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Will There Be SAFE Passage for a Grab-Bag of ERISA Changes?

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The Internal Revenue Code of 1986 (the ''Code'') and the Employee Retirement Income Security Act of 1974 (''ERISA'') have long provided comprehensive and complex rules governing the private U.S. retirement system. Over time, Congress tinkers with what it has wrought, and sometimes makes significant changes to basic rules.

In July 2013, Sen. Orrin G. Hatch (R-Utah) introduced the Secure Annuities for Employee Retirement Act of 2013 (the ''Act''),[2] or the SAFE Act. The introduction of the Act attracted a modicum of publicity in light of the provisions in Title I of the Act that attempt to address the troubled state of government pension plans.[3]

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[2] S. 1270 (July 9, 2013), *available at* https://www.congress.gov/bill/113th-congress/senate-bill/1270/text.

[3] See, e.g., ''Press Release: Hatch Pension Overhaul Plan Receives Top Grade From the Urban Institute,'' (Sept. 10, 2014), *available at* http://www.hatch.senate.gov/public/index.cfm/2014/9/hatch-pension-overhaul-plan-receives-top-grade-from-the-urban-institute.

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For any number of reasons, however, the question of whether there should be what might be referred to as a public ERISA, or ''PERISA,'' has always been a contentious and political issue.[4] As a result, the path to passage of the public-plan provisions of Title I of the Act is arguably at best an uncertain one.

Flying more under the radar were the provisions in Title II of the Act, which include a fairly extensive grab-bag of miscellaneous changes. It turns out that, while several of the proposed changes are highly technical in nature, some of them are significantly substantive. The Title II provisions are generally less politically charged, and in a number of cases may not be overly controversial.

Shortly before the President's 2015 State of the Union Address, Sen. Hatch indicated that the Act will be re-proposed.[5] With Sen. Hatch's ascension to the chair of the Senate Finance Committee, several of the Act's less politically-charged provisions may well be poised to become law, particularly in light of the possible desire of Democrats and Republicans alike to find some area of common ground.

In light of this background, the authors believe it is now SAFE to outline the proposals included in Title II of the Act, as previously introduced. A summary of Title II of the Act follows below.

Discussion

Stemming from the overarching policy of ensuring adequate retirement income for retirees, the Act's Title II reforms seek to encourage employers to establish and maintain retirement plans and amend current laws that

[4] Reflecting the legislative tension over whether ERISA should address pension security for government employees, ERISA included a provision, Section 3031, that required Congress to study the state of retirement plans established, maintained or financed by federal, state and local governments and their political subdivisions, agencies and instrumentalities. See PENSION TASK FORCE OF THE H. COMM. ON EDUC. AND LABOR, 95TH CONG: REPORT ON PUB. EMP. BENEFIT RETIREMENT SYSTEM (Comm. Print Mar. 15, 1978); *Public Employee Pension Benefit Plans: Joint Hearing Before the Subcomm. on Oversight of the H. Comm. Of Ways and Means and the Subcomm. On Labor-Management Relations of the H. Comm. On Education and Labor*, 98th Cong., Nov. 15, 19desc83.

[5] ''Sen. Hatch to Reintroduce SAFE Act; Bill would Shift Fiduciary Rule to Treasury,'' (13 PBD, 1/21/15)(Jan. 21, 2015).

discourage employers from maintaining retirement plans.[6]

The proposals under Title II of the Act include, for example, expanded plan-design options, simplified administrative and notification requirements, extended deadlines and the elimination of certain restrictions on rollovers and forfeitures.

These proposals may have evolved over time out of frustration with shortcomings in the law or efforts to identify areas particularly ripe for relatively non-controversial improvement. Indeed, one almost gets the sense that an effort was made to scour the legislative and regulatory halls in an attempt to collect an array of identified trouble spots and other potential improvements—arguably, quite a worthwhile endeavor.

I. 401(k) Provisions

A. ''Starter 401(k)'' Plan (Act § 201)

Perhaps the most substantive proposed change in Title II of the Act is the addition of a new tax-preferred savings vehicle referred to as a ''Starter 401(k),'' which was identified by Sen. Hatch as a centerpiece of the Act's private pension reform.[7] The Starter 401(k) would be available to employers who don't already have a retirement plan in place, enabling them to maintain a retirement savings vehicle without the administrative burdens or contribution obligations of a traditional 401(k) plan.

Under a Starter 401(k), an employer would automatically contribute a minimum of 3 percent of each employee's compensation to the plan, subject to the employee's election to opt out. The maximum contribution for an employee would be capped at the lesser of 15 percent of the employee's compensation and $8,000 (as adjusted for cost-of-living increases), which would be a limitation that is potentially higher than the maximum annual contribution to an individual retirement account (IRA), which under Section 408(a)(1) of the Code is presently $5,500 ($6,500, with a catch-up contribution).

Thus, a Starter 401(k) would help employees save for retirement with their own funds to a greater extent than they could on their own.[8] The Starter 401(k) seems to draw together elements from existing law, including (i) the automatic employer contribution that is the hallmark of the existing ''safe harbor'' and ''SIMPLE'' 401(k) plans,[9] (ii) the automatic enrollment provisions applicable to certain 401(k) plans,[10] and (iii) the higher IRA contribution limits applicable to SIMPLE IRAs.[11]

B. Other Provisions Relating to Automatic Enrollment

The Act has other provisions that seek to increase employee saving by encouraging the adoption of automatic-enrollment provisions.

1. Automatic Enrollment Safe Harbor (Act § 220). The Act would add a new 401(k) ''safe harbor'' if the plan provides for certain minimum default contribution rates via automatic enrollment features. A retirement plan would meet this safe harbor if minimum default levels of contributions were set at no less than 6 percent in the first year of an employee's participation, no less than 8 percent in the second year, and no less than 10 percent in all subsequent years, provided that the employer makes matching contributions equal to 50 percent of an employee's elective contributions up to 2 percent of the employee's compensation and 30 percent of an employee's elective contributions from 2 percent to 8 percent of the employee's compensation. This safe harbor would be exempt from nondiscrimination and top heavy testing (similar to the current 3 percent matching safe harbor).

2. Relaxing Limitations on Automatic Contributions (Act § 204). The Act proposes to relax the generally applicable limits on contribution rates under ''qualified automatic contribution arrangements'' (''QACAs''). Under a QACA, each employee that has not made an affirmative decision to participate in the plan is treated as having elected to defer at least 3 percent of his or her compensation until the end of the participant's first full year of participation.

If initially set at the 3 percent minimum, contribution rates must be increased by 1 percent for each of the next three successive years, such that the employee elective contribution percentages are 4 percent of compensation in the second year, 5 percent in the third year and 6 percent for the fourth and all subsequent plan years. Under current law, an employer establishing a QACA has discretion, subject to these minimum contribution rates, to set the initial level of automatic contributions as well as automatic increases, so long as the automatic contribution rate does not exceed 10 percent of the participant's compensation. The Act would eliminate the 10 percent limitation for any year after the first year of the employee's participation in the plan.

3. Additional Tax Credit (Act § 220). The Act proposes to add an additional tax credit, based upon a percentage of matching and nonelective contributions, available to small employers who adopt the automatic enrollment safe harbor described above. The amount of the credit would be equal to 10 percent of the total amount of employer and employee contributions on behalf of all non-highly compensated employees. The maximum annual credit is $10,000, available for each of the first three years of a new plan's adoption.

C. Hardship Distributions (Act § 214)

The Act proposes to allow participants to access earnings on their elective contributions when calculating the maximum distributable amount for a hardship distribution, and to permit participants to take hardship distributions with respect to safe harbor contributions, qualified non-elective contributions and qualified matching contributions.

In addition, the Act would eliminate the requirement that participants take a plan loan prior to taking a hardship distribution and also eliminate the prohibition on employee deferrals or employee contributions for at least six months following a hardship distribution. Arguably, a loosening of the restrictions on taking hard-

[6] See ''Prepared Remarks: Statement on the Senate Floor: Introduction of the SAFE Retirement Act of 2013'' (July 9, 2013), *available at* http://www.hatch.senate.gov/public/_cache/files/7644a3b9-be99-4e6f-bb2f-4f691bf50640/Hatch%20Floor%20Statement%20SAFE%20Retirement%20Act.pdf (''SAFE Floor Statement'').

[7] See SAFE Floor Statement.

[8] See *Id*.

[9] Code § § 401(k)(11)(B), 401(k)(12)(B).

[10] See Code § 401(k)(12)(B).

[11] See Code § 408(p)(2)(B)(ii).

ship distributions could have the unintended consequence of making less money available for eventual retirement, and it isn't clear that the proposed changes in the name of simplifications would be an improvement from a policy perspective.

D. Certain Other Safe-Harbor Provisions

1. Notice-Related Provisions (Act § § 206, 211). Although regarded by many as a beneficial and often preferred plan option, safe harbor 401(k) plans can be subject to a number of requirements that may be perceived by some as somewhat inflexible and otherwise burdensome. The Act would loosen the rules for safe harbor 401(k) plans to allow a plan to be amended after the beginning of a plan year to provide that a plan will meet the safe harbor requirements for that plan year.

In addition, the Act would enable employers to wait until after the end of the plan year to elect ''safe harbor'' status for a 401(k) plan, to upgrade a SIMPLE IRA savings plan to a safe harbor 401(k) plan and to adopt certain discretionary plan amendments at any time before the due date for filing the tax return of the employer. Finally, the Act would allow any amendment to a safe harbor 401(k) plan to be made during the year as long as the amendment, considered with any other plan provisions and amendments, wouldn't cause the plan to violate the enumerated safe harbor requirements.

2. Use of Forfeitures (Act § 216). The Act would allow plan sponsors to fund safe-harbor contributions with forfeitures. Such forfeitures could be reallocated as either matching or employer nonelective contributions, at the discretion of the plan sponsor.

II. Increased Tax Credit (Act § 202)

The Act contains a proposal relating to tax credits in addition to the proposal described above with respect to 401(k) plans that have certain automatic-enrollment features. Section 45E of the Code presently provides for a tax credit to subsidize the establishment or administration of a new retirement plan and retirement education provided to plan participants.

To be eligible for the credit under Section 45E, generally, an employer must have 100 or fewer employees who earn at least $5,000 in the relevant plan year. The current credit is capped at the lesser of 50 percent of the start-up costs or $500 for each of the plan's first three years. The Act proposes to increase the $500 annual limit to $5,000, available for use in each of the first three years of the plan's operation.

III. Plan Adoption (Act § 205)

The Act proposes that, for employers that would like to start a new retirement plan, the employer need only adopt such plan on or before the due date (with extensions) for the employer's tax return and the plan will be treated as if it had been adopted on the last day of the taxable year to which the tax return relates.

IV. Disclosure-Related Provisions

A. Summary Plan Descriptions, Generally (Act § 242). Under the Act, a summary plan description (an ''SPD'') would only need to be updated for so-called ''required amendments''—i.e., those amendments necessary to comply with legislative and regulatory changes—prior to the plan's restatement deadline.

B. Qualified Preretirement Survivor Annuities (Act § 217). A notification regarding the election to take a qualified preretirement survivor annuity would be relaxed so that it could be provided within a reasonable period after the employee becomes a participant in the plan, and such a notice would be able to be incorporated directly into the SPD.

C. Other Inclusions of Notices in the SPD (Act § 222). In addition to allowing notices relating to qualified preretirement survivor annuities to be included in SPDs, as described above, the Act would allow notices relating to matching contributions to be included in the SPD, in lieu of the provision of periodic notices.

D. Electronic Communications (Act § 241). The Act would allow plan sponsors to use websites and other electronic means to deliver communications to participants and beneficiaries. The Act provides that all notices that are either required or permitted to be provided to plan participants and their beneficiaries may be provided in electronic form so long as the system of dissemination is designed to result in participant access to the documents and plan participants have the opportunity to opt out of electronic disclosure and instead receive paper notices.

Prior to any electronic disclosure, the plan sponsor must give prior notice of the imminent electronic disclosures, including a description of the participant's right to opt out of electronic disclosure.

V. Required Minimum Distributions

A number of the Act's provisions are targeted at allowing participants to retain assets in tax-preferred vehicles for longer periods of time or otherwise increasing options regarding other forms of savings.

A. Mortality Tables (Act § 232). The Act would require that mortality tables used in connection with the determination of the amount of required minimum distributions (''RMDs'') be updated within one year of the date of enactment of the Act and thereafter at least once every five years, thereby enabling participants to keep more assets in their retirement accounts.

B. Roth Conversions (Act § 233). Continuing a trend expanding the availability of Roth conversions, participants and beneficiaries would be allowed to elect to convert their RMDs into Roth amounts. While this change could result in short-term increases in tax revenues, one can reasonably wonder what the trend towards ever increasing the availability of Roths will have on future tax revenues.

C. Annuities (Act § 215). The Act would eliminate the requirement to make annual RMDs with respect to the portion of an account used to purchase a deferred joint and survivor life annuity for up to 25 percent of the account balance, so long as the annuity is purchased on or prior to the participant's initial RMD.

VI. Certain Miscellaneous Changes

A. Third-Party Annuity Providers (Act § 234). The Act would allow an employer to transfer responsibility for administering the joint and survivor annuity rules to a third-party annuity provider.

B. Life Insurance (Act § 215). The Act would allow a limited exception to the rule that prohibits an IRA from holding life-insurance contracts in cases where the life-insurance contract was transferred to the IRA through an eligible rollover distribution from a tax-qualified plan or tax-sheltered annuity and the life-insurance contract satisfies applicable incidental death-benefit requirements.

C. Top-Heavy Plans (Act § 212). The top-heavy rules of Section 416 of the Code are viewed by many as arcane and cumbersome, and maybe even unnecessary in light of the nondiscrimination rules applicable to tax-qualified plans. The Act generally would prospectively eliminate the vesting and minimum-benefits requirements under Section 416. However, to the extent that a top-heavy plan had accrued benefits prior to Jan. 1, 2014, the plan would still be subject to vesting rules for any accrued benefits derived during the plan year.

D. Eliminating Certain Barriers with Respect to Multiple Employer Plans (Act § 207). Multiple employer plans generally are plans in which several employers jointly sponsor and maintain a plan with individual accounts, similar to a 401(k) plan, potentially enabling the employers to use their combined bargaining power to drive increased plan features and lower fees.

Currently, compliance failures on the part of one employer under a multiple employer plan can affect the qualification of the plan with regard to participants of another employer. The Act would address the risk that the actions of one employer could affect the qualification of the portion of the plan covering any employer that has satisfied the relevant requirements.

Employers would be unaffected by the noncompliance of another employer so long as the plan was administered by a ''designated plan provider,'' which would be a person that has registered with the Secretary of the Treasury and consented to audits in the Secretary's discretion.

The Act would also simplify various administrative and notice requirements for a ''small multiple employer plan,'' which is defined under the Act as a plan that doesn't have more than 2,500 participants and that includes no employer sponsor that has more than 500 employees as participants in the multiple employer plan.

E. Certain Terminations of 403(b) Plans (Act § 219). The Act would allow balances under Section 403(b) custodial accounts and annuities to be distributed upon termination of the 403(b) plan in the same manner as fully-paid annuities can be distributed under current Treasury guidance.

F. Rules Relating to the Form 5500 (Act § 243). The Act would change the thresholds triggering annual plan-audit requirements to thresholds based on the number of participants with account balances or accrued benefits rather than the number of eligible participants.

G. Corrections Program (Act § 235). Due to the increasing complexity of plan documents and regulatory compliance burdens, the Act would modify the Employee Plans Compliance Resolution System (''EPCRS'') by expanding the IRS Voluntary Correction Program to allow for more internal self-corrections and to reduce correction fees.

Specifically, the Act would allow for self-correction of loan errors and inadvertent errors with regard to delinquent distributions of RMDs. The Act would also require the Secretary to expand EPCRS to allow custodians to correct certain inadvertent errors, including waivers of the IRA excise tax under Section 4974 of the Code and waivers of the 60-day rollover requirement (where the deadline is missed for reasons beyond the reasonable control of the account owner).

VII. Administrative Regulatory Changes (Act § 301)

The Act would reverse, in part, administrative transfers of authority under the Reorganization Plan No. 4 of 1978 from the Internal Revenue Service (the ''IRS'') to the Department of Labor (the ''DOL''). In particular, authority relating to prohibited transactions under Section 4975 of the Code would be returned to the IRS. The authors are concerned about this proposal, in that we could return to a situation in which interpretations of similar provisions under the Code and ERISA wouldn't necessarily be consistent. It is also worth noting that the DOL has built up substantial expertise over time with prohibited transactions under the Code as well as under ERISA.

The Act would also transfer back to the IRS all authority with respect to professional standards of care owed by brokers and investment advisors to account holders, whether involving fiduciary, suitability or other standards. An effect—and maybe even an intent[12]—of the proposal to return this authority back to the IRS could be to hinder the DOL's controversial efforts to re-propose and ultimately adopt changes to the ''investment advice'' regulations that relate to the definition of ''fiduciary'' under ERISA and Section 4975 of the Code.[13]

Conclusion

While there is arguably no clear path to enacting the higher-profile PERISA-type provisions of Title I of the Act, there may be relatively SAFE passage for some of

[12] See ''Senator Hatch to Reintroduce SAFE Act'' (quoting Sen. Hatch as saying that ''[it] only makes sense to give Treasury the lead; after all, the fiduciary duty rule for IRAs is in the tax code.''); see also Arthur D. Postal, "Hatch Vows to Trip DOL's Drive to Expand Fiduciary," Insurancenewsnet.com, December 16, 2014, *available at* http://insurancenewsnet.com/innarticle/2014/12/16/hatch-vows-to-trip-dols-drive-to-expand-fiduciary-a-579574.html (quoting Sen. Hatch as stating that the Act "takes action to stop the Department of Labor from unilaterally over-regulating 401(k) plans and IRAs''); "Sen. Hatch's 2015 Priority: Torpedo DOL Fiduciary Efforts," ThinkAdvisor.com, December 15, 2014, *available at* http://www.thinkadvisor.com/2014/12/15/sen-hatchs-2015-priority-torpedo-dol-fiduciary-eff (quoting Sen. Hatch as stating "[we] shouldn't have the DOL writing these sort of things").

[13] 29 C.F.R. § 2510.3-21(c); 26 C.F.R. § 54.4975-9(c).

the grab-bag of under-the-radar goodies contained in Title II of the Act. It may be a good time to become familiar with some of these provisions now that Sen. Hatch has indicated that he will re-introduce the Act. It could be that he and the Senate Finance Committee may well attempt to build consensus and move the Act forward.