, such as the rules regarding the required vesting schedule applicable to matching contributions, the new safe harbor is the same as the existing safe harbor.
- (2) **Multiple employer plan sanction:** Under current law, if one or more employers participating in a multiple employer plan (“MEP”) violate the qualification rules with respect to their portion of the plan, the entire plan can be disqualified. This potential liability attributable to the acts of others can prevent some small employers from joining a MEP. Under the legislation, Treasury would be directed to prescribe regulations under which the violations of one or more participating employers would not taint the entire plan.
- (3) **Open MEPs:** DOL has consistently taken the position that in order for a plan to be a MEP, the participating employers generally must have a strong relationship to each other aside from maintaining the same plan. Under the legislation, a defined contribution plan maintained by employers with no relationship to each other can be a MEP (referred to below as an “open MEP”) if it meets the following conditions:

- a. The plan's Form 5500 includes the name and identifying information of each participating employer.
 - b. Each participating employer retains fiduciary responsibility for:
 - i. The selection and monitoring of the named fiduciary; and
 - ii. The investment and management of its portion of the plan assets, except to the extent that responsibility is delegated to another fiduciary.
 - c. Participating employers cannot be subject to unreasonable charges or restrictions with respect to leaving the plan.
 - d. Each participating employer has no more than 500 employees (subject to a five-year grace period for employers that grow beyond 500 employees).
- (4) Reporting and disclosure simplification:** Certain reporting and disclosure relief could apply to open MEPs and other MEPs that meet the 500 employee rule described in (2)d above. Specifically with respect to such plans, DOL may:
- a. Prescribe simplified rules for summary plan descriptions, Form 5500s, and benefit statements, and
 - b. Waive the requirement to engage an independent qualified public accountant where appropriate.
- (5) Saver's Credit:** Treasury would be directed to modify the Form 1040EZ to allow individuals filing that form to claim the Saver's Credit.