Washington Update: A Challenging & Confusing Time for Investors, Plan Sponsors and Plan Participants

By Michael Townsend, July 20, 2020

As July began, the country remained roiled by a trio of culture-altering crises: the ongoing coronavirus pandemic, unprecedented economic upheaval and nationwide activism around social justice. Yet the markets in the second quarter showed astonishing positive momentum – the best quarterly performance since 1998 and the best quarter-to-quarter swing since 1932. It all adds up to a confusing and challenging time for investors, plan sponsors and plan participants.

In the nation's capital, Congress is back to full-time work, although under dramatically altered circumstances, including social distancing, a huge increase in remote and virtual committee proceedings, and, for the first time ever, the use of proxy voting in the House of Representatives. With an election looming in less than four months, lawmakers and regulators are scrambling to get work done before a possible change in the political balance in 2021. There are a number of key developments for plan sponsors and plan participants to be following.

Another coronavirus aid package coming from Congress?

Topping the list of policy items to watch is the next coronavirus aid and economic stimulus package from Congress. After lawmakers came together in March and April to produce four bipartisan aid packages totaling roughly $2.8 trillion, action slowed significantly in May and June. The House of Representatives narrowly approved the $3 trillion HEROES Act on May 15, but unlike its four predecessors, the bill was not the result of bipartisan negotiations. Instead, House Democrats drafted and passed with only 1 Republican vote, a kind of wish list that even House Speaker Nancy Pelosi (D-CA) acknowledged was a starting point for negotiations with the Republican-controlled Senate.

The HEROES Act includes about $900 billion for state and local governments, the top priority for Democrats. The bill also features another round of direct payments to low- and middle-income taxpayers; hazard pay for front-line workers; money for assistance with rent, mortgage payments and utilities; funds for hospitals, health care providers, coronavirus testing and contact tracing; $25 billion for the Postal Service; and forgiveness for up to $10,000 in student loans for certain borrowers, among dozens of other provisions.

But the bill was a non-starter in the Senate, where Republicans have not only refused to consider it but by the start of July had not put forward an alternative proposal. That is expected to change later in July. Both the House and the Senate were scheduled for a two-week recess from which lawmakers will return to Washington on July 20. That return is expected to trigger frantic negotiations between House Democrats, Senate Republicans and the White House over the contents of the next round of aid. A key driving factor is the July 31 expiration of the enhanced unemployment benefits approved by Congress in the CARES Act. Democrats want to ensure that the $600 extra payments on top of normal benefits continue, while Republicans, concerned that the money acts as a disincentive to return to work, are countering with a system of bonus payments for individuals who return to their jobs. That is shaping up to be the trickiest item to navigate in the negotiations.

All of the posturing aside, both sides have remained confident that another major bill will get done this summer. While Republican leaders have argued for a bill of about $1 trillion, President Trump said in mid-June that he would support a package of around $2 trillion, roughly splitting the difference between the Republican suggestion and the HEROES Act. While it's always possible that the talks could bog down, look for a deal to come together at the very end of the month or in the early days of August.

One element of the negotiations that plan sponsors and participants should keep an eye on is discussions for additional retirement savings incentives. The CARES Act waived required minimum distributions (RMDs) for 2020, as well as allowing for penalty-free hardship withdrawals from retirement accounts. The House-passed HEROES Act would retroactively waive RMDs for 2019, though it is not clear that proposal will survive negotiations with the Senate. But a bipartisan group of Senators is reportedly working on other retirement savings changes for possible inclusion in the next aid bill. Ideas in the mix include waiving RMDs for 2021, enhanced catch-up contributions and changes to multiple-employer plans. Stay tuned in late July to see whether any of these provisions make it into the final package.

Regulatory developments

The final months before an election are often busy, as regulatory agencies race to finalize proposals before a potential change in the administration. This year is shaping up as no exception, with several regulatory developments critical to the retirement savings world:

- **IRS issues further clarification on RMD provisions of CARES Act.** On June 23, the IRS issued additional guidance that clarified some confusing aspects of the waiving of RMDs for 2020. The guidance indicated that all RMDs taken in 2020 were eligible to be rolled back into an individual's account. Prior to the guidance, there had been some uncertainty about whether an RMD taken in January would be eligible for a rollover. In addition, the agency states that any RMDs taken in early 2020 are not subject to the 60-day rule; the deadline for rollovers was extended to August 31. The IRS also waived the "one rollover every 12 months" rule. This ensures that individuals who, for example, take their RMD in monthly installments could roll any or all of those distributions back into their account. Further details can be found here.

- **Department of Labor (DOL) unveils new fiduciary proposal.** The DOL on June 29 proposed a new rule to govern investment advice in retirement accounts that would allow financial advisors to provide fiduciary advice and still receive compensation in some situations. The long-awaited proposal is the department's attempt to revise its standards after the so-called "fiduciary rule" was vacated by the courts in 2018. The proposal would provide exemptions under the Employee Retirement Income Security Act (ERISA) to allow fiduciaries to receive compensation for advice as they act in the retirement savers' best interests. The proposal reinstates the five-part test under ERISA to determine who is a fiduciary. The rule aligns with the SEC's Regulation Best Interest, the new standard for broker-dealers and investment advisors who provide advice that went into effect on June 30. The DOL proposal will now be subject to a 30-day public comment period. It could be finalized by the end of the year.

- **New electronic delivery rules.** On May 21, the DOL finalized a much-anticipated rule making it easier for employers to deliver retirement plan information to participants electronically. The new rule allows for delivery of information to participants by e-mail and by posting certain information on a website, but also allows for participants to choose to receive information in paper form.

- **DOL issues guidance making it possible for 401(k) plans to invest in private equity funds.** Pension funds have long had the ability to invest in private equity, and the new guidance will "level the playing field for ordinary investors," according to Labor Secretary Eugene Scalia. The opening of defined contribution plans to private equity investment options is not without controversy, and it remains to be seen how many plans will make it an option.

Voting uncertainty may dominate the months ahead

Finally, as we move through the summer, the election will increasingly become front and center. Former Vice President Joe Biden has secured the Democratic nomination; his selection of a running mate is expected by August. Both parties will hold their conventions in late August (significantly modified due to the coronavirus), and then the campaign for the White House will move into high gear.

For investors, however, the part of the election that may be the most important is the battle for control of the Senate. Republicans hold a 53-47 advantage at the moment, but there are 23 Republican-held seats up for re-election this November, and just 12 Democratic-held seats. While a Democratic majority is far from a sure thing, momentum in recent weeks seems to be favoring Democrats. Republicans have very tough battles on their hands to hold seats in Arizona, Colorado, Maine, Montana and North Carolina, and seats in Georgia and Iowa are also looking very competitive. Republicans are favored to pick up a seat currently held by a Democrat in Alabama, but there are few other opportunities for Republicans on the Senate map. Democrats are heavily favored to retain their majority in the House of Representatives, so control of the Senate (along with the White House) will be critical to determining what the policy agenda will look like in 2021. We'll have a more in-depth preview in the next edition of this newsletter in the fall.

But the X-factor now is looking to be what impact dramatic changes in voting may have on the fall election. Due to the pandemic, many states are turning to voting by mail rather than in person. The rules for voting by mail vary widely from state to state, which is likely to be confusing to voters and could increase turnout in some areas while dampening turnout in others. And the process for authenticating and counting ballots will be much more challenging and slow. The very real possibility exists that we will not know who won the White House or which party controls the Senate on Election night, or for days afterwards. Expect an increasing focus in the months ahead on the implications of significant changes to voting procedures on the outcome this November.

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