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Senators revive major bipartisan retirement reform legislation

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Wide-ranging retirement reform legislation aims to expand plan coverage, boost savings, increase lifetime income options and support defined benefit (DB) pension plans. Introduced May 21 by Sens. Ben Cardin, D-MD, and Rob Portman, R-OH, the Retirement Security and Savings Act of 2021 (S 1770) revives a bill from the last Congress. The measure also shares many provisions with a major House bill — the Securing a Strong Retirement Act of 2021 (HR 2954) — unanimously approved by the Ways and Means Committee earlier this month. The Senate Finance Committee, on which Cardin and Portman sit, will likely consider and approve the Cardin-Portman bill this year. Broad bipartisan support for the “SECURE 2.0” reforms in both the House and Senate bills suggest a good chance for enactment of a final package at some point, although timing and procedural challenges cloud the outlook for action this year. This GRIST provides a high-level overview of the Cardin-Portman bill’s key provisions and highlights changes from the prior version.

Student loan match programs

The bill would let sponsors of 401(k), 403(b), governmental 457(b) and savings incentive match (SIMPLE) plans match employees’ student loan payments as if the payments were salary-reduction contributions to the retirement plan. The benefit would apply only to repayments of student loan debt incurred for higher education.

Employers offering the benefit would have to make it available to all employees eligible to receive matching contributions on salary deferrals to the retirement plan. In addition, the match rate and vesting schedules for both types of match payments would have to be the same. Plans could apply the actual deferral percentage (ADP) test separately to employees who receive these matching contributions.

Automatic enrollment

Two provisions of the bill aim to increase the use of automatic-enrollment designs in defined contribution (DC) plans:

- **Secure deferral arrangement.** This new safe harbor design would have higher minimum deferral rates than the existing auto-enrollment safe harbor and a tiered safe harbor matching contribution of up to 10% of pay.

- **Auto-enrollment.** The bill directs Treasury to issue regulations simplifying the notice-delivery timing requirements and the auto-escalation rules for eligible automatic contribution arrangements (EACAs) and auto-enrollment church plans.

Expanded coverage of part-time workers

Sponsors of noncollectively bargained 401(k) plans would have to let part-time workers voluntarily contribute to the plan if they have completed at least 500 hours of service per year for two consecutive years. Under the Setting Every Community Up for Retirement Enhancement (SECURE) Act, part-timers currently become eligible to participate after meeting the hours-of-service requirement for three consecutive years.

Changes to catch-up contribution limits

The bill would make the following changes to the rules for catch-up contributions:

- **Increased limit at age 60.** For individuals age 60 or older, the catch-up contribution limit would increase to $10,000 under qualified, 403(b) and governmental 457(b) plans and to $5,000 under SIMPLE plans. (The 2021 limits are $6,500 and $3,000, respectively.)

- **Indexing.** The current $1,000 catch-up contribution limit for individual retirement accounts (IRAs) would be adjusted for cost-of-living increases. (The catch-up limits for employer-sponsored plans are already indexed.)

Minimum distribution requirements

The bill would make a number of changes to the Internal Revenue Code Section 401(a)(9) rules for required minimum distributions (RMDs):

- **Starting age.** A participant's RMD start date would increase from the current age of 72 (as set by the SECURE Act) to age 75 beginning in 2032. The House's Securing a Strong Retirement Act would make the same change but phase it in, starting at age 73 in 2022 and rising to age 74 in 2029 before settling at age 75 in 2032.

- **Actuarial increase for DB plan participants.** The bill would clarify that DB plan participants who retire after the year in which they turn 70-1/2 are still entitled to an actuarial increase for the post-age-70-1/2 period in which they are not receiving distributions. This is a technical correction to the SECURE Act, which some practitioners read as limiting the increase to participants who retire after age 72.

- **No penalty on partial annuitization.** Participants who elect to receive a portion of their DC account balances as an annuity could choose to determine their RMD on the total account balance, including the value of all purchased annuity contracts. The RMD payable from the remaining account balance for a given year would be the total RMD minus the annuity payments.

- **Small DC account balances.** Participants whose aggregate DC plan balances don't exceed $100,000 (indexed) would be exempt from RMDs. Plan administrators could rely on a participant's certification that the aggregate account balances are under the threshold.

- **Excise tax.** The excise tax on a missed RMD would be reduced from 50% to 25%.

- **Roth accounts.** Like standalone Roth IRAs, Roth accounts in employer plans would be exempt from RMDs and the incidental death benefit rules.

- **Surviving spouses.** The surviving spouse of a deceased employee could elect to be treated as the employee.

Preservation of income

The bill includes several provisions to help retirees make their savings last throughout retirement.

Qualified longevity annuity contracts (QLACs)

QLACs let employees use a portion of their retirement savings to purchase an annuity starting as late as age 85 without violating the RMD rules. The bill directs Treasury to amend its regulations on QLACs:

- **Premiums.** The bill would eliminate the requirement limiting QLAC premiums to 25% of the account balance and would increase the dollar limit on these premiums from $125,000 to $200,000 (indexed for inflation).

- **Joint and survivor benefits after divorce.** The bill would clarify the treatment of joint and survivor benefits for couples who get divorced after purchasing a QLAC but before commencing payment.

- **"Free look" periods.** The regulatory prohibitions on QLACs having commutation benefits, cash surrender rights and similar benefits would prohibit contracts from having rescission periods up to 90 days.

- **Indexed and variable contracts with guaranteed benefits.** The bill would direct Treasury to allow QLACs in the form of variable and indexed annuities with guaranteed benefits.

Remove barriers for life annuities

To remove what some retirees consider barriers to purchasing commercial annuities, the bill would allow the following:

- **Small increases.** Annuity payments could increase by up to 5%, as long as the increases occur at least annually.

- **Cashouts.** Annuitants could receive full or partial lump sum cashouts of the remaining annuity payments or the payments scheduled to be made for the next 12 months.

- **Dividends or similar distributions.** These distributions would be allowed if based on a reasonable comparison of the actuarial factors assumed when calculating the initial annuity payments and the issuer's experience with respect to those factors.

- **Refund on annuitant's death.** A refund of the amount paid for an annuity reduced by payments received would be permissible after the annuitant's death.

Expanded Self-Correction Program

The bill would expand the Self-Correction Program (SCP) under IRS's Employee Plans Compliance Resolution System (EPCRS):

- **Inadvertent errors.** Plans could use SCP to correct inadvertent failures at any time before Treasury identifies the error.
- **Loan failures and the Voluntary Fiduciary Correction Program (VFCP).** The bill would make SCP available for more plan loan failures and require the Department of Labor (DOL) to treat inadvertent loan failures corrected under SCP as meeting VFCP requirements.
- **Safe harbor corrections.** EPCRS would provide more safe harbors for correcting inadvertent errors, including a safe harbor method for calculating earnings that must be restored to a plan.
- **Correction by IRA custodians.** IRA custodians could correct inadvertent errors as long as the IRA owner is not at fault.
- **Deadline for RMD corrections.** Plans and IRA custodians/owners would have 180 days to self-correct inadvertent violations of the RMD rules without paying an excise tax.

Nondiscrimination testing

On the heels of the SECURE Act's closed-plan testing relief, the bill would make additional changes aimed at easing the nondiscrimination rules:

- **Minimum participation.** The bill would require Treasury to issue regulations allowing the minimum participation rule to apply separately to bona fide separate subsidiaries and divisions.
- **Safe harbor compensation.** Plans could use either base pay or rate of pay to determine benefits and contributions under the Section 401(a)(4) and the ADP/actual contribution percentage (ACP) safe harbor designs.
- **Catch-up contributions.** Employers using the separate line of business rules for coverage testing could use those rules to satisfy the nondiscrimination requirements for catch-up contributions.
- **Change to top-heavy rules for DC plans.** DC plans could apply the top-heavy minimum benefit rules separately to employees who haven't met the Code's minimum age (21) and service (one year) requirements for participation.

Reporting and disclosure

Several provisions would simplify reporting and disclosure requirements:

- **Joint agency report.** Treasury, DOL and the Pension Benefit Guaranty Corp. (PBGC) would have to review how to consolidate, simplify and standardize reporting and disclosure requirements. The agencies would have to report recommendations to Congress within 18 months of the bill's enactment.

- **Consolidated notices.** DOL and Treasury would have to let DC plans consolidate required notices, as long as the consolidated notice includes all the required content, meets the distribution timing and frequency requirements, and doesn't obscure important points for participants.

- **Performance benchmarks for asset allocation funds.** Within six months of the bill's enactment, DOL would have to issue new guidance allowing plan administrators to benchmark a target-date fund against a blend of securities market indices that is reasonably representative of the fund's asset holdings. This approach to benchmarking would be permitted but not required. DOL would also need to report to Congress on the effectiveness of the regulatory benchmarking requirements.

- **Model rollover notices.** DOL, Treasury and PBGC would have to simplify the model Section 402(f) rollover notices to facilitate better understanding of the different distribution options and corresponding tax consequences. The notices would also have to explain the effect of elections on spousal rights.

- **Exemption for nonparticipating employees.** Individual account plans would be exempt from providing notices, disclosures and plan documents to employees who choose not to participate and have no account balance. To qualify for the exemption, the plan must provide employees all documents in connection with initial eligibility and continue to send annual reminder notices about employees' eligibility to participate and any documents they'd otherwise be entitled to request.

Provisions specific to 403(b) plans

The bill contains several 403(b) plan enhancements:

- **Investment in group trusts.** The bill would allow 403(b) custodial accounts to invest in group trusts. These accounts currently can invest only in the stock of regulated investment companies. Collective investment trusts are held by banks and are considered less costly investment options than mutual funds.

- **Transferring assets between qualified and 403(b) plans.** Employers could transfer 403(b) account balances to or from a qualified 401(a) or 403(a) plan and merge those plans.

- **Hardship distribution rules.** 403(b) plans could permit hardship withdrawals of elective deferrals, qualified nonelective contributions (QNECs) and qualified matching contributions (QMACs), as well as earnings on those amounts. Employees may already take a hardship distribution of their elective deferrals, but not earnings on those amounts. The bill would also eliminate the requirement that employees take all available plan loans before requesting a hardship distribution. These changes would harmonize the 403(b) hardship distributions rules with the rules for 401(k) plans.

Separate Senate legislation (S 1703) would allow 403(b) plans to join multiple-employer plans (MEPs) and pooled employer plans (PEPs). The Finance Committee may decide to add those provisions to the Cardin-Portman bill during markup.

Retirement Savings Lost and Found

The bill would establish the Office of Retirement Savings Lost and Found, featuring an online searchable database of information about all lost retirement accounts, managed by the PBGC. Plans would have to transfer small lost accounts worth $1,000 or less to the office, which would invest the amounts in Treasury securities. As under current law, plans seeking to disburse a lost retirement account would have to roll over accounts worth more than $1,000 into an IRA established in the participant's name.

Recovery of retirement plan overpayments

The bill would give retirement plan fiduciaries the latitude to decide not to recoup benefit overpayments. If plan fiduciaries choose to recoup overpayments, limitations and protections would apply to safeguard retirees. Notably, fiduciaries wouldn't be able to recoup overpayments from a participant or a beneficiary if the first overpayment occurred more than three years before the participant or beneficiary first receives written notice of the error. Fiduciaries also could not attempt to recoup overpayments to a participant from any beneficiary of that participant.

Key provisions affecting DB plans

The bill contains a few targeted provisions for DB plan sponsors:

- **No indexing of PBGC variable-rate premiums.** The bill would put a halt to inflation increases on PBGC variable-rate premiums, which are a specified percentage of a plan's unfunded vested benefits. Variable premiums would be frozen at the 2018 level of $38 per $1,000 of unvested benefits. The inflationary indexing, in place since 2014, has been widely criticized as theoretically unsound.

- **Projected interest crediting rate.** To demonstrate compliance with applicable Code rules like the benefit limitations under Section 415 and the accrual rules of Section 411, statutory hybrid plans that credit interest at a variable rate could use a reasonable projection of the actual interest crediting rate — not to exceed 6% — rather than the previous year's rate, as IRS auditors have sometimes required.

- **Non-417(e) interest rates.** Plan sponsors using non-417(e) interest rates to provide "greater of" lump sums or to determine other optional forms could change the lookback month using the same rules that apply for the 417(e) rate. Once a rate is changed, it couldn't be changed again for five years without Treasury approval.

- **Mortality.** The mortality tables Treasury sets for sponsors to determine minimum funding requirements and minimum lump sums couldn't use future mortality improvements greater than 0.78% at any age, or another figure Treasury determines is consistent with the overall rate of mortality improvement projected by the Social Security Administration.

- **Section 420 transfers.** Employers' ability to fund retiree health and life insurance benefits with surplus pension assets would continue for an additional six years through 2031. Sponsors (except of collectively bargained plans) making *de minimis* transfers would get more generous rules for determining the available surplus, subject to a seven-year — rather than the usual five-year — cost-maintenance requirement.

Provisions of interest to small employers

Some provisions will be of special interest to small employers:

- **Tax credits.** New tax credits would be available to small employers that adopt the bill's new secure deferral arrangement or implement three-year re-enrollment periods for employees deferring less than the minimum auto-deferral rate. The current tax credit for small employers to start a retirement plan would increase.

- **SIMPLE plans.** Employers sponsoring SIMPLE plans could make nonelective contributions up to 10% of pay for employees who are eligible to participate and earn at least $5,000 a year. The bill would also permit Roth SIMPLE IRAs.

- **Military spouse eligibility credit.** Small employers could receive a three-year tax credit if they (i) make employees who are military spouses eligible for DB or DC plan participation within two months of hire, (ii) let eligible military spouses receive any matching or nonelective contribution that any nonhighly compensated employee could receive after two years of service, and (iii) make military spouses 100% immediately vested in all employer contributions. The credit would apply only to nonhighly compensated employees.

Miscellaneous

Other miscellaneous provisions that might be of interest to employers include:

- **Mandatory cashouts.** The bill would increase the permissible mandatory cashout limit from $5,000 to $6,000. Although included in the Retirement Savings Lost and Found section of the bill, the change would apply to all qualified DB and DC, 403(b), and 457(b) plans. The Form 8955-SSA reporting requirements would increase for terminated vested participants receiving mandatory cashouts, including participants whose benefits are transferred to the new Retirement Savings Lost and Found.

- **Missing participants.** DOL would have to issue regulations on what steps plan fiduciaries must take to meet their duty to keep track of deferred vested participants and find missing participants.

- **Post-termination elective deferrals.** Participants could make elective deferrals on severance and back pay as if they were still actively employed.

- **Cashout of annuity benefits.** Participants in qualified plans could cash out some or all of an annuity benefit already in pay status without triggering the additional tax on distributions made before age 59-1/2 (or changed within five years after payments start), as long as the benefit is rolled over to another qualified plan that continues the annuity stream. Plan sponsors could rely on a participant's certification that the new plan will continue the annuity stream. The same treatment would be available for payments from nonqualified annuity contracts rolled over into similar contracts.

- **Expanded Saver's Credit.** The Saver's Credit — currently applied against a taxpayer's tax liability — would be refundable. The refund would be deposited into a Roth IRA or Roth account in an employer plan. The bill would increase the credit for some taxpayers and direct Treasury to promote the credit to increase public awareness.

- **Rollovers.** Nonspouse beneficiaries could roll over a deceased participant's account to an "inherited IRA" established to receive the distribution or could transfer distributions among pension, 403(b) and 457(b) plans with tax-favorable rollover treatment. In addition, Roth accounts in employer plans could accept rollovers from Roth IRAs.

- **Small financial incentives for contributing to plans.** Employers could offer small financial incentives (e.g., gift cards) — without violating the prohibited transaction rules — to encourage employees to participate in the employer's 401(k) or 403(b) plan.

- **Qualified retirement planning services.** Employees offered a choice between receiving retirement planning services or cash wouldn't be taxed for constructive receipt if they choose retirement planning services. Highly compensated employees would receive this tax treatment only if the choice is available to each employee who's normally provided education and information about the employer's plan.

- **457(b) deferrals.** Governmental 457(b) plans could allow employees to change their deferral rate at any time before the deferred compensation would otherwise have been available to them. Current rules require making the change before the beginning of the month of deferral.

- **Charitable contributions.** Participants age 70-1/2 or older could use their pension, governmental 457(b) and 403(b) plan funds to make donations of up to $100,000 directly to a charity without paying tax on the withdrawals. Current rules only exempt charitable donations from IRAs.

Related resources

Non-Mercer resources

- Press release (Sen. Ben Cardin, May 21, 2021)

- S 1770, the Retirement Security and Savings Act of 2021 (Congress, May 20, 2021)

Mercer Law & Policy resources

- Senate bill boosts PEPs, eases fixes for plans with automatic features (May 24, 2021)

- Major bipartisan retirement reform bill gets House committee approval (May 6, 2021)