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Change is Coming to the Retirement Landscape

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In recent months, there has been heightened activity in Washington DC in the area of retirement policy, with plans and proposals that could meaningfully alter the landscape. Drew Carrington, head of Institutional Defined Contribution at Franklin Templeton Investments, and Michael Doshier, vice president, Retirement Marketing, discuss the latest legislative developments and ideas.

This past year we've seen heightened buzz in Washington DC about retirement. Issues and proposals have included debate over the definition of "fiduciary," treatment of multiple employer retirement plans (MEPs), and how to help more Americans better save for retirement, including those saddled with student debt.

We think the big takeaway is "Change is coming." It's no longer a question of if, but when. Whether legislation happens this year or next year, we are likely to see the most meaningful alterations to the retirement landscape since the Pension Protection Act (PPA) of 2006.

Retirement policy seems to come in waves about once per decade, so it appears now is the time to get things done. So, we feel now, more than ever, is the time to be engaged in the discussions. We've spent time in Washington talking to policymakers to help champion the cause of improving the US retirement system so that more Americans are even better prepared for the future. We will outline a few recent developments.

Department of Labor (DOL) and Association Retirement Plans (ARP)

On October 22, the DOL released proposed regulations that include a new interpretation of how "employer" is defined within the Employment Retirement Income Security Act of 1974 (ERISA). This proposal is in direct response to President Trump's August 31, 2018, Executive Order, which directed the DOL to "clarify and expand the circumstances under which United States employers, especially small and mid-sized businesses, may sponsor or adopt a MEP,"—or as the proposal calls them, "Association Retirement Plans" (ARPs)—as a workplace retirement option for their employees, subject to appropriate safeguards.

With the proposed ARP language out for comment with a deadline of December 23, we think it's likely we will see this new form of plan starting next year.

Portman-Cardin Bill to "Enhance Retirement Security"

In October of this year, we saw US Senators Rob Portman (R-OH) and Ben Cardin (D-MD) propose a new bill which proposes to "Enhance Retirement Security." This bill builds on many of the policy proposals included in other legislation before Congress, such as the Retirement Enhancement and Savings Act (RESA) and the Family Savings Act. The Portman-Cardin bill highlights several ways to expand coverage and increase retirement savings. These include:

Establishing a new, automatic enrollment safe harbor. The legislation proposes raising the minimum percentage of an individual's salary that would be deferred into a retirement plan under automatic enrollment to 6% from 3% currently in the first year.

Mandatory matching contributions. The employer would be required to make dollar-for-dollar matching contributions on behalf of all eligible non-highly compensated employees up to 1% of pay, 50 cents per dollar on the next 5% of pay, and 25 cents on the next 4% of pay, so that at least some level of matching contribution is made on up to 10% of pay.

Special tax credit and Saver's Credit. A special tax credit would apply to small employers that adopt the new automatic enrollment safe harbor. The current "Saver's Credit" is a nonrefundable credit for individuals—that is, it can reduce the amount of taxes owed, but it can't be provided as a refund. This new bill proposes to make the Saver's Credit refundable; it must be contributed directly into a retirement plan or Roth IRA. It would also expand the eligibility for a 20% credit.

Student Debt Stalling Retirement Savings

We know student debt is a challenge in the United States, particularly for younger investors who have seen their tuition costs skyrocket. US student loan debt has risen to more than $1.5 trillion, and in 2017, one-fifth of those with debt were behind on their payments.[1]

When individuals have large amounts of debt, it goes without saying that they have fewer resources for discretionary purchases—and for saving for the future. In fact, a recent survey from OneAmerica revealed nearly one in four respondents indicated they were paying a student loan for themselves or someone else, and of those, 85% said that obligation impacted their ability to save for retirement.[2]

What happens if we start addressing the student debt challenge within defined contribution (DC) plans? We think giving employees an option to funnel some of their matching retirement-plan contributions toward paying off student-loan debt is an interesting idea—although it might not be right for everyone. That is the idea behind two new student-loan legislative solutions circulating right now.

In 2016, Senator Ron Wyden (D-OR) released a draft proposal called the "Retirement Improvements and Savings Enhancement Act of 2016," which permits an employer to make matching contributions under a 401(k) plan, 403(b) plan or SIMPLE IRA on account of "qualified student loan repayments." Put simply, the proposal allows employees to direct their matching contributions toward paying off student debt, instead of saving for retirement. The other way it works is to "match" student loan repayments into the plan.

The other proposal circulating involves the ability of an employer to reimburse employees for their student loan payments on a nontaxable basis, in lieu of providing a matching contribution to a retirement plan.

DOL Fiduciary Rule: Not Dead Just Yet

The Department of Labor's "Fiduciary Rule" was vacated this year, but it may not be dead just yet, as discussions about it continue to resurface. We expect we could see more discussion on this issue in the year ahead, and it's clear that the DOL will be linked to the SEC and their "Best Interest" regulation going forward.

The Implications

Our view is that not everyone is considering the far-reaching and near-term implications this policy activity could have on the retirement landscape. One additional factor in the potential evolution of retirement plans today is the intersection of changing regulation with the availability of technology to implement those changes.

Worth noting, nobody expected PPA 2006 (which was intended to address defined benefit plan funding) to fundamentally, radically alter the way we deliver DC plans to participants. And yet, it did (and mostly for the better) due to things like an increased number of plans automatically enrolling participants.

So, we have to think about what the unintended consequences of all of the changes currently under consideration will be. What happens when you have new entities running an ARP that aren't as afraid of fiduciary litigation (because they run fiduciary risk as a normal part of their business)?

We know what statistics look like on large plans—fees, participation rates, prevalence of automation, etc. What happens if we consolidate thousands of small plans, and make them look like big plans? How many more individuals enter the system, save more and develop a habit of saving?

Despite all these unanswered questions, we are excited about the focus of the dialogue in the area of retirement, and policymakers' desire to move some meaningful policy changes toward the finish line.

Now is the time for everyone interested in helping to improve the overall retirement system to voice their opinion and participate in the dialogue. We look forward to continuing to provide solutions that better prepare people for retirement.

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1. Source: US Federal Reserve, "Consumer Credit Outstanding Levels," as of second quarter 2018; "Report on the Economic Well Being of US Households in 2017 – May 2018."

2. Source: OneAmerica® Survey: Student Loans Have Significant Impact on Retirement Preparation," August 2018.