

NATIONAL ASSOCIATION OF GOVERNMENT DEFINED CONTRIBUTION ADMINISTRATORS

FEDERAL LEGISLATIVE AND POLICY PRIORITIES

117th Congress, Second Session (2022)

INTRODUCTION

Founded in 1980, the National Association of Government Defined Contribution Administrators (“NAGDCA”) is the premier professional organization of public employer-sponsored deferred compensation and defined contribution plan administrators. NAGDCA’s mission is to support plan sponsors and service providers of government-sponsored deferred compensation and defined contribution retirement plans in creating successful retirement security outcomes for their plan participants. NAGDCA governmental members oversee plans for participants from 63 state and territorial government entities and 147 local government entities, including counties, cities, public safety agencies, school districts and utilities. NAGDCA’s members administer governmental deferred compensation and defined contribution plans, including Section 457(b), 401(k), 401(a), and 403(b) plans (“DC Plans”), which provide for employee and employer contributions. The association provides a forum for working together to improve DC Plan operations and outcomes by sharing information on investments, marketing, administration, and the federal laws and regulations governing DC Plans. NAGDCA is also the sole sponsor of National Retirement Security Month, a national campaign to improve retirement security.

IMPROVE INVESTMENT OPTIONS FOR 403(b) AND DEEMED IRA PLAN PARTICIPANTS

Expand the Funding Vehicle Options for 403(b) Plans to Include Collective Investment Trusts (CITs) and Individual (Separate) Accounts

Current Law: Generally, with only limited exceptions, IRC Section 403(b) limits funding arrangements to annuity contracts issued by an insurance company and custodial accounts invested solely in mutual funds.

Proposed Policy: IRC Section 403(b) should be amended to permit collective investment trusts (CITs) and individual (or separate) accounts as investment vehicles for all types of IRC Section 403(b) plans. Corresponding changes should also be made to the Investment Company Act of 1940, the Securities Act of 1933, and the Securities Exchange Act of 1934. See Section 117, Retirement Security and Savings Act of 2019, S.1431, 116th Cong. (2019). In addition, other related rules and regulations which apply to CITs and separate accounts (such as exemptions from commodity pool status under CFTC rules and regulations, and regulations which otherwise restrict the types of investments for CITs, such as the so-called QIB rules) should be adjusted accordingly.

Rationale: Both CITs and separate accounts are common investment choices in 401(a), 401(k) and 457(b) governmental DC plans. However, due to the statutory provisions

described above, all participants in 403(b) plans are not able to take advantage of these options, potentially costing them thousands of dollars in retirement as a result of higher investment expenses or reduced returns from not having available the same breadth of investment structures as have long been available to other types of governmental DC plans. Plan sponsors would thus benefit from the use of CITs and separate accounts by having increased flexibility to build more robust investment lineups, at lower costs, often with improved speed to market or other efficiencies. In addition, CITs and separate accounts support increased customization of asset allocations and glidepaths for the 403(b) plan. Amending IRC Section 403(b) to include these additional investment vehicles has the potential to reduce costs, increase retirement security and improve the overall experience of plan members and sponsors. Finally, improved 403(b) plans can help plan sponsors better recruit and retain top talent.

Provide Clarification on Availability of Collective Investment Trusts (CITs) for Deemed IRA Accounts

Current Law: Deemed IRA accounts may be established pursuant to IRC Section 408(q) in IRC Section 401(a), 403(b) and governmental 457(b) plans. 401(a) and governmental 457(b) plans are eligible investors in collective investment trusts (CITs). IRAs are generally not considered eligible investors in CITs which instead typically restrict the investor to tax-qualified retirement plans. See for example Section 3(c)(11) of the Investment Company Act which does not enumerate IRAs. Furthermore, as noted above, there are statutory restrictions on the investment of 403(b) plans in CITs.

Proposed Policy: The IRS and SEC should issue policy clarifications, or IRC and securities laws should be amended, to confirm there is no impediment to investing Deemed IRA assets or governmental DC plan with Deemed IRAs in CITs, regardless of whether the Deemed IRA is maintained in an IRC Section 401(a), 403(b) or a governmental 457(b) plan.

Rationale: Deemed IRAs are an important policy tool for governmental DC plans as they can provide participants with lower fees and greater efficiencies than retail IRA accounts. They can also help participants create greater combined account balances in their governmental DC plans and potentially prevent leakage of retirement assets from small IRA accounts. Deemed IRAs' account aggregation can also create simplicity and ease of administration for plan participants and can allow spouses to maintain deemed IRAs in plans as well which can help with family financial planning.

CITs are common investment choices in 401(a), 401(k) and 457(b) governmental DC plans. When added to a governmental 401(a), 401(k) or 457(b) plan, the Deemed IRAs form a part of that plan. The addition of Deemed IRAs to these plans should clearly not serve as a disadvantage to these plans by jeopardizing their ability to invest in CITs. We also see no reason why 403(b) plans are not eligible CIT investors (see 403(b) policy point above) and a 403(b) that elects to establish Deemed IRA accounts should similarly

not be disadvantaged. Accordingly, we seek clarification and/or legislative changes to reflect that there is no impediment to governmental DC plans that have adopted Deemed IRA programs to invest in CITs. The availability of CITs would provide flexibility to build more robust investment lineups, at lower costs, often with improved speed to market or other efficiencies.

PROMOTE ADMINISTRATIVE EFFICIENCY AND SAVINGS

Permit Non-spousal Beneficiaries to Roll Assets to 457(b), 401(k), 401(a) and 403(b) Plans

Current Law: IRC Section 408(d)(3)(C) prohibits non-spousal beneficiaries of inherited IRA assets from rolling over such assets into their employer-based plans.

Proposed Policy: The IRC should be amended to permit non-spousal beneficiaries to roll IRA assets to their 457(b), 401(k), 401(a) and 403(b) governmental DC plans. See Section 110, Retirement Plan Simplification and Enhancement Act of 2017, H.R.4524, 115th Cong. (2017); see also Section 304, Retirement Security and Savings Act of 2019, S.1431, 116th Cong. (2019).

Rationale: Lower expenses and coordination of retirement plans are two important ways to improve retirement outcomes.

In the Economic Growth and Tax Relief Reconciliation Act of 2001 and the Pension Protection Act of 2006, Congress acknowledged that coordination of retirement plans is valuable to those with multiple retirement savings accounts. Allowing non-spousal beneficiaries to roll inherited IRA assets to their employer-sponsored plan would be beneficial to those plan participants as employer-sponsored governmental DC plans generally have lower fees and administrative costs than other retirement savings plans. In addition, allowing IRA rollovers to employer sponsored governmental DC plans would help participants achieve consolidation, enhanced portability, and administrative simplicity.

Eliminate the “First Day of the Month” Requirement in 457(b) Plans

Current Law: IRC Section 457(b) provides that deferral changes must be made prior to the first day of the month in which the change is to commence.

Proposed Policy: IRC Section 457(b) should be amended to repeal the requirement that deferral changes be made prior to the first day of the month in which the change is to commence. The proposed language would permit governmental 457(b) plans to allow deferrals changes up to a date prior to which the compensation is otherwise available. See Section 307, Retirement Plan Simplification and Enhancement Act of 2017, H.R.4524, 115th Cong. (2017); see also Section 305, Retirement Security and Savings Act of 2019, S.1431, 116th Cong. (2019).

Rationale: This provision of Section 457(b) was enacted as an administrative convenience prior to the advent of modern record keeping technology. Now it is an administrative inconvenience to delay requested changes and is an unnecessary impediment to participants' ability to manage their retirement assets. This restriction is not imposed on other retirement savings plans and should no longer apply to 457(b) plans

IMPROVE FUNCTIONALITY OF ROTH ACCOUNTS IN PLANS

Allow Participants with Roth Accounts in 457(b), 401(k), 401(a) and 403(b) Plans to Roll Roth IRA Assets into These Plans

Current law: If permitted by the respective plan, plan participants may make Roth contributions to a governmental 457(b), 401(k), 401(a) and 403(b) plan, but such plans are not permitted to accept rollovers of Roth IRA assets.

Proposed Policy: The IRC should be amended to allow 457(b), 401(k), 401(a) and 403(b) plans with Roth contributions to accept participant rollovers from Roth IRAs into these plans. See Section 504, Retirement Security and Savings Act of 2019, S.1431, 116th Cong. (2019).

Rationale: Lower expenses and coordination of retirement savings are two important ways to improve retirement outcomes.

In the Economic Growth and Tax Relief Reconciliation Act of 2001 and the Pension Protection Act of 2006, Congress acknowledged that coordination of retirement plans is valuable to those with multiple retirement savings accounts. Rolling Roth IRA assets to an employer-sponsored plan would be beneficial to those plan participants who are making Roth contributions to these plans as employer sponsored plans generally have lower fees and administrative costs than other retirement savings plans. In addition, allowing Roth IRA rollovers to Roth accounts in employer-sponsored governmental DC plans would help participants achieve consolidation, enhanced portability, and administrative simplicity.

Exempt Designated Roth Contributions from RMD Rules, as Roth IRA Assets are Presently Exempt

Current Law: Roth contributions in 457(b), 401(k) and 403(b) governmental DC plans are subject to required minimum distribution (RMD) rules and must be included when calculating the amount of a participant's RMD.

Proposed Policy: The IRC should be amended to exclude any designated Roth account in 457(b), 401(k) and 403(b) plans from RMD requirements. See Section 501, Retirement Security and Savings Act of 2019, S.1431, 116th Cong. (2019).

Rationale: The disparate treatment between Roth IRA assets and Roth assets in 457(b), 401(k) and 403(b) plans creates an incentive for plan participants to roll their Roth assets to a Roth IRA in order to avoid the RMD rules. It would be beneficial for participants to maintain Roth assets in their employer-sponsored governmental DC plans because these plans generally offer lower administrative costs and fees than retail market IRAs. The change should be revenue neutral.

ENHANCE DISTRIBUTION CHOICE

Permit 457(b), 401(a), 401(k) and 403(b) Plan Participants to Make Qualifying Charitable Distributions

Current Law: IRC Section 408(d)(8) permits “qualifying charitable distributions” (QCDs) from traditional IRA or Roth IRA accounts of up to \$100,000 to be excluded from gross income each year. The taxpayer’s required minimum distribution (RMD), made on or after the taxpayer has attained age 70 ½, or any portion thereof, may be considered a QCD and, therefore, is distributed tax free directly to the qualifying organization. This same tax break is not available for RMDs from qualified plans, 403(b) or governmental 457(b) plans.

Proposed Policy: The IRC should be amended to permit QCDs from 457(b), 401(a), 401(k) and 403(b) plans of up to \$100,000 to be excluded from gross income each year, just as QCDs are permitted from traditional IRAs. See Section 502, Retirement Security and Savings Act of 2019, S.1431, 116th Cong. (2019).

Rationale: Under current law, in order to take full advantage of a QCD, a governmental DC plan participant would have to roll plan assets to an IRA prior to the participant attaining age 70 ½ (RMDs, which begin at age 70 ½, are not eligible rollover distributions). If participants were eligible to make QCDs from their 457(b), 401(a), 401(k) and 403(b) governmental DC plans, this rollover step would not be required, and participants’ funds could remain in their governmental DC plans until such participants choose to make QCDs.

Provisions of the Tax Cuts and Jobs Act of 2017, effective in 2018, make this issue more relevant. Making QCDs from an IRA allows the taxpayer to donate RMDs tax free even if claiming the standard deduction (\$26,500 standard deduction for married couples), rather than itemizing deductions. Many more taxpayers are expected to use this increased standard deduction.

Thus, allowing governmental DC plans to have this added benefit could further incent participation and retention in governmental DC plans.

PASS A RESOLUTION SUPPORTING NATIONAL RETIREMENT SECURITY MONTH

Congressional Support for National Retirement Security Month

Background: To elevate the importance of building awareness of personal retirement planning, NAGDCA proposed the idea of a congressionally endorsed National Retirement Security Month (NRSM). Since 2006 NAGDCA has worked with members of the U.S. House and Senate who have introduced and passed annual resolutions supporting NRSM. The most recent, S.Res.404, 117th Cong. (2021), was sponsored by Sen. Benjamin Cardin (D-Md.), co-sponsored by four Republican and two Democratic senators, and adopted unanimously by the Senate on September 20, 2021.

Proposed Policy: NAGDCA proposes designating the month of October as National Retirement Security Month (NRSM) and requests that the House and Senate adopt annual resolutions supporting the ideals and goals of NRSM.

Rationale: Over the years NAGDCA has found that congressional resolutions provide powerful promotional and educational tools. However, even with the materials provided by recordkeepers and NAGDCA, many plan sponsors have found it difficult to devote time and energy to NRSM planning and programming at the same time that they are preparing and communicating for open enrollment. This has resulted in valuable NRSM messaging getting lost in all of the other communications plan sponsors circulate at that time. Designating the whole month of October as NRSM will give sponsors the flexibility to emphasize retirement security along with other open enrollment messages.

PRESERVE IMPORTANT UNIQUE PLAN FEATURES

Preserve Unique Plan Features, Generally

Current Law: Each of the different types of governmental DC Plans (IRC Section 457(b), 401(k), 401(a), and 403(b) plans) provide unique plan features due to their status as governmental plans that are important to preserve.

Proposed Policy: Maintain the unique plan features available in the different types of governmental DC Plans. Any attempts at streamlining for the sake of streamlining should be avoided; changes to the important unique provisions included in governmental DC plans should be studied for their lasting effects and risk of unintended consequences.

Rationale: NAGDCA believes that the existing unique plan features of the different types of governmental DC plans should not be changed merely for the sake of creating

consistency with other plan types (e.g. merely for streamlining or consolidation). NAGDCA is concerned about any push to create a new retirement plan type to replace existing defined contribution 457(b), 401(k), 401(a) and 403(b) plans if it would mean eliminating existing unique plan features. Further, changes to the existing structure are likely to be confusing to participants, creating risks of lower participation and savings. In addition, they could introduce potentially significant costs for modifying recordkeeping systems, and those costs would likely then fall on plan participants. In addition, plan providers may need to maintain the existing infrastructure for any grandfathered assets, resulting in more administrative complexity and participant communications challenges.

Preserve Both Pre-Tax and Roth Savings Options

Current Law: Pre-tax employee deferrals are permitted under governmental DC plans established pursuant to IRC Section 401(k), 403(b) and 457(b), as well as to plans established under IRC Section 401(a) if such deferrals are designated as pick-up contributions under IRC Section 414(h)(2). Roth deferrals are permitted under plans established pursuant to IRC Section 401(k), 403(b) and 457(b).

Proposed Policy: Current options for both pre-tax and Roth contributions in governmental DC Plans should be retained.

Rationale: Mandating a shift in retirement incentives toward after-tax savings could have adverse unintended consequences that have not been studied and could result in reduced retirement savings and decreased retirement security overall. NAGDCA's 2018 Benchmarking Survey found that while 62 percent of plans offered a Roth option, only .3 percent of reported assets were Roth assets. Roth contributions are an option that are not fully understood or fully utilized by governmental DC Plan participants and in any case Roth contributions appeal to some but not all of our participants. The immediate tax advantage created by pre-tax saving is an effective incentive for employees to enroll and to save. Losing or reducing that incentive would be detrimental to the goal of early enrollment and future retirement security. Therefore, retaining both pre-tax and Roth savings options provides the flexibility to be supportive of and responsive to the diverse needs of our participants and support their retirement readiness.

Protect Distribution Choice/Exemption from Ten Percent Penalty for Early Distributions

Current Law: Distributions from a governmental 457(b) plan are exempt from the ten percent excise tax penalty that is generally imposed on distributions made prior to age 59 ½, except to the extent such distribution is attributable to assets rolled over from another qualified plan or IRA. See IRC Section 72(t)(9).

Proposed Policy: The exemption from the ten percent excise tax penalty for distributions from governmental 457(b) plans before age 59 ½ should be retained.

Rationale: One of the ways to encourage greater savings is by reassuring prospective participants that they have some level of flexibility in accessing their savings (through hardships, loans, etc.). A participant's access to their 457(b) plan savings prior age 59 ½ and without imposition of the ten percent tax on early distributions is of immense value in marketing state and local governmental 457(b) plans.

NAGDCA surveyed its members to learn the extent to which their participants are taking distribution prior to age 59 ½ and found that only approximately 1.3 percent of total plan assets are being withdrawn annually by participants who have not reached age 60. Although rarely used, prospective 457(b) plan participants are reassured by knowing that flexibility exists in the limited but important situations that may result in separation of service prior to age 59 ½. This provision is also responsive to those participants who may be impacted by unique life circumstances requiring earlier access to their funds, without jeopardizing retirement security.

Maintain Special Catch-Up Provision in 457(b) Plans

Current Law: A governmental 457(b) plan may include a special catch-up contribution provision. Under IRC Section 457(b)(3), a 457(b) plan may permit a participant in the last three years before attainment of normal retirement age to contribute up to the lesser of: (i) twice the annual contribution limit (\$39,000 in 2020) or (ii) the annual contribution limit plus the amounts that were allowed in the prior years that were not contributed.

Proposed Policy: Maintain the availability of this feature for governmental 457(b) plans.

Rationale: This provision is frequently used by retiring government employees to defer significant payments made to them upon their severance for accumulated vacation, sick leave and compensation time benefits. It allows the retirees to defer recognition of these often-significant payments for earnings into their retirement over an extended period. Without the special catch-up they would have to recognize the additional income in the year of payment and assume a significant tax burden all at once, and their long-term retirement savings would necessarily be reduced. Many of these retiring government employees, especially public safety professionals, retire well before Medicare eligibility and transition to a second career. The additional resources in their retirement accounts help with this transition.