

Notes

Retirement Policy Directions in 2017 and Beyond

By Stephen Blakely, Employee Benefit Research Institute

A T A G L A N C E

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First, because of the new majority's plans to overhaul the entire U.S. tax structure and federal budget in ways that could fundamentally change how private-sector retirement plans are treated in the tax code. Retirement, as a stand-alone issue, is no longer a high legislative priority in Washington.

And second, because of the drive to simplify and lower income tax rates, tax-favored retirement provisions in the tax code are vulnerable. As one of the top sources of "revenue foregone" by the federal government, ending or reducing current tax breaks for employment-based retirement plans (particularly 401(k)s) would free up revenue for other things the new Congress and president want to do.

These and other issues were discussed at the Employee Benefit Research Institute's December 2016 policy forum in Washington, DC, attended by more than a hundred people, on the topic "Retirement Policy Directions in 2017 and Beyond." Panelists included:

- Shai Akabas, director of fiscal policy at the Bipartisan Policy Center.
- Randy DeFrehn, executive director of the National Coordinating Committee for Multiemployer Plans.
- Alane Dent, vice president for federal affairs at the American Council of Life Insurers.
- Josh Gotbaum of the Brookings Institution Retirement Security Project and former director of the Pension Benefit Guaranty Corp.
- Brian Graff, CEO of the American Retirement Association.
- Will Hansen, senior vice president of retirement policy with the ERISA Industry Committee.
- Randy Hardock, a partner in the benefits law firm of Davis & Harman, a former staffer with the Senate Finance Committee, and a former official in the U.S. Treasury Department.
- David John, a retirement expert with AARP and the Brookings Institution.
- Eugene Steuerle, a tax expert with the Urban Institute.

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Speaking at the Employee Benefit Research Institute's December 2016 policy forum, **Brian Graff**, CEO of the American Retirement Association, said retirement savings incentives in the current tax code are an inevitable target to help finance Republicans' other priorities. "They want to do tax reform that's revenue neutral, they want to lower rates, they want to lower taxes on investments, and they want to lower corporate rates," Graff said. "To be revenue neutral, the money that has to come from someplace else, and historically, we [retirement tax preferences] have been a target to pay for other priorities."

Graff added that policymakers in Washington today are not focused on retirement savings in the same way as those in the retirement sector. Specifically, he cited recent comments by Rep. Kevin Brady (R-TX), chairman of the tax-writing House Ways and Means Committee, calling for a radical simplification of the federal tax code.

"He mentioned the importance of savings and that Americans aren't saving enough—but the conversation wasn't about *retirement* savings, it wasn't about *saving for health care*, it wasn't about *saving for education*. It was about *reducing the taxes on capital gains*," Graff said. "They're not talking about retirement—they're talking about the way to increase savings is by reducing the taxes on investments."

Since more than 80 percent of capital gains tax incentives go to households with over \$250,000 in adjusted gross income, he added, "I don't think there's much of a debate about who gets the incentives for reductions in capital gains, and that's the problem: We're not even viewed as savings in that prism."

Randy Hardock, a partner in the benefits law firm of Davis & Harman, a former staffer with the Senate Finance Committee, and a former official in the U.S. Treasury Department, agreed that existing tax-code preferences for retirement programs are at high risk in the new Congress and with the Trump administration.

"Quite honestly, it is incomprehensible to me that Congress will not go after retirement plans in some way in tax reform, even if it's just trying to shift from traditional retirement savings to Roth-like vehicles, because it raises money [for the federal budget]," Hardock said. "Over the short term, it raises money generally from higher-income people. But they are going to move in that area and there are ideas out there now."



He also predicted that this will happen quickly in the early days of the Trump administration, especially since Republicans now have full control of the federal government and will want to act fast. The retirement industry should be prepared to also act quickly if they hope to add particular provisions to legislation when it begins to move. "We do have an opportunity, things are happening," he said. "You've got to get on the train when it's leaving the station."

The EBRI policy forum, held in Washington Dec. 15, brought together more than a hundred policy experts to discuss "Retirement Policy Directions in 2017 and Beyond." A panel of 10 specialists, including industry representatives, former government officials, think-tank leaders and EBRI researchers, discussed the state of the U.S. retirement system today and what they think the future is likely to hold. This article provides a synopsis of the policy forum discussion.

A webcast of this policy forum is online at <http://bit.ly/1gE99nX>

The U.S. Retirement System Today

Hardock, with Davis & Harman, said a fundamental problem is the currently unfocused approach to retirement policy in the United States. "We have a variety of individual bits and pieces that are floating out there and it's sort of an ad hoc [retirement] policy that has been developed over time, without any real focus or any real idea of how this is going to work in the long run," he said. "The elephant in the room is that we don't really have a retirement policy in the United States. We just have these bits and pieces."

Hardock also noted that retirement issues "were not mentioned in the recent presidential campaign," partly due to other issues (especially health care) dominating the debate. He urged the retirement industry "to find a way to come up with some solutions everybody can get around to make things better."



Josh Gotbaum

Josh Gotbaum of the Brookings Institution Retirement Security Project and former director of the Pension Benefit Guaranty Corp., suggested that having a decentralized national retirement policy will eventually bring pressure on Congress to address the issue, in particular the current trend to create state-backed retirement plans for the private sector.

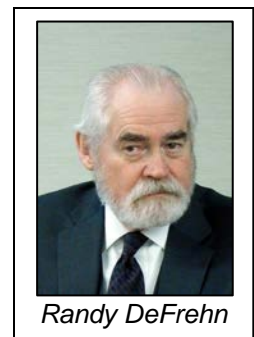
"If enough states try it in enough different ways, the financial services industry will go to Congress and say, 'We don't want 50 different rules, we're willing to live with a national requirement.' I am hopeful that that will happen...it would be the largest advance in retirement coverage, frankly, since Social Security," Gotbaum said.

However, he added, this carries the downside of removing employers from retirement plan sponsorship, which would eliminate consumer protections, education and administrative advantages of the current employer-based retirement system. "With employers out of that picture, there's a question of how do you do consumer protection...[since most] people are demonstrably not competent to protect themselves," Gotbaum said.

Randy DeFrehn, executive director of the National Coordinating Committee for Multiemployer Plans, noted that traditional defined benefit (DB) pensions are eroding "because of a host of different reasons," and that a wholesale reconsideration of the basic structure of the U.S. retirement system is needed.

"We know that there are fundamental flaws in both the defined benefit and the defined contribution systems, yet we're very reluctant to try to do something about them and take it head-on. Why don't we take the best of both worlds and really look at whether or not we can restructure the system to provide the kind of coverage that people need?" he said.

DeFrehn said other nations have been more innovative, shifting away from the traditional



Randy DeFrehn

defined benefit/defined contribution systems “to things called defined division or shared-risk plans in ways that will address some of the concerns that we talk about all the time: lifetime income, pooled longevity risk, the kinds of money management issues that very, very few of us are competent to decide on our own.”

Will Hansen, senior vice president of retirement policy with the ERISA Industry Committee, representing the nation’s largest employers, highlighted the flexibility that private-sector plan sponsors have and need under the existing voluntary retirement system. He blamed over-regulation of private-sector plans for part of the ‘coverage gap’—the roughly 50 percent of workers who do not have a retirement plan at work.



“The various agencies [government] that are out there making it too complicated for our employers to provide plans is one of the biggest reasons for the fact that there isn’t enough coverage here in America today,” he said.

Hansen stressed that employers provide a retirement plan not solely for a worker’s retirement but as “part of their total rewards package, part of their compensation package,” and that each plan sponsor needs the flexibility to craft different parts of their total compensation package to fit their needs. “If we go down the road of mandates—mandating plans across America, mandating certain products be offered—I honestly think that would just make it even worse, because that will take away the flexibility employers want to provide their employees, based on their individualized workforce,” he said.

Eugene Steuerle, a budget and tax expert with the Urban Institute, argued that it’s “a gigantic mistake” to consider retirement issues in isolation from health care and larger societal issues such as the labor force and the federal budget.



In particular, he stressed, the growing budgetary demands of the big entitlement programs (Social Security and Medicare/Medicaid), the related decline in adult employment rates and its impact on revenues, and interest on the federal debt threaten to overwhelm other pressing social needs. “If you look at all the growth schedule in government, all of it, it’s all scheduled to go for retirement and health—everything—and nothing for our kids, nothing for investment, nothing for education, nothing for infrastructure,” he said.

With the post-World War II Baby Boom generation now entering retirement and the labor force shrinking, and with the greater longevity of the U.S. population, Steuerle said the current Social Security normal retirement age structure is unsustainable. For instance, he noted that when Social Security was first established in the 1940s, the average retirement age was 68—an equivalent age of 76 today, based on remaining life expectancy. Having most people retire at 64, as they are today, hurts Social Security program’s finances, but it’s bigger impact is on personal income, personal saving, and general revenues, largely through reductions in the labor pool. “We need those people,” he said.

Graff, of the American Retirement Association, warned that those in the retirement industry are failing to understand that the policymakers who now control the federal government have a fundamentally different perspective about saving.

Graff said “we have to do a much better job to start educating, conveying the point that retirement savings *is* savings for middle America... we need to do a much better job of getting the folks who are in a position to change policy to recognize that if you really want to increase savings, it’s here—it’s in retirement—because that’s where mainstream Americans save.”



Shai Akabas, director of fiscal policy at the Bipartisan Policy Center, pointed to the Social Security system as the base of success in sharply reducing the elderly poverty rate in the last

50 years, with the employment-based system as a crucial additional component. But he added that “all these pieces don’t really work together, they’re very siloed.”

The Future

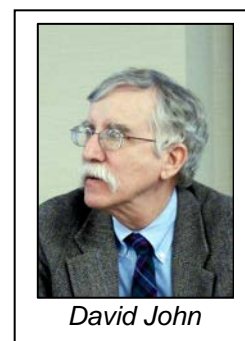
Hansen, with the ERISA Industry Committee, said a key problem is that so few members of Congress and their staff know much about current federal law governing private-sector retirement plans—specifically the Employee Retirement Income Security Act, or ERISA—and that a major education effort is needed to bring them up to speed quickly.

“There are probably five Capitol Hill staffers who know what ERISA is,” Hansen said. “Until we start to really educate America on what the importance of savings is, whether it’s for health care or retirement, we’re not going to get anywhere in this country.”

He added: “Unfortunately, we have to educate our policymakers on the importance of retirement security and we have to do it very quickly because with tax reform potentially coming down the pike within a matter of months I think we just need to play defense in order to protect a lot of those tax preference rules and regulations that we have in place.”

But **David John**, a retirement expert with AARP and the Brookings Institution, viewed that approach as a non-starter. “I don’t think we have a hope in hell of educating people into understanding retirement plans. It’s just too complex and there are too many moving pieces. And this includes employers,” he said.

John advocated expanding the “auto” structures in retirement plans (auto-decumulation, in addition to the existing auto-enrollment, auto-allocation, and auto-escalation provisions in 401(k) plans), in order “to structure something that an idiot can be successful in without necessarily having to pay someone else to do it.”



He also said employer-sponsored plans are “not sufficient” to get the coverage levels

needed to achieve national retirement income adequacy and argued for some type of retirement coverage mandate, not necessarily through an employer.



Alane Dent, vice president for federal affairs at the American Council of Life Insurers, noted that in the voluntary private-sector retirement plan system, “80 percent of full-time workers are covered by a plan and 80 percent participate, and that’s a pretty successful system.”

She said the key retirement problem “is coverage by small employers and part-time workers, and how do we get them in the system to be covered and actively participate.” Dent argued that “I don’t think we need to scrap the system, I just think we need some targeted solutions.”

Retirement Policy Under Trump and a Republican Congress

Akabas noted many proposals in the Bipartisan Policy Center’s Commission on Retirement Security and Personal Savings were included in proposed legislation on Capitol Hill (the Retirement Enhancement and Savings Act, sponsored in the last Congress by Senate Finance Committee Chairman Orrin Hatch of Utah), focusing in particular on increasing retirement coverage in the small-business sector. The measure cleared Hatch’s committee unanimously last fall, although it was not enacted into law. “For a target of what things look like 20 years from now, I think the Commission’s package is a pretty good suggestion,” he said.

Hardock said that Congress is “going to do things that raise money by moving to Roth-like [after-tax] vehicles. They’re going to do it no matter what we say. To me, the question is how can some of that money be rolled back into retirement savings?”

David John said “the big question we don’t know yet is whether the Republican House, Senate, and presidency can actually agree on what they want and come to some sort of a conclusion.” He added: “As I recall, in the last 10 years, comprehensive tax reform has been confidently predicted about three times. And as I recall, it has actually been accomplished none. So we’ll see what happens here.”

Graff noted that former Ways and Means Chairman David Camp (R-MI) offered a tax-reform proposal in 2014 that would have limited or reduced current 401(k) and IRA tax provisions, including a “double tax on employer and employee contributions at the top tax bracket. That raised about \$250 billion in a 10-year window, which is really the point: We’re a big piggy bank that they look at as money they can use for tax reform.”

This has happened in the past under both political parties, Graff added, “because we’re not the priority. We’re not seen as one of the most important things that they should be doing. And, fundamentally, it’s that indifference about retirement that is our biggest challenge.

Steuerle said that for lower-income people, “home ownership is actually more important than pensions” in terms of economic value, which makes subsidized borrowing through reverse mortgages an unhelpful policy if one cares about the wealth distribution, including among succeeding generations. He advocated tying pension reform to Social Security reform, since much larger amounts of money are affected by changes in the Social Security system and because private pension reform should be seen as an “add-on” to the larger policy issue.

He also said reforming private-sector retirement plans would have far more impact on lower-middle to middle-income Americans, since the lowest-income groups have such scattered work histories and other problems that they would not be much affected. And he argued that “the gains from additional work are extraordinary, and interestingly enough, most of them are outside Social Security”—such as big gains in income taxes and personal income.

But Akabas argued that Social Security reform by itself “is going to be incredibly hard to get much before 2034” when its trust fund is exhausted and pro-rata benefit cuts would have to take effect unless Congress solves the funding shortfall. That’s because the polar-opposite solutions being advocated by both political parties—benefit cuts by Republicans, tax increases by Democrats—are both unpopular with the public. “That’s not a great selling point,” he said.

Gotbaum noted there are various legal, regulatory, and institutional impediments to helping older workers stay on the job past normal retirement age. If more Americans are to work past age 65, he said, they will need more incentives to do so, such as rules that encourage phased retirement, a suspension of Social Security FICA taxes on post-65 workers, and “other institutional changes that will permit the demographic revolution to actually result in a workplace that works.”

David John noted this will require societal changes as well as legal ones, especially among the attitudes of both older workers and employers. “This is much deeper, more complex than anything we’ll ever solve in Washington,” he said.

Other Issues

Hansen raised the point that state-run automatic enrollment retirement plans run the risk of setting savings thresholds so low as to be ineffective.

Akabas expressed skepticism about the ability of a broad financial literacy campaign to have much impact on low savings rates. However, he did recommend focusing on specific action points that can influence individual decisions, such as postponing the claiming of Social Security benefits, working longer, and participating in workplace retirement plans when they are offered.

David John predicted that recent advances in financial technology—known as “FinTech”—will help accelerate personal savings by making it easier for people to set up flexible, low-cost “sidecar” accounts for retirement or emergency events. “The flexibility that’s coming from the advance FinTech opportunities, whether they are at scale yet or not, is going to change this debate as we go forward,” he said.



Notes

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