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THE ARGUMENT FOR RETAINING THE CURRENT TAX TREATMENT OF RETIREMENT SAVINGS

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The current tax regime for employer provided retirement plans is highly effective in accumulating retirement assets for workers at all income levels.

Total retirement assets were $20.8 trillion as of March 31, 2013.[1] Approximately $16 trillion of that amount is attributable to employer provided retirement plans. Defined contribution plans, including assets rolled over to an IRA, total approximately $9 trillion dollars. 401(k)-type plans held $4.8 trillion.

The Department of Labor Form 5500 analysis for 2010 (latest available data) reports 701,012 private sector retirement plans covering 90.6 million workers.[2] These plans hold $6.28 billion. Defined contribution plans held $3.83 billion in 654,469 plans covering 73.4 million workers. 518,675 401(k)-type plans were available to 60.5 million workers. In 2010, $250 billion was contributed to 401(k)-type plans, $88 billion from employers and $162 billion from employees.

The Bureau of Labor Statistics reports that in March 2013, employer provided retirement plans were available to 74 percent of full-time and 64 percent of all private sector wage and salary workers, with respective participation rates of 59 and 49 percent.[3] It is important to note that plan eligibility is targeted to full-time year-round workers age 21 and older. A minimum service requirement is permitted. Additionally, part-time workers working more than 1,000 hours are generally eligible under law.

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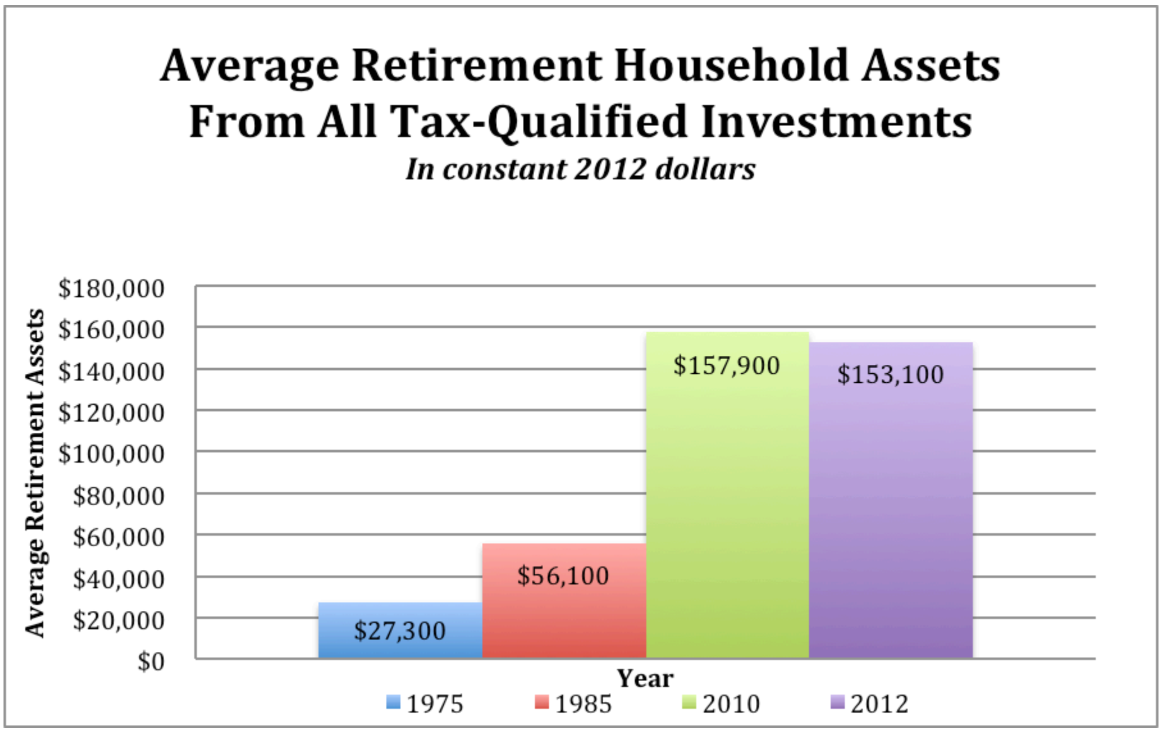
[1] *The U.S. Retirement Market, First Quarter 2013*, Investment Company Institute, June 2013.
[2] *Private Pension Plan Bulletin, Abstract of 2010 Form 5500 Annual Reports,* U.S. Department of Labor Employee Benefits Security Administration, November 2012.
[3] *Employee Benefits in the United States, March 2013,* Bureau of Labor Statistics, July 2013.

A ground-breaking analysis by the Social Security Administration that examined tax records found that in 2006, 72 percent of all private sector workers were offered a plan at work and 58 percent participated.[4]

The current tax regime has resulted in significant accumulation of retirement assets. America is not facing a retirement crisis.

In 2011, the poverty rate for people age 65 or older was 9 percent, compared to 14 percent for people age 18 to 64 and 22 percent for people younger than 18.[5]

Average household retirement assets from all tax-qualified investments, in constant 2012 dollars, grew from $27,300 in 1975 to $153,100 in 2012, a 5.6 times increase. Assets grew 2.7 times since 1985.[6]



Source: **Peter Brady, Kimberly Burham, and Sarah Holden, The *Success of the U.S. Retirement System,* Investment Company Institute, December 2012.**

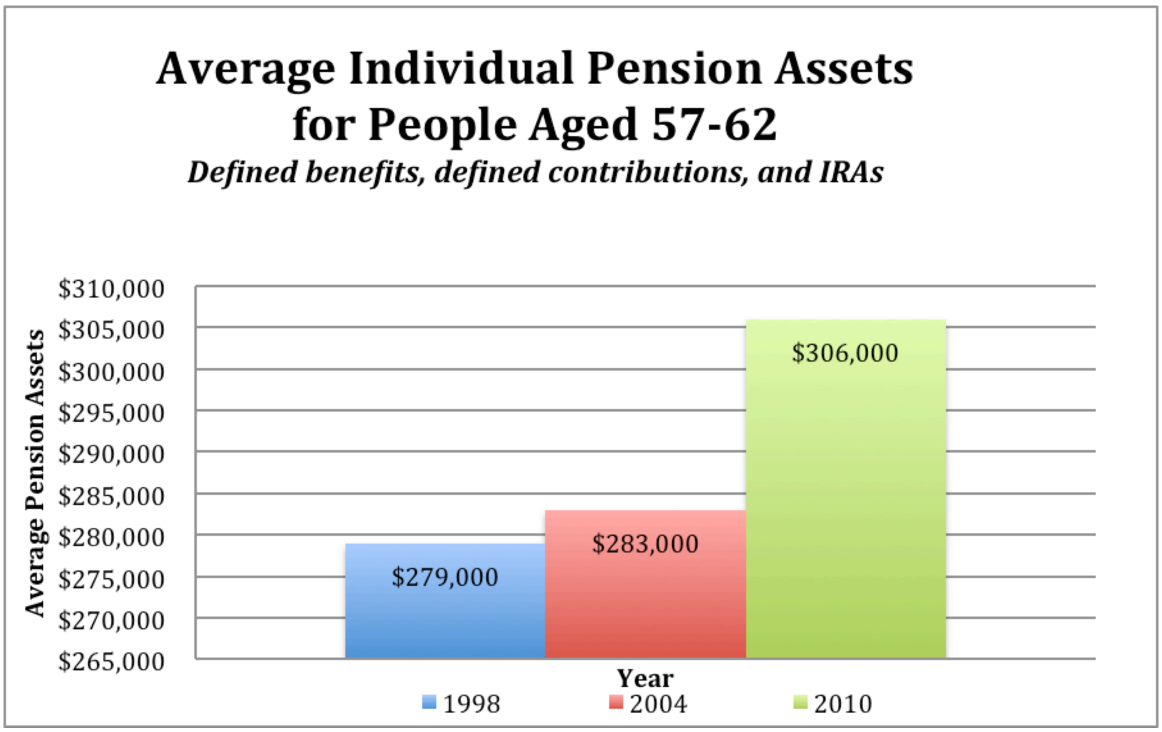
It is widely recognized that practically no retirement savings occurs outside employer plans or IRAs. In 2010 Congressional testimony, Jack VanDerhei, Research Director at the Employee Benefits Research Institute, while discussing retirement income adequacy, noted "If you eliminated the expected retirement income generated by defined benefit pensions, defined

[4] *Social Security Bulletin, Volume 71, No .2, 2011, Assessment of Retirement Plan Coverage by Plan Size, Using W-2 Tax Records,* Irena Dushi, Howard M. Iams, and Jules Lichtenstein, 2011. .
[5] Peter Brady, Kimberly Burham, and Sarah Holden, The *Success of the U.S. Retirement System,* Investment Company Institute, December 2012.
[6] Ibid.

contribution plans, and IRAs, the at-risk percentages would be even larger than without Social Security benefits."[7]

401(k) account balances provide an imperfect assessment of retirement assets. They do not reflect other assets, including additional 401(k) accounts or defined benefit plan assets, or a household's aggregate savings. The age of the participant, and how long they have been saving, distort average balances. In 2011, the average account balance was $58,991. However, for participants in their sixties with 30 years tenure with one employer, the average balance was $208,892.[8] A recent Fidelity study revealed that individuals with both workplace savings and an IRA had a combined average balance of $225,600, compared to the average 401(k) balance of $77,300.[9]

A study commissioned by the Social Security Administration found that individuals age 57-62 in 2010 held an average of $306,000 in pension assets (defined benefit plans, defined contribution plans, and IRAs). In constant 2010 dollars, individuals in the same age bracket in 2004 held $283,000 and those age 57-62 in 1998 held $279,000.[10]



Source: Alan L. Gustman, Thomas L. Steinmeier, and Nahid Tabatabai, *How Did the Recession of 2007-2009 Affect the Wealth and Retirement of the Near Retirement Age Population in the Health and Retirement Study?,* Social Security Bulletin, Vol. 72, No. 4, 2012.

7 Testimony by Jack VanDerhei, EBRI research director, before the Senate Health, Education, Labor and Pensions Committee, on "The Wobbly Stool: Retirement (In)security in America", October 7, 2010.

8 *401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2011*, EBRI Issue Brief #380, Employee Benefit Research Institute, December 2012

9 Fidelity news release, February 28, 2013.

10 Alan L. Gustman, Thomas L. Steinmeier, and Nahid Tabatabai, *How Did the Recession of 2007-2009 Affect the Wealth and Retirement of the Near Retirement Age Population in the Health and Retirement Study?,* Social Security Bulletin, Vol. 72, No. 4, 2012.

The current tax regime results in broad participation at all income levels.

All tax qualified private sector employer provided retirement plans, including 401(k), profit sharing, and defined benefit pension plans, must meet broad coverage and nondiscrimination rules that guarantee that the plans are offered to rank and file workers, that those workers participate, and that benefits are fairly provided. For 401(k) plans, the maximum salary deferral percentage rate for highly compensated participants, composed of those earning $115,000 or more in 2013, the "top-paid" group, or business owners, is mathematically tied to the average deferrals of nonhighly compensated employees. This often results in the inability of high income workers and owners to defer the maximum amount permitted under law. To address this problem, plan sponsors undertake significant measures to induce participation in the employer's plan through educational campaigns, offering matching contributions, or providing safe harbor plans that are deemed to meet the nondiscrimination tests if certain vesting and matching or nonelective contribution requirements are satisfied. In PSCA's annual survey of the 2011 plan year, 36 percent of plans used a safe harbor design to meet the nondiscrimination rules and another 28 percent of plans limited the deferral rates of highly compensated participants below the statutory limits in order to meet the nondiscrimination requirements.[11]

Vanguard's analysis of 2011 activity of 500 plans and one million workers reveals that participants earning between $30,000 and $50,000 deferred an average 5.8 percent of salary into a 401(k) type plan, compared to 7.18 percent for all participants.[12]

Other tax provisions favor low and moderate-income workers.

The top heavy rules add a second layer of vesting and contribution requirements for nonhighly compensated employees if 60 percent of plan assets are held by key employees – a very common occurrence in small employer plans.

As an additional incentive for lower-paid workers, the Saver's Credit provides a nonrefundable matching income tax credit based on retirement plan contributions.

Social Security's progressive benefit formula results in the payroll tax having greater value for lower income workers. The taxation of Social Security benefits when income exceeds certain limits also favors lower income workers who are less likely to trigger the tax in retirement.

The current tax regime has resulted in employers offering retirement plans that are absolutely critical to the retirement security of American workers.

The tax treatment of employer provided retirement plans should not be judged by an income distribution analysis, but on its effectiveness in providing retirement benefits to working families. In that regard, the evidence is overwhelming that the existence of an employer provided retirement plan is the preeminent criteria in determining the retirement assets of American workers.

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[11] *55th Annual Survey Reflecting 2011 Plan Experience,* Plan Sponsor Council of America. September 2012.
[12] *How America Saves 2012 – A Report on Vanguard Defined Contribution Plan Data,* Vanguard, June 2012.

The Congress Research Service recently reported that in 2007 only 2.6 percent of taxpayers with adjusted gross incomes between $25,000 and $50,000 contributed to a traditional IRA.[13] In comparison, the author's analysis of the Employee Benefit Research Institute's study of the March 2010 Current Population Survey (for 2009) reveals that 53.4 percent of private sector wage and salary workers age 21-64 earning between $20,000 and $50,000 worked for an employer or union that sponsors a retirement plan and 43.5 percent participated. For all workers (private sector and public) in the same category, 59.4 percent are covered and 50.6 percent participate.[14] While this is not an apples-to-apples comparison, in this analysis low and moderately-paid workers are 19.5 times more likely to participate in an employer provided retirement plan than contribute to a traditional IRA.

Employers add immeasurable value to these plans by acting as fiduciary and investment management overseers, monitoring plan fees, selecting quality investment alternatives, making very significant employer contributions, providing financial education, and encouraging and facilitating savings through payroll deductions.

Contrary to popular belief, employers gain no tax benefit from offering a retirement plan as compared to merely providing additional deductible cash compensation. In fact, they incur significant additional administrative and compliance costs, and fiduciary exposure, as the result of offering a retirement plan. Absent an attractive tax incentive, a significant majority of employers will not offer a retirement plan to their workers.

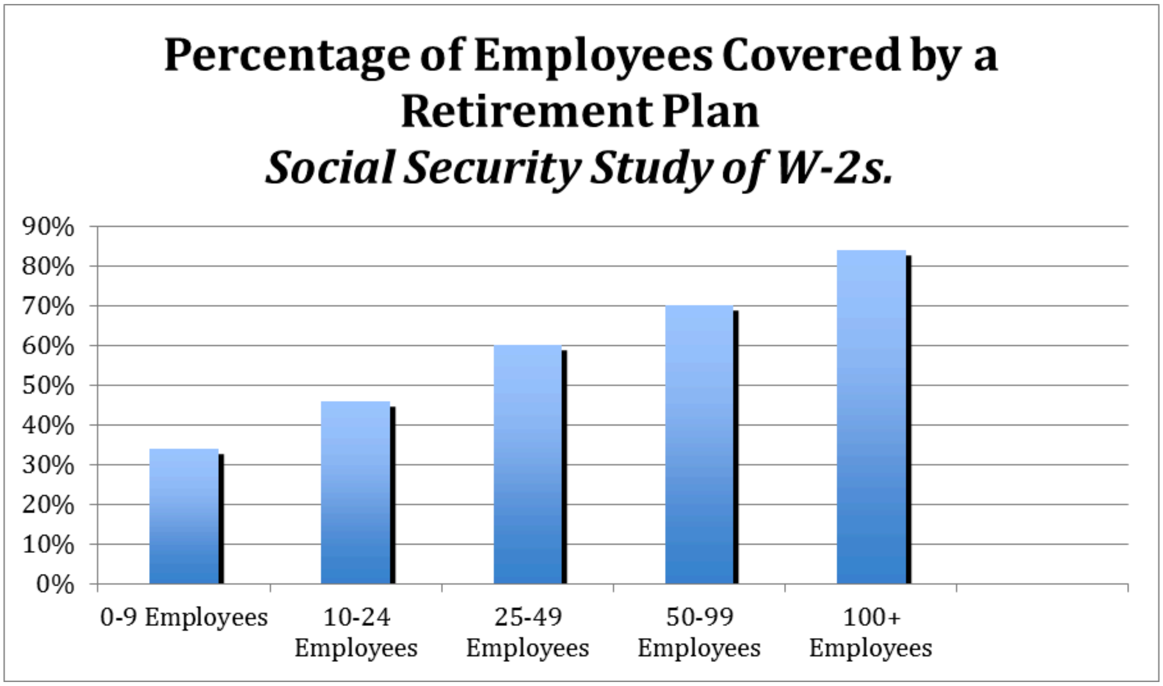
Low and moderate income workers are 15 to 2o times more likely to save in an employer provided plan than an IRA.

Focus on small business plans

- For firms with less than 100 employees, 50% are covered, and 34% participate. (*BLS NCS, March 2012*)

- A Social Security Administration study of actual W-2 records reveals a higher coverage rate than the BLS survey. Additionally, a number of small business plans provide an employer nonelective contribution which is made regardless of whether the participant made a 401(k) contribution and is not included in the W-2. It is very likely that the coverage numbers are even better than reflected in this study. (*Social Security Bulletin, Vol 71, Number 2 (2011))*

[13] *Ownership of Individual Retirement Accounts (IRAs) and Policy Options for Congress,* Congressional Research Service, November 5, 2010.
[14] *Employment-Based Retirement Plan Participation: Geographic Differences and Trends, 2009,* Employee Benefit Research Institute Issue Brief 348, October 2010.



SMALL PLANS FACE ADDITIONAL BURDENS

- Many lack in-house HR and benefits staff.

- They lack economy of scale, resulting in higher relative fees. This is especially acute for start-up plans.

- They are uniquely impacted by the top heavy rules that result in extraordinary costs for the business owner.

- A small business owner faces a personal cost-benefit analysis that does not apply to larger business.

THE BOTTOM LINE

- **The single criterion most likely to affect retirement security is whether or not a worker is offered a retirement plan at work.**

- **Small business owners face special challenges in offering retirement benefits. A crucial factor is how attractive the plan is to the owner.**

- **Reducing the attractiveness of a plan to the owner, by increasing complexity or costs, or by reducing the benefits available to the owner, threatens the retirement security of rank and file workers.**