NAGDCA Legislative Alert - 11/3/17

House Draft Tax Legislation: No Rothification, No Consolidation, No Repeal of 10% Penalty Exemption

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On Thursday, November 2, House Ways and Means Committee Chairman Kevin Brady (R-Texas) released much anticipated draft legislative language to overhaul the U.S. tax code, cutting taxes for businesses and individuals. (The committee also released a section-by-section analysis.) The draft bill's introduction marks the beginning of a major push to fulfill a central campaign promise of President Donald Trump and congressional Republicans.

After review, we can report that the "Tax Cuts and Jobs Act" (H.R. 1) does not change the pre-tax contributions to defined contribution retirement plans – so-called Rothification. Similarly, the draft does not impose consolidation of the various defined contribution plans or contain language which would repeal 457 plans' exemption from the ten percent penalty for early withdrawal. While the bill introduction is only the first step in the legislative process, we are very encouraged that Chairman Brady did not include any of the potential provisions which NAGDCA had argued were the most harmful to government defined contribution plans and participants.

The draft bill does include language (Sec. 1502) which would reduce the age at which in-service distributions can be made from 70 ½ to 59 ½ in government defined contribution plans. NAGDCA had endorsed this change, which would bring 457 plans in line with other defined contribution plans.

The H.R. 1 would make other changes to retirement plans:

- Sec. 1501 would repeal the rule allowing re-characterization of IRA contributions and conversions, effective for tax years after 2017.
- Sec. 1503 would require the IRS to change its guidance to allow employees taking hardship distributions to continue making contributions to the plan, effective for plan years after 2017.
- Sec. 1504 would permit employers to allow hardship distributions to also include account earnings and employer contributions. Currently hardship distributions may be allowed only for amounts actually contributed by the employee and may not include account earnings or amounts contributed by the employer. This provision would be effective for plan years beginning after 2017.
- Sec. 1505 would give employees whose plan terminates or who separate from employment while they have plan loans outstanding until the due date for filing their tax return for that year to contribute the loan balance to an IRA in order to avoid the loan being taxed as a distribution. The provision would apply to tax years after 2017.

- Sec. 1506 would allow expanded cross-testing between an employer’s defined benefit and defined contribution plans for purposes of the nondiscrimination rules, effective on the date of enactment.

NAGDCA appreciates that Chairman Brady’s draft acknowledges the importance of defined contribution plans as a component of retirement security for Americans and does not include provisions in H.R. 1 which would have undermined them. As the process continues with the Ways and Means Committee formal consideration of the bill – or “markup” – on Monday, November 6, NAGDCA hopes that committee members will maintain this stance at markup and through consideration on the House floor. This is particularly important as powerful interest groups mobilize to protect their favored loopholes which have been slated for closure in the draft bill. If significant revenue-generating provisions are removed or changed, it could prompt Congressional tax writers to train their sights on important features of defined contribution plans again.

Senate Finance Committee Chairman Orrin Hatch (R-Utah) has indicated that he hopes to roll out his draft bill the week of November 6. Senate rules may put more pressure on the upper chamber’s tax writers to pay for desired tax cuts, so Rothification, consolidation and repealing the exemption to the ten percent penalty could be considered, since they could generate revenue for the Treasury.

We will continue to work with Congress and to keep you updated. NAGDCA encourages its members to write to their Senators and Representatives to convey our concerns. If you have questions or comments about this legislation, please direct them to NAGDCA Headquarters so that we can review them. Although many details may not be left until and unless it becomes law, and the agencies issue implementing regulations, NAGDCA member questions are very helpful as we move forward, engaging members of Congress and their staff.