

Private Retirement Benefits in the 21st Century: A Path Forward



100 Years Standing Up for American Enterprise
U.S. CHAMBER OF COMMERCE



LABOR, IMMIGRATION &
EMPLOYEE BENEFITS DIVISION
U.S. CHAMBER OF COMMERCE



Dear Reader:

The U.S. Chamber of Commerce is a well-regarded thought and advocacy leader for national and global employee benefits issues. Our unmatched grassroots clout enables us to orchestrate business involvement to win critical regulatory and legislative initiatives and advocate for our members' most pressing business issues.

In response to concerns about retirement security, the Chamber has prepared this white paper to offer guidelines on initiatives that will bolster the voluntary employment-based retirement benefits system and retirement security for workers. These guidelines include ways for employers to create and maintain retirement plans, and for workers to increase their savings. The paper also identifies ways to make retirement assets last for future retirees.

The Chamber is determined to protect the retirement security of America's workforce and preserve the ability of employers to provide flexible and comprehensive compensation to employees.

It is my pleasure to manage the Chamber's dynamic employee benefits portfolio and, if you have not already done so, I encourage you to join the U.S. Chamber and help shape the organization's agenda in these critical areas.

Sincerely,

A handwritten signature in black ink, appearing to read 'Randel K. Johnson'. The signature is fluid and cursive, with a long horizontal flourish extending to the right.

Randel K. Johnson
Senior Vice President
Labor, Immigration & Employee Benefits Division

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Introduction

Businesses in America, large and small, maintain a long-held commitment to providing voluntary benefits that support the welfare of their workers. Retirement security in particular is a significant focus of voluntary benefit offerings. As Americans live longer, healthier lives, retirement security becomes a greater concern. The private employer-provided retirement system has contributed greatly to the current retirement security of millions of Americans. To continue the success of the system and ensure that employer-provided plans continue to play an important role in retirement security, the Chamber believes that certain issues must be addressed. First, steps must be taken to encourage employers to maintain existing retirement plans and to set up new plans. Second, participants must be encouraged to accumulate greater savings inside of retirement plans. Third, the issue of making assets last throughout retirement must be addressed.

The U.S. Chamber of Commerce Employee Benefits Committee has developed this white paper to offer a path on initiatives and reforms that build on existing institutions and approaches to bolster the voluntary employment-based retirement benefits system and enhance retirement security for workers. The ideas in this paper represent a long-term view of retirement changes that are needed. While some steps can be implemented immediately, we realize that other steps may require additional time. Our recommendations include ways to encourage employers to create and maintain retirement plans, to encourage workers to save more, and to identify ways to make retirement assets last for future retirees.

The private retirement system is a success.

Conventional wisdom suggests that today's retirees receive less income from employment-based plans than in the "good old days." However, income from defined benefit and defined contribution plans represented 19% of retiree income in 1975; whereas, by 2009, it accounted for 26% of retiree income.¹ The number of retirees receiving retirement income from employment-based plans has also grown, from 20% of retirees in 1975 to 31% in 2009.² Today, 82 million households

have defined benefit plans, defined contribution plans, or individual retirement accounts (IRAs).³ These households have a combined \$17.9 trillion earmarked for retirement.⁴

Innovative plan design is central to the success of the private retirement system.

One of the great successes of the private retirement system has been the ability of employers to implement new plan designs to accommodate changing demographics and evolving workforce needs. Since 1980, there has been an expansion of defined contribution and hybrid plans. Innovation in plan design has encouraged employers to continue to participate in the private retirement system.⁵

In 1875, the American Express Company implemented the first employer-provided retirement plan.⁶ It was a defined benefit plan. By 1987, more than 232,000 private defined benefit plans covered nearly 40 million workers.⁷ Today, almost 30,000 single and multiemployer defined benefit plans cover roughly 44 million workers.⁸

Defined benefit plans allow employers to provide an important retirement benefit to workers. In a defined benefit plan, employers bear the investment risk. If the plan assets are insufficient to pay benefits, the employer and its affiliated companies must do so. Moreover, when a company is liquidated in bankruptcy, certain plan benefits are guaranteed by the Pension Benefit Guaranty Corporation (PBGC). In addition, defined benefit plans must offer an annuity form of payment. Annuities can provide a lifetime payment stream that ensures that retirees do not outlive their retirement benefit. Thus, defined benefit plans provide access to a fixed, guaranteed, and secure retirement benefit.

Despite the decreasing numbers of defined benefit plans, many employers remain committed to providing these plans as an important part of their compensation package. Furthermore, defined benefit plans are an integral part of the national economy. Their \$1.9 trillion in assets represent a significant share of the nation's long-term capital.⁹ Moreover, defined benefit plans paid out over \$167 billion in retirement benefits in 2009.¹⁰

The greatest growth in the private retirement plan space has been in defined contribution plans. The number of participants in defined contribution plans has increased from 47 million in 1995 to 87 million in 2009.¹¹ Since 1975, the number of defined contribution plans has almost quadrupled, from 207,748 to 659,530 in 2007.¹² In 1992–93, 32% of workers in private industry participated in a defined benefit plan, while 35% participated in a defined contribution plan.¹³ According to the 2008 National Compensation Survey, private industry workers' participation in defined benefit plans decreased to 21%, while participation in defined contribution plans increased to 56%.¹⁴

Two decades from now, the first cohort of workers will begin to retire under a system dominated by defined contribution plans. As the design of the 401(k) plan has evolved, it has become a truly meaningful source for accumulating retirement assets. Academic research projects that 60% of participants who will retire following a full career of 401(k) saving and investing will have accumulated enough in their 401(k) plans to replace half their salaries.¹⁵

Moreover, the design of 401(k) plans has proven to serve participants well during market fluctuations. For example, in 2008—the height of the economic recession—fewer than 1 in 25 participants withdrew money from their plan. Fewer than 1 in 50 took a hardship withdrawal, and fewer than 1 in 7 adjusted their asset allocation.¹⁶ Consistent saving and dollar cost averaging helped participants stay the course. Even though the market decline reduced the average 401(k) account balance of consistent participants by 27.8% between 2007 and 2008, investment gains, along with the pro-saving elements of plan design, resulted in a 31.9% gain from 2008 to 2009.¹⁷

The hybrid plan design was developed in an effort to combine the benefits of both defined benefit and defined contribution plans. Hybrid plans are defined benefit plans that combine the advantages of a 401(k) plan with those of a traditional pension plan. The two most common types of hybrid plans are cash balance plans and pension equity plans. The basic plan formula consists of a compensation

credit and an interest credit. Compensation credits end after a participant terminates employment, but interest credits continue until a participant withdraws his or her benefit. Hybrid plans include cash balance plans, pension equity plans, and contributory pay plans. Almost 3,000 hybrid pension plans currently cover more than 10 million workers.¹⁸

Employers have implemented hybrid plans in response to the changing demographics of the workforce. In a traditional pension plan, most of the benefit accrues close to retirement, which tends to favor senior employees by rewarding longevity and increasing compensation. In a hybrid plan, however, benefits accrue evenly over a participant's career. For an increasingly mobile workforce, steady accruals under a hybrid plan provide greater benefits than under a traditional pension plan. Moreover, workers appreciate hybrid plans because of their similarities to 401(k) plans. Workers can more easily determine their benefit and understand the amount of their benefit at any point during their career. Also, these benefits are more portable than benefits under a traditional pension plan.

No single plan design is perfect for every company or every worker. Therefore, the private retirement system has encouraged innovation in plan design, and many employers have more than one type of plan as part of their retirement program. The Chamber believes that the key element of the private retirement system is its voluntary nature. For employers that choose to implement retirement programs, flexibility and choice are key considerations. The mix of types of benefit plans in the future will be diverse—defined benefit, defined contribution, multiemployer, and hybrid plans. Demographic and competitive needs will spur the creation of plan designs that we have not even begun to contemplate. Consequently, it is more important than ever to ensure that there are no statutory, practical, or political barriers to innovation that would discourage participation in the private retirement system.

Americans are living and working longer, and their views of retirement are changing.

In addition to innovations in plan designs, we are witnessing an evolution of another type. Retirement in America is changing, a fact that can be attributed both to hard economic times and evolving views of what retirement should be.

Many of today's older workers see retirement as a whole new life chapter rather than a time to wind down.¹⁹ Workers aged 55 and over plan to remain in the workforce longer than prior generations. According to various surveys, anywhere from 60-80% of baby boomers plan to include some work in their retirement.²⁰ Of those surveyed by AARP, only about 16% say they will not work at all. The majority of those who will work plan on it for the sake of interest and enjoyment (71%) and for the income that will let them live the lifestyle they would like (61%).²¹ Obviously, there is no longer a monolithic vision of retirement. Therefore, flexible laws are needed to continue to serve retirees who no longer work while also encouraging those who are able and willing to continue to work.

Along with the trend to keep working is the growing self-reliance factor. A study by AARP found that 7 in 10 baby boomers do not want to rely on their children during retirement.²² Thus, it is increasingly important that employers have the flexibility to allow for innovative retirement programs, such as phased retirement, that reflect the changing views of retirement.

Although many workers envision a longer work life, some will not be physically able to continue working in their later years. And regardless of actual retirement age, millions of Americans will live very long lives. Men who reach age 65 can expect to live, on average, another 17 years. Women who reach age 65 can expect to live, on average, another 20 years.²³

This longevity has important implications for employment-based benefits. The provision of insurance products such as disability and long-term care, for example, can mitigate financial risk to those who face health challenges. Lifetime income products, such as annuities, managed payout funds,

and systematic withdrawal programs, can mitigate the risk of outliving one's savings. Voluntary phased retirement programs can help older workers transition from full-time work to alternative schedules. And financial education and advice on issues such as decumulation strategies can help workers understand how to effectively manage their assets in retirement.

The voluntary employment-based system of retirement benefits works on several fronts. Nonetheless, there are still workers without access to plans or who do not participate in the plans offered to them. Regulatory and legislative policies can help increase access and participation by encouraging the formation of new plans and the maintenance of existing plans, particularly among small employers.

Maintaining current tax incentives for retirement saving is critical.

The success of private retirement plans is at risk of being undone by short-term political wrangling. Employer-sponsored retirement plans have introduced tens of millions of American workers to retirement saving. Eliminating or diminishing the current tax treatment of employer-provided retirement plans would jeopardize the retirement security of tens of millions of American workers, impact the role of retirement assets in the capital markets, and create challenges in maintaining the quality of life for future generations of retirees.²⁴

While we work to enhance the current private retirement system and reduce the deficit, we must not eliminate one of the central foundations—the tax treatment of retirement savings—on which today's successful system is built. Doing so would imperil the existence of employer-sponsored plans and the future retirement security of working Americans.

In this paper, the Chamber lays out a path to continue the success of the private employer-provided retirement system and increase retirement security for millions of workers.

Overview of Recommendations

I. Encourage employers to create and maintain retirement plans

A. Grow plan sponsorship among small businesses.

1. Enhance the small business tax credit for 401(k) start-up costs by expanding it and making it refundable.
2. Eliminate top-heavy rules. Alternatively, relax the rules to encourage greater implementation and maintenance of plans.
3. Simplify discrimination testing by creating an optional nondiscrimination test for average deferral percentage testing.
4. Facilitate the expansion of multiple employer plan designs.
5. Give small business a dedicated voice on the relevant advisory committees of the Department of Labor, the Department of the Treasury, and the Pension Benefit Guaranty Corporation.

B. Streamline notice requirements and allow for greater use of electronic disclosures.

C. Reform multiemployer defined benefit funding rules to prevent bankruptcy among small employers and allow plans to remain financially solvent on an ongoing basis.

D. Reform single-employer defined benefit funding rules to allow for greater predictability.

E. Clarify the hybrid plan rules and regulations.

F. Create greater transparency in accounting standards for employer-provided benefit plans.

G. Avoid competition between government entities and private plan sponsors.

II. Encourage greater individual savings

A. Encourage use of automatic plan features.

1. Modify the safe harbor rules by removing the top end auto deferral limit and relaxing the matching formula.
2. Adjust language around automatic escalation by informing participants that they can either “opt out,” “opt down,” or “opt up” so participants can recognize that it is not an all-or-nothing decision.

B. Encourage financial education for retirement.

C. Help preserve retirement assets.

1. Permit elective contributions following a hardship distribution.
2. Extend the rollover period for plan loans.

III. Strategies to make retirement assets last

A. Encourage additional distribution options.

1. Encourage innovation in accumulation and decumulation strategies in a product-neutral manner.
2. Encourage, but do not require, payout options other than a lump sum.
3. Hold employers to a fiduciary standard with respect to annuity selection from a defined contribution plan.

B. Address required minimum distribution rules.

1. If the rules are not eliminated, move the starting age to age 75 and permit 5% owners who continue working to not begin required distributions.
2. Exclude money used to purchase longevity insurance from minimum distribution rules.

C. Encourage employers to offer voluntary products.

1. Permit employers to offer retiree health savings and insurance products such as long-term care insurance and longevity insurance through cafeteria plans.
2. Allow employees, within reasonable limits, to access 401(k) assets to purchase long-term care insurance, longevity insurance, and retiree health care.
3. Exclude money used to purchase longevity insurance from minimum distribution rules.

D. Eliminate barriers to phased retirement.

1. Continue to treat phased retirement programs and practices as discretionary arrangements.
2. Legislative and regulatory modifications are required.
 - a. Clarify that phased retirement benefits are not protected under Section 411(d)(6).
 - b. Eliminate restrictions against rehiring people who have recently retired.
 - c. Allow in-service distributions at early retirement age as defined in the plan.
3. Allow, but do not require, employers to continue to offer health benefits to phased retirees.

I. Encourage Employers to Create and Maintain Retirement Plans

Policymakers can encourage more private retirement plan formation and existing plan maintenance in several ways. These include simplifying rules for small employer plans, reforming multiemployer and single-employer plan funding, clarifying the rules for hybrid plans, addressing employer concerns about accounting standards pertaining to employer-provided benefits, and avoiding competition between state governments and private employers.

A. Grow Plan Sponsorship Among Small Businesses

Many small employers, like larger employers, offer benefits to their employees. These small businesses want to continue offering benefits but have their own unique issues. Other small businesses would like to start offering retirement benefits but face significant burdens.²⁵

Policymakers can take several steps to increase plan sponsorship and participation among small businesses. Many of these recommendations would also be helpful to larger businesses. However, we have highlighted them under this section because we think they would be particularly encouraging to small plan sponsors.

1. Enhance the Small Business Tax Credit

Enhancing the current small businesses tax credit for 401(k) start-up costs could encourage greater plan formation. The credit is allowed for the first three years of start-up costs of a new small business retirement plan (with fewer than 100 participants). It includes up to 50% of the first \$1,000 (i.e., \$500) in start-up administrative and retirement-education expenses.²⁶

The current credit is too small and short-lived to change behavior. Lawmakers should consider expanding the credit and making it refundable to increase the incentive for small businesses to set up 401(k) plans.

2. Eliminate Top-Heavy Rules

The top-heavy rules are an unnecessary burden on employers that want to offer a 401(k) plan but are not inclined or are unable to provide a matching contribution.²⁷ Under current requirements, if a key employee makes a deferral and the plan is top-heavy, it triggers a 3% required contribution for nonkey employees.²⁸ In addition, the deferrals made on behalf of family members of key employees are attributed to the key employee, which increases the likelihood of triggering the top-heavy contribution. Because these rules directly affect the decision makers and owners in the company, they may deter the implementation of the plan, which would have benefited all employees.²⁹

The Chamber believes that the top-heavy rules are unnecessary since the contributions are already subject to average deferral percentage (ADP) testing to ensure equity between highly paid and non-highly paid employees. Therefore, we believe the top-heavy rules should be eliminated. If they are not eliminated, we recommend that they be modified to encourage greater implementation and maintenance of retirement plans. For example, eliminating the requirement that deferrals made by family members be attributed to the key employee would be extremely useful.³⁰

3. Simplify Discrimination Testing

Another step policymakers could take is to simplify the ADP test for nondiscrimination. For example, a plan would not pass the ADP test if (1) non-highly compensated employees' contribution percentage is less than 6%, and (2) the contribution percentage of highly compensated employees is 200% or more of that amount. If non-highly compensated employee contributions exceed 6%, then the plan would pass the ADP test.³¹

4. Facilitate the Expansion of Multiple Employer Plan Designs

Another way to increase retirement plan sponsorship among small businesses would be to facilitate and expand the use of multiple employer plans (MEPs). MEPs offer an attractive and cost-efficient alternative for small businesses for which a stand-alone 401(k) plan is not feasible.

A MEP is a single plan that is maintained by a MEP sponsor and one or more unrelated employers (“adopting employers”). Common sponsors of MEPs include professional employer organizations, human resource outsourcing organizations, and some trade associations. MEPs permit adopting employers to enjoy many of the features and benefits of a 401(k) plan, such as flexibility in plan design and higher deferral limits, without having to sponsor a stand-alone plan. Each adopting employer must continue to conduct certain Employee Retirement Income Security Act of 1974 (ERISA) requirements, such as discrimination testing, as if it were maintaining a separate plan. In addition, for tax purposes, each adopting employer may deduct the contributions it makes on behalf of its employees, including, in the case of a professional employer organization arrangement, worksite employees from whom it receives services.

The greatest advantage of the MEP is the centralized functions that the MEP sponsor can provide. Costs are shared among the adopting employers, regardless of their number. For example, one plan administrator, trustee, and named fiduciary can act for the entire MEP. The MEP can provide centralized payroll, one investment lineup, and one annual report and audit for the entire plan. This translates to substantial economies of scale and cost efficiencies over stand-alone plans for small businesses.

However, there are also significant disadvantages to participation in a MEP. The biggest is that every employer is jointly liable for the testing and funding mistakes of

every other employer in the MEP. This liability can be a daunting hurdle for many employers. In addition, some employers may be discouraged by the inability to find a MEP sponsor or by the notice and disclosure requirements that are not required to be completed by the plan administrator.

Changing several of the rules regarding MEPs could significantly expand their use. For one, the Chamber recommends the implementation of safe harbors for MEP sponsors and adopting employers that would immunize them from noncompliant adopting employers. We also recommend that the reporting and disclosure obligations under ERISA be simplified. In addition, we recommend that the Department of Labor (DOL) clarify that “employer commonality” is not required to establish a MEP. While the Chamber believes that there is no reason to apply this requirement to MEPs, there is sufficient ambiguity to create reluctance on the part of employers that might otherwise consider participation in a MEP.³²

5. Give Small Businesses a Dedicated Voice on Advisory Councils

Small businesses play an important role in the debate over the effectiveness of the voluntary employer-provided system; therefore, it is important to increase their representation in the debate. The advisory councils to the DOL, Internal Revenue Service (IRS), and Pension Benefit Guaranty Corporation (PBGC) are important sources of input to those agencies. However, none of them have a seat specified for small business.³³ An important way to increase the voice of small business in the discussion of the employer-provided system is to have a small business representative on each of these advisory councils.³⁴

B. Streamline Notice Requirements and Allow for Greater Use of Electronic Disclosure

Consolidating and streamlining certain notice requirements would make retirement plan sponsorship more attractive for all

business and for small businesses in particular. Currently, plan sponsors and participants are overwhelmed by the disclosure requirements. This feeling is particularly acute for small businesses that may not have a human resources department to focus on notice requirements.³⁵ Furthermore, the notice requirements do not occur in a vacuum. Most employers that offer a retirement plan also offer other benefit plans such as a health care plan, so they are also subject to those notice requirements. Additionally, employers are required to provide many other notices outside of the ERISA context.

In general, the Chamber recommends a congressional review of all retirement plan notices under ERISA and the tax code to determine where there is overlap and duplication. We offer the following specific recommendations:

- Eliminate the notice for the 3% nonelective safe harbor. It may have served a policy purpose at one time, but it appears to serve no purpose today.
- Include the 401(k) safe harbor match information in the Summary Plan Description rather than leaving it as a stand-alone notice.
- Replace quarterly investment statements with annual notices for participants who have Internet access to their investment account information.

Many more notices can be consolidated or eliminated. A thorough Congressional review could identify many ways of relieving unnecessary administrative burdens of little or no utility while ensuring that participants receive information that is meaningful and relevant.

In addition to consolidation and elimination, it is important for regulators to recognize the benefit of electronic delivery, which is faster, cheaper, and better than any other form of delivery. Among the reasons it is better, is that: senders can track delivery; the information can be easily stored by the recipient; the information can be searchable; and hypertext links can be included to guide recipients to other useful information. Moreover, we believe that it is critical for the DOL, Treasury, and the PBGC to create a single, uniform electronic disclosure standard.

To start, the Chamber recommends that the DOL's safe harbor for the use of electronic delivery of required disclosures be changed in accordance with the guidance provided under Field Assistance Bulletin 2006-03.³⁶ This bulletin provides that good faith compliance is met if pension benefit statements are provided in accordance with Treasury regulations.³⁷ According to the Treasury regulations, information may be provided electronically without consumer consent with this stipulation: the "electronic medium used to provide an applicable notice must be a medium that the recipient has the effective ability to access." The Treasury standard differs from the DOL standard in that the ability to effectively access the electronic medium is not required to be located where the participant performs his or her job duties and use of the medium does not have to be an integral part of those duties.

Beyond this initial step, we recommend that all of the agencies change their standards to encourage the use of electronic delivery and to allow, for plan sponsors that wish, electronic delivery to be the default delivery option for benefit notices. The Chamber believes that modernizing the restrictive rules on electronic delivery is a critical element in the larger task of reforming employee benefit plan notice and disclosure requirements. These changes can allow important information to be provided without being submerged in an avalanche of rarely used information.

As electronic media continue to develop, we believe that plan sponsors must have the flexibility to adapt to these changes to meet workforce needs.

C. Reform Multiemployer Defined Benefit Plan Funding

The Chamber supports comprehensive multiemployer funding reform to prevent bankruptcy among employers, including many small, family-owned businesses. Multiemployer defined benefit plans are collectively bargained and jointly administered by employers and unions. Funding comes entirely from employers, which are at financial risk when a plan faces funding problems. Demographic and industry trends—not fund management—have created significant funding problems for many employers.

Because of the nature of multiemployer plans, when one employer goes bankrupt, the remaining employers in the plan are responsible for paying the vested accrued benefits of all the workers. This is often referred to as “the last man standing.” As the number of employer participants dwindles, employers remaining in the plan see their liabilities increase exponentially—forcing them to pay for benefits for retirees who never worked for them (often referred to as the “orphan participant problem”). The remaining employers can be forced into bankruptcy by the higher contributions they must make to fund the plan or by the withdrawal liability incurred if they drop out of the plan.

Withdrawal liability is a great burden that may force employers to stay in multiemployer plans even when it is not economically feasible. The Chamber feels that a comprehensive solution must be sought to allow for a more robust multiemployer plan system and to maintain equity among contributing employers.

Another problem arises from the nature of multiemployer plan funding. Benefit increases are not anticipated in funding but are often granted at contract renewal. These increases often apply not only to active workers, but also to retirees. This practice may put the plan into an underfunded situation because the benefit increases cause a “loss” for the year. This loss is generally funded over a long amortization period, such as 20 years. While this additional expense is generally affordable for active employers that are contributing a negotiated contribution rate (usually cents per hour or a percentage of pay), a withdrawing employer may be immediately liable for its share of the underfunding.

In order to prevent bankruptcy among remaining employers in multiemployer plans and unanticipated bankruptcy on withdrawing employers, comprehensive funding reform should focus on allowing plans to be financially solvent on an ongoing basis. Examples of such provisions include, but are not limited to, partitioning plans and permitting mergers and acquisitions between certain plans.³⁸

Even for plans that are not at financial risk, changes could ensure that they remain financially viable. For instance, the assumptions used to determine withdrawal liability should

be consistent with those used to determine contribution requirements. They should not be more conservative, forcing the withdrawing employer to subsidize active employers.³⁹

In addition, benefit increases should be moderated. In the past, benefits were increased if the plan became overfunded and, as noted above, granted even when the benefit increase would make the plan underfunded. This prevented plans from being able to fall back on extra contributions in later years. As a result, any future underfunding would require additional contributions by current employers. Reform efforts should focus on moderating benefit increases so that they are not made simply because the plan is overfunded. One way to do this would be to require disclosure of the amount of withdrawal liability associated with benefit increases—not just contribution increases.

Finally, the procedural rules that allow employers to arbitrate disputes over the amount of withdrawal liability require change, at least with respect to small employers. For example, the time frame for requesting arbitration is very short, and a small employer, who may not have significant administrative resources, is likely to miss it.

The suggestions above are just examples of steps that policymakers can take. The Chamber is committed to addressing multiemployer funding issues and is willing to discuss any viable ideas that allow participating employers to remain financially solvent.

D. Reform Single-Employer Defined Benefit Funding Requirements

The number of defined benefit plans has been declining.⁴⁰ Plan sponsors face a number of challenges, the greatest of which is the need for predictability and flexibility. Since 2002, Congress has passed five laws that address defined benefit funding.⁴¹ For more than a decade, the legality of hybrid plans was unresolved, and plan sponsors of those plans were unable to get determination letters.⁴² Since the recent financial crisis, inflexible funding rules have created unexpected financial burdens for plan sponsors. All of these scenarios have had a negative impact on the employer-provided retirement system. Therefore, the Chamber urges

Congress to keep in mind the need for predictability and flexibility to ensure that employers can continue to maintain plans that contribute to their workers' retirement security.

The current economic environment creates additional challenges for employers that want to maintain retirement plans. In addition to complying with the normal set of rules and regulations, plan sponsors must make tough decisions about their retirement plans and other competing needs. The more certainty they have about the rules, the better they will be able to make these decisions.

On August 17, 2006, the Pension Protection Act of 2006 (PPA) was signed into law. The PPA fundamentally changed the funding rules for defined benefit plans. A major impetus behind the PPA was to increase the funding level of pension plans. Most plan sponsors entered 2008 ready to comply with the new funding rules, but the severe market downturn at the end of 2008 drastically changed the situation.⁴³ Because of the accelerated funding scenarios spelled out in the PPA, and notwithstanding the efforts of Congress to provide some temporary funding relief, many plan sponsors were faced with having to contribute two to three times more than they expected.

A matter of recent concern is the consideration of PBGC premium increases. Increasing these premiums without the opportunity for discussion, careful consideration of the potential impact, or buy-in from all interested parties would present another challenge to the private sector's defined benefit pension system.

Raising the PBGC premiums without making contextual reforms to the agency or the defined benefit system amounts to a tax on employers that have voluntarily decided to maintain defined benefit plans. An increase in PBGC premiums, when added to the multibillion-dollar impact of accelerated funding enacted in 2006, could divert critical resources from additional business investment and subsequent job creation.

Policymakers can take several steps to encourage sponsorship of defined benefit plans. To improve defined benefit plan funding, the law should allow for unlimited

prefunding up to the amount of projected future benefits in the plan. Additionally, the IRS should eliminate the tax penalty for the reversion of assets in a pension plan after all promised benefits have been paid out to participants.⁴⁴

E. Clarify the Hybrid Plan Rules and Regulations

The Chamber views hybrid plans as an important part of the private retirement system. Therefore, the Chamber worked for several years toward the confirmed legality of hybrid plans in the PPA (and as amended by the Worker, Retiree, and Employer Recovery Act of 2008). However, because of the previous controversy surrounding hybrid plans, they are less widespread than they should be. Therefore, we believe that the rules provided under the PPA and the ensuing guidance from the Treasury and the IRS should provide plan sponsors with enough certainty to establish and maintain hybrid plans and to allow for greater participation in these plans.

We appreciate the efforts by the Treasury and IRS to provide a framework for the regulation of hybrid plans. The PPA's hybrid plan provisions are intended to provide plan sponsors with legal certainty to establish and maintain hybrid plans and to allow for greater participation in these plans. However, we believe that greater clarification on the regulations is needed to meet these goals. For example, recently issued regulations do not contain enough information on how the PPA's hybrid plan rules are applied to pension equity plans (PEPs).⁴⁵ Under the regulations, PEPs might be subject to varying sets of rules depending on how the benefit is described, even with respect to the same benefit calculation. We urge the Treasury and IRS to set forth a clear and rational approach to PPA compliance for PEPs. More broadly, because of the complexity of hybrid plans and their regulation, additional guidance is critical to ensure that plan sponsors have enough clarity and flexibility to adopt and maintain hybrid pension plans with legal certainty.

F. Create Greater Transparency in Accounting Standards for Employer-Provided Benefit Plans

Under Sarbanes-Oxley, the Securities and Exchange Commission designates an accounting standard-setter and sets its budget. The Financial Accounting Standards

Board (FASB), a quasi public-private organization, has been designated as this accounting standard-setter. The Chamber fully supports independent standard-setting. However, dialogue and input from stakeholders is important to the process, and we believe that process improvements, such as transparency and cost-benefit analysis, are needed to ensure appropriate levels of input.

Various accounting rules and practices in the past have discouraged the continuation of defined benefit pension and retiree health care plans. Despite the best efforts of policymakers to create an environment that encourages more assertive action in these areas, these efforts can be significantly affected or undone by the actions of FASB. The negative impact of FASB standards has been seen in the area of retiree health care plans, single-employer defined benefit plans, and, most recently, multiemployer defined benefit plans. To ensure that employers are not unintentionally discouraged from participation in the retirement system, it is necessary to address the accounting practices associated with voluntary benefit plans. The following are examples of where accounting standards could or have negatively affected benefit plans.

FASB and Retiree Health Care. Over many years, retiree health benefits have helped millions of retired workers manage health care costs. However, the percentage of large employers offering this benefit has declined over the last 20 years. In 1991, 46% of large employers sponsored retiree health plans. Today the number stands at 28%.⁴⁶

The primary reason for this erosion relates to accounting rules implemented under FASB's direction. In 1990, FASB issued Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions" (FAS 106). Under FAS 106, an employer must account for the present value of future retiree health benefits on its balance sheet. However, few employers prefund for retiree health benefits because there is no tax-advantaged funding for these benefits. Consequently, the entire future liability must be included on the balance sheet of the employer's financial statement. The inequity resulting from this rule drove many employers to discontinue retiree health programs and discouraged others from implementing new programs.

FASB and Single-Employer Defined Benefit Plans. On September 29, 2006, FASB issued FAS 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans." Under FAS 158, companies were required to begin reporting the net financial status of pension and other benefits on the company's balance sheet rather than in the footnotes. In addition, plan assets and benefit obligations were to be measured as of the date of the employer's fiscal year end, and employers were to use the projected benefit obligation (PBO) measure of liabilities.

At the same time, FASB announced that there would be a Phase II in which it would evaluate and propose changes to the accounting standards for measuring pension and other postretirement benefit costs, obligations, and assets. FASB indicated that it intended to remove smoothing periods from the measure of liabilities. The intent was to coordinate Phase II with the International Accounting Standards Board (IASB) to facilitate international uniformity with the new accounting standards.

FASB's requirements create a picture of immediacy on the balance sheet for a defined benefit plan even though it is to be funded and perpetuated over the course of decades. Some plan sponsors assert that the accounting changes in Phase I have forced them to shut down their defined benefit plans. Others have stated that implementing Phase II would force them to shut down their plans. FASB has announced that it is postponing Phase II indefinitely; however, the threat of these changes remains.

FASB and Multiemployer Defined Benefit Plans. On September 1, 2010, FASB issued the Proposed Accounting Standards Update, "Compensation—Retirement Benefits—Multiemployer Plans (Subtopic 715-80): Proposed Improvements to Disclosures about an Employer's Participation in a Multiemployer Plan." The proposed standard would require employers that participate in multiemployer defined benefit pension plans to provide additional information about these plans in the footnotes to their financial statements. Most employers and the unions associated with the plans argued that many of the additional disclosures would be overly burdensome and could have a negative financial impact on businesses that contribute to multiemployer plans. In

particular, there was grave concern about the requirement to disclose a withdrawal liability estimation even if there was no reasonable possibility of withdrawal.

Persuaded by a massive effort from employers and unions, FASB substantially changed its original proposal.⁴⁷ This effort, however, required input from the administration and Congress in addition to substantial time and resources from the affected parties.

In each of these cases, additional transparency into the FASB process as well as cost-benefit analyses would have helped to prevent the unintended consequences of these changes.

G. Avoid Competition between Government Entities and Private Plan Sponsors

A number of states are trying to increase private retirement saving by their residents. In particular, some states have sought to increase retirement plan participation among

workers of small employers and nonprofit organizations by allowing these workers to join state pension programs. Others would have the state establish and maintain 401(k) or similar plan designs to cover those who work for small employers. Massachusetts,⁴⁸ Connecticut,⁴⁹ Maryland,⁵⁰ Vermont,⁵¹ and California⁵² have considered bills aimed at increasing employee participation in some form of state pension savings program.

The Chamber believes that the private sector should not be put in the position of having to compete with state governments to provide retirement benefits. State actions could have the unintended consequence of reducing economies of scale for national providers. This would make it more difficult for them to offer plans to small employers. Moreover, such programs could discourage innovation in the private sector.

II. Encourage Greater Individual Savings

Qualified plans provide significant benefits to both employers and employees by encouraging retirement saving through favorable tax treatment. They allow employers to obtain a tax deduction for plan contributions and employees to delay paying taxes on this benefit until funds are distributed. Employees do a better job saving for retirement when an employer plan is available. Payroll deduction facilitates the savings habit, and employer matching contributions, as well as the Savers' Tax Credit, provide further incentives. Recent research finds that the single best predictor of retirement readiness is participation in a work-based savings plan.⁵³

Innovation in defined contribution plan design has strengthened plan participation. Automatic enrollment makes savers out of nonsavers. Increases in automatic contributions grow employee contributions from year to year by taking advantage of inertia.

Nonetheless, some employees still do not participate in the system. Legislative and regulatory actions, as well as plan design and financial education, could lead to greater participation in retirement plans and encourage higher savings rates.⁵⁴

A. Encourage Use of Automatic Plan Features

The advent of automatic features in defined contribution plans has greatly reduced the incidence of nonparticipation, thanks to inertia. The number of plans that employ automatic enrollment has quadrupled since 2005.⁵⁵ In a SunAmerica survey, 85% of workers reported that automatic enrollment helped them start saving earlier than they would have on their own.⁵⁶ Automatic enrollment and escalation is especially successful in targeting the most likely undersavers: women, minorities, moderate-income workers, and younger workers. Automatic enrollment can increase participation among these groups from one out of five to four out of five.⁵⁷ Policymakers, employers, unions, and the benefits industry

should work to increase awareness of the benefits of automatic plan design and encourage its adoption.

1. Modify the Safe Harbor Rules

To encourage greater implementation of automatic enrollment features, the Chamber encourages Congress to modify the safe harbor rules. The safe harbor requires either (1) a minimum employer matching contribution of 100% of the first 1% deferred and 50% of the next 5% deferred, for a total contribution of 3.5% for participants who defer at least 6%; or (2) a nonelective employer contribution of 3% of compensation.⁵⁸ Specifically, the Chamber recommends removing the top end limit to increase the level of employee contributions and relaxing the matching formula to make the safe harbor more attractive to plan sponsors. For example, if the matching formula allowed for a 50% matching contribution of up to 6% of compensation deferred, it might be more attractive to employers.

2. Adjust Language Around Automatic Escalation

The Chamber also recommends certain best practices. For one, plan sponsors should be encouraged to adjust language around automatic escalation. In addition to informing participants that they can "opt out" of automatic escalation, sponsors could inform them they can "opt down" or "opt up." This sends a signal to participants that it is not an all-or-nothing decision, and that they can choose a lower or higher deferral increase rather than no deferral at all.

Also, plan sponsors should be encouraged to default participants at higher than a 3% rate. Experts advise that workers should be saving anywhere from 10% to 30% of their income for retirement.⁵⁹ However, the average contribution to a 401(k) plan is 8%.⁶⁰ If participants are automatically enrolled at a higher rate than 3%, the average deferral rate should rise.

B. Encourage Financial Education for Retirement

Employers are the primary source of retirement savings options and education for most workers. Education is critical to employees' understanding of their retirement savings options and the need to plan for retirement. Employers understand their role in providing education to their workers and rely heavily on Department of Labor Interpretative Bulletin 96-1 (IB 96-1) in defining the educational information that they can provide without fear of liability.

Many employers have years of experience providing financial education to their workers. They have broad experience with financial education alternatives, including face-to-face counseling, workshops, online sites and tools, paper-based information, webinars, and podcasts. Employers often tailor financial education to their audiences because they know—and research has confirmed—that the most effective education initiatives recognize demographic differences.⁶¹ Allowing employers to provide this education not only will help workers make important decisions at the time of retirement but can also help encourage workers to save more before they reach retirement. Providing education to workers early in their careers gives them more opportunity to properly prepare.

An obstacle to encouraging a stream of retirement income payments is that plan participants often have an “all or nothing” mind-set regarding plan distributions. This outlook needs to change. Retirement savings should not be thought of as a single lump-sum benefit payment, but rather, as a means to get a stream of income in retirement, however it may be generated.

While many employers want to provide retirement education to their workers about accumulation and decumulation strategies, a major concern is their ability to do so without incurring fiduciary liability. Employers recognize that providing financial advice is a fiduciary action, but they believe providing general retirement education should not be held to the same standard. For example, employers would like to provide a general discussion of the pros and cons of seeking a distribution and managing retirement assets outside the plan without incurring fiduciary liability.

The DOL encouraged participant investment education when it preserved the status of IB 96-1. The DOL has since asked for comments on the provision of information to help participants make choices regarding decumulation strategies. It might consider expanding IB 96-1 to allow employers to provide information to help participants to make choices regarding their decumulation strategies without its being considered investment advice. Expanding IB 96-1 to allow employers to provide information regarding decumulation products and various distribution options, including those provided in installments or a guaranteed income stream for life, would help workers to make informed decisions about their retirement savings.

C. Help Preserve Retirement Assets

An important component of retirement security is ensuring that retirees have sufficient assets to fund their retirement. Congressional action in key areas could help ensure that participants can continue to make retirement contributions during financially difficult times.

1. Permit Elective Contribution Following a Hardship Distribution

The Chamber encourages Congress to allow 401(k) plan participants to continue to make elective contributions following a hardship withdrawal. The current financial crisis has forced many workers to take hardship distributions from their retirement plans. The loss of retirement savings should not be exacerbated by prohibiting these workers from making ongoing contributions to their retirement plan.

2. Extend the Rollover Period for Plan Loans

In addition, the Chamber supports an extended rollover period for plan loan amounts after a termination of employment. Default on a loan is treated as receiving a deemed distribution of the outstanding loan at the time of the default. The participant is taxed on the amount of the default unless he or she makes a “rollover” contribution to an IRA within 60 days.⁶² Since relatively few participants make a rollover contribution in connection with a plan

loan default due to termination of employment, extending the rollover period could decrease the number of participants who default on their outstanding loans and incur tax penalties in addition to the loss of retirement savings.

It is important to note that the Chamber differentiates between using retirement assets to purchase products that may be used in retirement (such as long-term care insurance or health care costs) and using them for preretirement consumption (such as buying a car). In order to reach the goal of sufficient retirement assets, it is important to ensure that retirement assets are used for retirement purposes. While it may not always be possible to avoid using retirement savings before retirement, the Chamber believes that making the changes above could help to preserve or replenish some retirement assets that would otherwise be spent before retirement.

III. Strategies to Make Retirement Assets Last

There is growing recognition that retirement planning needs to occur throughout workers' lives; it is not something they should focus on only at the moment of retirement. While asset accumulation has long been the focus of retirement planning discussions, the decumulation of those assets in retirement has become an important consideration. As people live longer in retirement, they must consider ways to manage assets to provide a steady retirement income stream.

Policymakers, industry, and employers are increasingly focused on ways to help individuals convert their accumulated savings into retirement income streams (including guaranteed options and systematic withdrawals) that will see them through a retirement that could last more than 30 years. The Chamber supports greater education for participants, innovation among products, and flexibility for employers to try new products and programs.

A. Encourage Additional Distribution Options

To encourage continued innovation and growth of financial products, it is important that lawmakers approach decumulation issues in a product-neutral manner. Public policy in this arena should encourage education on the various distribution options and to encourage product innovation to meet the varied needs of savers and retirees.

Employers should not be required to offer specific distribution options in their retirement plans. There are many practical reasons why employers may choose to include one distribution option over another in a plan. Lawmakers should encourage and incentivize employers to implement additional payout options beyond the lump-sum option.

One deterrent to providing annuities from a defined contribution plan is the annuity selection rule. Even with DOL guidance on annuity selection from a defined contribution plan, the provider selection requirements are overly complex. It is particularly difficult for small businesses to compare different annuity options. In general, it would be helpful if, for all product choices, employers were held to a fiduciary standard regarding the providers and products to be offered through a retirement savings plan.

B. Address Required Minimum Distribution Rules

The Required Minimum Distribution (RMD) rule requires that retirement plan participants receive annual distributions from their 401(k) or IRA accounts beginning at age 70 ½. Participants may delay distributions if they are still working. However, 5% owners must begin receiving distribution at age 70 ½ regardless of whether they are working or retired.

Ideally, employers would like to see the RMD rule eliminated altogether because the rule is complicated and its application provides limited value. If the rule is not eliminated, the Chamber makes the following recommendations:

- Move the starting age to 75 to match longevity increases.

- Treat 5% owners like all other account holders and permit them to continue working and not begin required distributions.
- Exclude assets invested in longevity insurance from the distribution rules.

C. Encourage Employers to Offer Voluntary Products

There are a number of voluntary products that participants might find helpful in managing retirement assets. However, not every product will be appropriate or necessary for every participant. Therefore, we recommend that employers be able to make these products available to their workers in the most efficient and flexible way possible, such as through a cafeteria plan or with 401(k) plan savings.

1. Retiree Health Care

Medical cost for retirees is a major concern. In a 2010 study, the Employee Benefit Research Institute estimated that a retiring couple with median health expenses will need \$271,000 set aside just for health costs in retirement.⁶³

Rather than requiring that employers offer specific products or implement retiree health plans, the Chamber recommends that plan sponsors be allowed to offer insurance products and retiree health savings accounts through cafeteria plans. This step would provide important tools for employees to manage future costs in retirement. It could also reduce retiree reliance on state and federal government support systems.

2. Long-term Care Insurance⁶⁴

The increase in life expectancy is spurring a need for long-term care. At present, about 10 million Americans receive some form of long-term care, either at home or in institutions.⁶⁵ Nearly 70% of all 65-year-olds will need some form of long-term care before they die.⁶⁶

More than half of all long-term care is informal unpaid assistance provided by family members. It is estimated

that 44 million relatives and friends provide assistance to an older adult.⁶⁷ Informal care has hidden costs, including lost productivity of the caregiver.

Paid long-term care can be prohibitively expensive. A private room in a nursing home costs an average of \$78,000 per year, and home health aides cost an average of \$20 per hour.⁶⁸ Because few people carry it, long-term care insurance pays only 10% of the aggregate costs of long-term care.⁶⁹ Medicaid and Medicare together bear approximately 70% of the aggregate costs, and the remainder is paid out-of-pocket.⁷⁰

Encouraging the purchase of long-term care policies would have far-reaching benefits. It would reduce the extreme financial burden of long-term care costs to individuals and their families, and to government support systems.

Long-term care insurance policies are more affordable and accessible when the applicant is below retirement age. The cost of a basic policy with average benefits is \$1,725 a year for a 45-year old. The same policy for a 65-year old is double that amount, at \$3,451 a year.⁷¹ To help pay for long-term care insurance premiums while they are affordable, employees should be able to access 401(k) plan assets during their working years.

Another alternative is to encourage employers to offer long-term care insurance through a cafeteria plan. To motivate employers to offer long-term care insurance policies, the Internal Revenue Code provides an income tax deduction.⁷² In addition, the benefits are typically not considered taxable income to the insured. One way to increase access and affordability of long-term care insurance is to make these policies available through cafeteria plans on a pretax basis.

3. Longevity Insurance

The increase in life expectancy also increases the chances that retirees will outlive their retirement income. To avoid this situation, a retiree could purchase longevity insurance, a form of deferred annuity with a payment start date that begins at a later age in retirement.

The purchase of longevity insurance could reduce retirees' exposure to the risk of running out of income. A way to encourage this purchase would be to exclude money used to buy the product from the RMD rules.⁷³ Also, as with long-term care insurance, longevity insurance could be purchased through a cafeteria plan or with 401(k) plan savings.

D. Phased Retirement

Given current unemployment numbers, it is difficult to imagine an employment shortage. However, because of the demographics of our population, we can expect employment strains in certain industries and regions.

Although there is no official definition of phased retirement, it generally refers to any arrangement whereby a worker at or near regular retirement age continues to work, but at a reduced schedule, a reduced salary, reduced responsibility, or a combination of all three. Sometimes the phased retiree will continue receiving health benefits or will begin receiving a pension. Many phased retirement arrangements are informal, but some employers—particularly universities—have formal phased retirement programs.

Our population is aging fast, with 10,000 baby boomers turning 65 every day for the next 19 years.⁷⁴ Businesses risk facing a knowledge shortage as baby boomers retire. By 2015, 70% of managers and key professionals in many companies will be eligible for retirement.⁷⁵

Employers looking at a possible brain drain want to keep their experienced and skilled workers in order to remain competitive. Fortunately, it seems that older workers are willing to continue to participate in the workforce. A study by SunAmerica found that two-thirds of workers age 55 and over would like to work part-time before full retirement.⁷⁶

Some workers interested in phased retirement will be “planned phasers” who do so out of choice and voluntarily enter into a phased retirement arrangement. Others will opt for phased retirement out of need, typically related to financial requirements. A 2010 survey of baby boomers by

the Pew Research Center found that 60% might have to delay retirement due to the Great Recession.⁷⁷

However, several barriers exist to phased retirement. Legal barriers restrict when benefits can be paid out. Fiscal barriers include the costs associated with employing older workers, such as increased pension payments and higher health care coverage costs. Policy and practical barriers include how accruals should be calculated during phased retirement or how to apportion the payout. These barriers have prevented many employers from implementing phased retirement programs.⁷⁸

1. Continue to Treat Phased Retirement Programs and Practices as Discretionary Arrangements

Minor modifications could address barriers to phased retirement programs and practices. Most important, they should remain a discretionary arrangement that is mutually agreed upon by both the employer and the employee.

Phased retirement programs should be narrowly tailored to meet certain needs. Any rules, legislation, or proposals should be viewed with the following goals in mind:

- Keep experienced workers with critical skills in place to ensure a transfer of knowledge to younger generations.
- Combat labor shortages in specific industries and job categories.
- Allow the business to remain competitive.

2. Legislative and Regulatory Modifications Required

Current laws and regulations protect employees from forced retirement and discrimination. Phased retirement practices can operate within these bounds, so new requirements are not needed. A few small legislative and regulatory modifications are needed, however. For one, the law should be clarified to state that phased retirement benefits are not protected under Section 411(d)

(6). Deeming phased retirement a protected benefit would increase employer costs and not allow for the dynamic nature of phased retirement. In addition, restrictions against rehiring people who have recently retired should be eliminated. In-service distribution rules should be modified to better accommodate phased retirees.⁷⁹ In-service distributions should be allowed at early retirement age as defined in the plan, but not earlier. Also, plan beneficiaries who participate in a company's phased retirement program should be excluded from the general discrimination testing for the plan.

Moreover, plan payments to a current employee may constitute some or all of the employee's benefit. In addition, the Chamber recommends that employees who continue to work past early retirement age be permitted to commence receiving retirement benefits without regard to whether they reduce their work schedule.⁸⁰ These rules are appropriate because many employees who would like to continue working full-time feel compelled to terminate employment due to their inability, while still employed, to receive valuable benefits such as a lump-sum benefit based on a low interest rate or an early retirement substantial subsidy.⁸¹

Employers are also concerned that phased retirees might be held to a different standard than other employees. For example, statutory or regulatory requirements could give phased retirees a greater right to benefits (e.g., additional accruals or other form of benefit). Such requirements could make it harder to fire a phased retiree (even for cause) for fear of discrimination claims.

3. Allow, but not Require, Employers to Continue to Offer Health Benefits

Some employers allow employees in phased retirement programs to maintain their health benefits, which are valuable to these participants. Many of them are not yet old enough to qualify for Medicare but are unable to afford or qualify for insurance on the individual market. Provided there is no mandate, allowing employers to continue to offer health benefits to phased retirees (e.g., by eliminating any antidiscrimination issues provided that similarly situated phased retirees are treated similarly) would create a valuable incentive for employers that want to retain experienced employees in a phased retirement program. Providing health care benefits to phased retirees should be subject to the employer's practices as established for all workers generally.⁸²

Conclusion

The private employer-provided retirement system has contributed greatly to the retirement security of millions of American workers. The Chamber encourages action by policymakers that will maintain the success of the system and ensure that employer-provided plans continue to play an important role in retirement security.

The Chamber presents this white paper to provide guidance to ensure a path forward for the continuation of private retirement benefits. Action taken by policymakers going forward should encourage employers to maintain existing plans and sponsor new plans, encourage employees to save more through work-based plans, and identify ways to help make assets last in retirement. The future of the private retirement benefits system depends on it. The Chamber looks forward to working with policymakers on these important issues.

(Endnotes)

- 1 Investment Company Institute, Helping Working Americans Achieve a Financially Secure Retirement: How the 401(k) System Is Succeeding, July 2011, http://www.ici.org/pressroom/speeches/11_pss_ayco_401k.
- 2 Id.
- 3 Id.
- 4 Investment Company Institute, Retirement Assets Total \$17.9 Trillion in Fourth Quarter 2011, April 2, 2012, http://www.ici.org/research#retirement_research. These figures also include assets held in government-sponsored plans. Although this paper focuses on private employer plans, there is overlap in participation between private and government plans and participation in government plans is also an important part of retirement security.
- 5 The total number of pension plans, which decreased each year over the 2001–2005 period, rose for the third straight year in 2008 to approximately 718,000 plans, a 1.4% increase over 2007. The number of defined contribution plans rose by 1.6%, while the number of defined benefit plans decreased by 1.2%. (U. S. Department of Labor, Employee Benefits Security Administration. Private Pension Plan Bulletin, Abstract of 2008 Form 5500 Annual Reports, December 2010; p. 1.)
- 6 Patrick W. Sebum, “Evolution of employer-provided defined benefit pensions,” Monthly Labor Review (Dec. 1991), p. 16, <http://bls.gov/mlr/1991/12/art3full.pdf>, citing William C. Greenough and Francis P. King, Pension Plan and Public Policy (New York: Columbia University Press, 1976).
- 7 Id.
- 8 Pension Benefit Guarantee Corporation, Pension Insurance Data Book 2009, Summer 2010.
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- 11 U.S. Department of Labor, Employee Benefits Security Administration, Private Pension Plan Bulletin Historical Tables and Graphs, December 2011, p. 5. <http://www.dol.gov/ebsa/pdf/historicaltables.pdf>.
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- 14 Bureau of Labor Statistics, “Percent of Workers in Private Industry With Access to Retirement and Health Care Benefits by Selected Characteristics: 2008,” <http://www.census.gov/compendia/statab/2010/tables/10s0639.pdf> (accessed August 11, 2010).
- 15 Investment Company Institute, Helping Working Americans Achieve a Financially Secure Retirement: How the 401(k) System Is Succeeding, July 2011, http://www.ici.org/pressroom/speeches/11_pss_ayco_401k.
- 16 Id.
- 17 Consistent participants are workers who have had 401(k) accounts at the same employer every year from year-end 2003 to year-end 2009. This helps focus on account growth over time by excluding job changers, new participants, and rollover activity. See Investment Company Institute, Helping Working Americans Achieve a Financially Secure Retirement: How the 401(k) System Is Succeeding, July 2011, http://www.ici.org/pressroom/speeches/11_pss_ayco_401k.
- 18 Pension Insurance Data Book 2009, <http://www.pbgc.gov/documents/2009databook.pdf>, pp. 73–74.
- 19 SunAmerica Financial Group, The SunAmerica Retirement Re-Set Study. Redefining Retirement Post-Recession, 2011, <http://retirementreset.com/>.
- 20 Id; Tim Begany, “Retirement Planning In A Changing World,” Investopedia, December 13, 2011. Web, January 5, 2012, <http://www.investopedia.com/articles/retirement/11/retirement-planning-changing-world.asp#axzz1ibZYwN8t>; “Baby Boomers Envision What’s Next? Research and Strategic Analysis Integrated Value and Strategy,” June 2011. Web, January 5, 2012, <http://assets.aarp.org/rgcenter/general/boomers-envision-retirement-2011.pdf>.
- 21 “Baby Boomers Envision What’s Next? Research and Strategic Analysis Integrated Value and Strategy,” June 2011. Web, January 5, 2012, <http://assets.aarp.org/rgcenter/general/boomers-envision-retirement-2011.pdf>.
- 22 Id.
- 23 Centers for Disease Control and Prevention, Life Expectancy, 2007, <http://www.cdc.gov/nchs/fastats/lifexpec.htm>.
- 24 Changing the tax treatment and/or lowering contribution levels will result in lower retirement savings and fewer workers being offered retirement plans by their employers. A recent proposal authored by William Gale of the Brookings Institution would change the structure of the tax incentives for retirement savings from a tax deferral to a tax credit. In recent testimony before the Senate Committee on Finance, Jack VanDerhei, Research Director at the Employee Benefit Research Institute (EBRI), stated that under the Gale proposal the average reductions in 401(k) accounts at the normal retirement age under Social Security would range from a low of 11.2% for workers currently age 26–35 in the highest-income groups, to a high of 24.2% for workers in that age range in the lowest-income group. Another analysis by EBRI reveals that the recommendation by the National Commission on Fiscal Responsibility to limit contributions to defined contribution retirement plans to the lesser of \$20,000 or 20% of compensation will reduce retirement security for workers at all income levels, not just high-income workers. According to the study, those in

the lowest-income quartile will have the second highest average percentage reductions. Small business owners may be less likely to offer a plan to their employees if contribution limits are lowered. Proposals to reform retirement savings incentives need to focus on crafting policy that will result in better long-term retirement outcomes for Americans, rather than on short-term deficit reduction. United States Senate Committee on Finance Hearing, "Tax Reform Options: Promoting Retirement Security," September 15, 2011, <http://finance.senate.gov/hearings/hearing/?id=ba387157-5056-a032-5252-c7bf71fc6c90>.

25 It is important to note, however, that plan sponsorship among small employers is significant. The recommendations in this section are made to increase these numbers even further.

26 I.R.C. section 45E.

27 A qualified retirement plan that primarily benefits key employees—a top-heavy plan—can qualify for tax-favored status only if, in addition to the regular qualification requirements, it meets several special requirements. A retirement plan is top-heavy if more than 60% of the plan's assets are attributable to key employees.

28 I.R.C. § 416(g) ; Treas. Reg. § 1.416-1, Q M-7.

29 I.R.C. § 416(i)(1).

30 Another recommendation is to revise the rule so that, if a plan were top-heavy, the participants eligible to receive the benefit would be only those who meet the age and service requirements under Code section 401(a)(4) and 410(b) rather than all eligible individuals who remain employed on the last day of the plan year regardless of the number of hours worked in the plan year.

31 Another alternative is to use the nondiscrimination rules under Code section 403(b)(12), which are based on eligibility rather than utilization.

32 Under ERISA's definition of an "employer" that can sponsor a retirement plan, the independent provider of a MEP can be construed as a person "acting indirectly" in the interest of an employer in relation to an employee benefit plan, and a group of participating employers can be reasonably construed as a group of employers acting in such capacity (ERISA section 3(5)). By contrast, in two often-cited ERISA Advisory Opinions, the DOL found that certain organizations that were not organized primarily for the purpose of providing retirement benefits, and were open to membership by individuals and other nonemployers, were not bona fide groups of employers, and therefore were not employers under ERISA (See ERISA Adv. Op. 83-15A (March 22, 1983); and ERISA Adv. Op. 88-07A (March 28, 1988)). Thus, the Chamber believes that these Advisory Opinions can be differentiated in cases in which the "members" must be employers.

33 ERISA section 512; ERISA section 4002(h)(1); Federal Advisory Committee Act, 92.

34 The importance of the voice of small business is underscored by the President's recent decision to elevate the head of the Small Business Administration to a Cabinet-level post, <http://www.whitehouse.gov/blog/2012/01/31/cabinet-meeting-focused-small-business>.

35 Roughly 95% of small businesses have 25 employees or fewer. In addition, many do not have a human resources department or a chief financial officer. Consequently, small businesses may not have management personnel who can effectively deal with the volume of notice and disclosure requirements.

36 The safe harbor rule is found under ERISA section 2520.104b-1(b).

37 Field Assistance Bulletin 2006-03 requires compliance with Treasury regulation section 1.401(a)-21.

38 In 2010, Senator Casey introduced S. 3157, the Create Jobs and Save Benefits Act of 2010, which included a number of options for multiemployer funding reform.

39 Note that more conservative assumptions may be appropriate for "mass withdrawals," where remaining employers would be unable to continue the plan.

40 In 2007, 54 of the 100 largest employers offered a traditional pension plan to new workers, down from 58 in 2006, according to Watson Wyatt Worldwide. That 7% decline compares with a 14% drop as recently as 2005. Jennifer Levitz, "When 401 (k) Investing Goes Bad," The Wall Street Journal Online, August 4, 2008, <http://online.wsj.com/article/SB121744530152197819.html> (accessed August 21, 2009). Also see U.S. Department of Labor, Employee Benefits Security Administration, Private Pension Plan Bulletin Historical Tables, June 2010, <http://www.dol.gov/ebsa/pdf/1975-2007historicaltables.pdf> (accessed August 11, 2010).

41 Job Creation and Worker Assistance Act of 2002 (PL 107-147), increasing the range of permissible interest rates for determining pension liabilities, lump-sum distributions, and PBGC premiums for underfunded pension plans to 120% of the current 30-year Treasury bond interest rate; Pension Funding Equity Act of 2004, replacing the interest rate assumption for two years; Pension Protection Act of 2006, fundamentally changed the funding rules for both single-employer and multiemployer defined benefit plans; The Worker, Retiree, and Employer Recovery Act of 2008, providing limited funding relief; The Preservation of Access to Care for Medicare Beneficiaries and Pension Relief Act of 2010, providing defined benefit plan funding relief for both single-employer and multiemployer plans.

42 In 1999, the Service's director of employee plans issued a Field Directive that effectively halted the determination letter applications of hybrid plans from being processed. In 2002, the Treasury Department, with input from the Equal Employment Opportunity Commission and the Department of Labor, issued proposed regulations addressing the issue of age discrimination in hybrid plans but withdrew the proposed regulations in 2004 in order to clear a path for Congress to act. The uncertainty surrounding hybrid plans has been even greater in the litigation arena, with contradictory decisions among various circuit courts.

43 At the beginning of 2008, the average funded level of plans was 100%. Data from a study published by the Center for Retirement Research at Boston College (Alicia H. Munnell, Jean-Pierre Aubry, and Dan Muldoon, "The Financial Crisis and Private Defined Benefit Plans," No. 8-18, November 2008) indicate the following as of October 9, 2008:

In the 12-month period ending October 9, 2008, equities held by private defined benefit plans lost almost a trillion dollars (\$0.9 trillion).

For funding purposes, the aggregate funded status of defined benefit plans unpredictably fell from 100% at the end of 2007 to 75% at the end of 2008. (See footnote 5 of the study.)

Aggregate contributions that employers will be required to make to such plans for 2009 could almost triple, from just over \$50 billion to almost \$150 billion.

44 Realizing that there are concerns about employers raiding pension assets, the Chamber would consider the incorporation of deterrents to such actions. An example of a deterrent would be to require an employer to wait a certain period of time between paying out benefits and being allowed to receive the excess assets.

45 75 Fed. Reg. 64,197 (Oct. 19, 2010); 75 Fed. Reg. 64,123 (Oct. 19, 2010).

46 The Early Retiree Reinsurance Program: \$5 Billion Will Last About Two Years. Notes, 31, no. 7 (July 2010), p. 2.

47 "FASB Completes Redeliberations on Multiemployer Pension Plan Disclosure Project (Subtopic 715-80), FASB in Focus, July 28, 2011, http://www.fasb.org/cs/ContentServer?site=FASB&c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&c_id=1176158802030.

48 H. 1194, An Act Relative to Universal Voluntary Retirement Accounts, was introduced in 2011 in the Massachusetts Legislature. It would authorize the state to create a state-operated 401(k) plan for certain private employees.

49 In 2008, Connecticut introduced a bill mandating the state comptroller to establish a tax-qualified defined contribution retirement program to provide retirement investment plans, including 401(k) plans, to (1) self-employed individuals, (2) businesses with 100 or fewer employees, and (3) certain nonprofit organizations. An Act Concerning Small Business Retirement Plans, S.B. No. 652, 2008 Sess. (Conn. 2008), <http://www.cga.ct.gov/2008/JFR/S/2008SB-00652-ROOCE-JFR.htm>,

50 In Maryland, two bills, H.B. 1228 and S.B. 728, were introduced on February 8, 2008, and February 1, 2008, respectively. Both bills sought to establish a Voluntary Employee Accounts Program within the Maryland Supplemental Retirement Plans that would allow nonstate employers to enroll in the program to offer tax-deferred defined contribution retirement plans to their employees. Both bills died in the House and Senate, respectively. An Act Concerning Maryland Voluntary Accounts Program, H.B. 1228, 425th Sess. (Md. 2008), <http://mlis.state.md.us/2008rs/bills/hb/hb1228f.pdf>; An Act Concerning Maryland Voluntary Accounts Program, S.B. 728, 425th Sess. (Md. 2008), <http://mlis.state.md.us/2008rs/bills/sb/sb0728f.pdf>

51 In Vermont, H. 710 was introduced on January 25, 2008. The bill sought to provide deferred compensation programs for state employees, and for the employees of other eligible entities that elect to participate in the state plan. The bill set up a state board to establish and administer a plan in which assets and income are held in trust in any funding vehicles permitted by the Internal Revenue Code. The Senate version of the bill, S.354, was passed, signed by

the governor, and became law on May 20, 2008. An Act Relating to Public Agency Deferred Compensation Plans, H. 710, 2007-08 Sess. (Vt. 2008), <http://www.leg.state.vt.us/docs/legdoc.cfm?URL=/docs/2008/bills/intro/H-710.HTM>; An Act Relating to Public Agency Deferred Compensation Plans. S.354, 2007-08 Sess. (Vt. 2008) <http://www.leg.state.vt.us/docs/legdoc.cfm?URL=/docs/2008/acts/ACT162.HTM>; Vt. Stat. Ann. tit. 3, §§ 650-53 (2008).

52 In California, AB 2940 was introduced on February 22, 2008. The bill sought to establish a system of voluntary, universal, portable retirement accounts for California private employees administered by a state board. The board was expected to design programs that encourage the use of automatic features, including, but not limited to, automatic enrollment and appropriate selection of default investments. AB 2940 amended on July 10, 2008, 2008 Sess. (Cal. 2008), http://www.leginfo.ca.gov/pub/07-08/bill/asm/ab_2901-2950/ab_2940_bill_20080710_amended_sen_v94.pdf.

53 Investment News, A Survey of Retirement Readiness, October 2, 2011, <http://www.investmentnews.com/apps/pbcs.dll/article?AID=/20111002/REG/310029977>.

54 In addition to the recommendations in this section, the Chamber believes there are additional tax incentives that would encourage retirement savings. For example, the federal government should return to taxing distributions from qualified retirement plans at the lower capital gains rate, instead of the income tax rate as was done before the Tax Reform Act of 1986. However, given the current fiscal environment, we have chosen not to highlight these changes at this time.

55 Vanguard, How America Saves 2011, https://institutional.vanguard.com/VGApp/iip/site/institutional/clientsolutions/dc/howamericasaves#/Accumulating_plan_assets.

56 SunAmerica Financial Group, The SunAmerica Retirement Re-Set Study. Redefining Retirement Post-Recession, 2011, <http://retirementreset.com/>.

57 David C. John, The Business Case for 401(k) Automatic Enrollment <http://www.retirementmadesimpler.org/ResourcesAndResearch/BusinessCaseForAuto401ks.shtml#3>.

58 I.R.C. section 401(k)(13)(d).

59 The exact percentage depends on the age of the worker, desired replacement rate, and number of years until retirement. See Employee Benefits Research Institute, "Retirement Income Adequacy for Today's Workers: How Certain, How Much Will It Cost, and How Does Eligibility for Participation in a Defined Contribution Plan Help?" 31, no. 9 (September 2010), http://www.ebri.org/pdf/notespdf/EBRI_Notes_09-Sept10.HCS-RSPM.pdf.

60 Jessica Dickler, "401(k) savings hit record high," CNNMoney, February 24, 2011, http://money.cnn.com/2011/02/23/retirement/401k_contributions_rise/index.htm.

61 For example, an Ariel study on the racial wealth gap finds that African Americans and Hispanics are more likely to take loans and early withdrawals from their 401(k) plans. They trail whites in participation, contributions, and equity exposure. This is just one example of findings that point to specific issues that financial education programs should target for African American

and Hispanic workers. Ariel Education Initiative/Hewitt, 401(k) Plans in Living Color, <http://www.arielinvestments.com/content/view/354/1228/>.

62 I.R.C. §408(d).

63 Employee Benefit Research Institute, Funding Savings Needed for Health Expenses for Persons Eligible for Medicare, December 2010, http://www.ebri.org/publications/ib/index.cfm?fa=ibDisp&content_id=4711.

64 While recognizing the importance of long-term care insurance, Chamber members believe that it is also important to ensure that these insurance products are viable options. Recent articles about substantial premium increases have raised concerns about the capitalization of these products and whether they are sufficiently capitalized and reinsured. (CNN Money, January 24, 2011, http://money.cnn.com/2011/01/24/pf/long-term-care_insurance.money/index.htm; Wall Street Journal, October 16, 2010, <http://online.wsj.com/article/SB10001424052748703298504575534513798604500.html>.) Consequently, the Chamber encourages further discussion and study of these products.

65 Howard Gleckman, *Caring for our Parents* (St. Martin's Press, May 2009, p. 18).

66 *Id.*

67 *Id.*

68 *Id.*, p. 132 and p. 29.

69 *Id.*, p. 19.

70 Georgetown University Long-Term Care Financial Project, Medicare and Long-Term Care. February 2007 Fact Sheet. <http://georgetown.edu/pdfs/medicare0207.pdf>.

71 Long Term Care Insurance Premium Sample, <http://www.guidetolongtermcare.com/premiumsample.html>.

72 I.R.C. §7702B(a)(3) (2004) (explaining that “any plan of an employer providing coverage under a qualified long-term care insurance contract shall be treated as an accident and health plan with respect to such coverage”).

73 See S. 1359, Retirement Savings and Security Act of 2005, as an example.

74 Pew Research Center, Baby Boomers Approach Age 65—Glumly. Survey Finding About America's Largest Generation, December 20, 2010, <http://pewresearch.org/pubs/1834/baby-boomers-old-age-downbeat-pessimism>.

75 William C. Byham, *70: The New 50; Retirement Management: Retaining the Energy and Expertise of Experienced Workers* (DDI Press, May 2007).

76 SunAmerica Financial Group, *The SunAmerica Retirement Re-Set Study. Redefining Retirement Post-Recession*, 2011, <http://retirementreset.com/>.

77 Pew Research Center, Baby Boomers Approach Age 65—Glumly.

Survey Finding About America's Largest Generation, December 20, 2010, at <http://pewresearch.org/pubs/1834/baby-boomers-old-age-downbeat-pessimism>.

78 Nonetheless, Monsanto, a multinational agricultural biotechnology corporation headquartered in St. Louis, Missouri, has been successful with its phased retirement program. Monsanto established its Resource Reentry Center (RRC) in 1991. As of September 2006, the RRC had more than 300 active individuals, 175 of whom were on assignment in various departments, including Engineering, Finance, Law, IT, and Research and Development. The RRC offers managers and former workers a bridge to workforce changes and allows retirees to continue an active and productive relationship with Monsanto. (Joanne Sammer, “Is Phased Retirement A Win-Win?” *Business Finance* September 2006, p. 31, <http://businessfinancemag.com/article/phased-retirement-win-win-0901>.) To be eligible, one must be a former Monsanto employee and must not have been terminated for poor performance. (Monsanto Careers Resource Re-entry Center Questions and Answers, <http://www.monsanto.com/careers/opportunities/reentry/ga.asp> (last visited Dec. 17, 2008)).

79 The employer should generally have flexibility regarding how benefit accruals would be earned for future service. For example, future service could be aggregated with prior service in determining a total benefit against which the value of the prior distribution would be offset. Or future service could be credited as though the employee were newly eligible. In some cases, the former approach will create a larger benefit; in other cases, the latter approach is more favorable for a participant. As with all issues relating to the size of the benefit offered under a plan, the decision as to which approach to use—including variations not described here—lies with the sponsoring employer. Of course, the choice must be clearly disclosed to the participants.

80 Any rule that conditions plan payments to a current employee on a prescribed reduction in the employee's work schedule would fail to be effective with respect to employees who would like to continue to work full-time, but terminate to obtain a current payment.

81 In July 2000, Senator Charles Grassley and Congressman Earl Pomeroy introduced the Phased Retirement Liberalization Act (S. 2853/H.R. 4837), which would permit pension plans to make distributions upon an employee's attainment of the earliest of (1) normal retirement age, (2) age 59½, or (3) 30 years of service. The Chamber views this as a good example of legislation that could facilitate a healthy policy discussion of the critical phased retirement issues.

82 There are additional changes that may be needed in the Social Security System to further encourage phased retirement. However, changes to the Social Security system are beyond the scope of this paper.



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