After a five-week late summer break, Congress reconvened to achieve some surprising policy wins in September. It was a stark contrast from the first eight months of the year, which were virtually devoid of legislative accomplishments, including the collapse of health-care reform. In a single September bill, Congress put off a debt ceiling fight until early 2018, extended government funding through early December; and provided billions of emergency aid to the victims of Hurricanes Harvey and Irma.

Once the dust settled, Congress turned their attention to what the administration hopes can become the signature legislative triumph of President Trump’s first year in office: tax reform. Washington, however, has grown skeptical that any tax legislation can pass before the end of the year, given both delays in introducing legislation and the overall complexity of the task. It is likely this issue will drag on into 2018.

For those in the retirement industry, 2017 to date has been relatively quiet on the legislative front, though that will change, as the tax debate gets underway. On the regulatory agenda, the Department of Labor’s (DOL) fiduciary rule remains front and center some 18 months after it was “finalized.” Here is an update on those two issues and other developments of note in the retirement space.

**Tax reform could have implications for retirement savers**

This fall should see the formal launch of long-awaited tax reform efforts. On August 30, President Trump began his push with a speech in Springfield, Missouri, that was long on enthusiasm for a tax code overhaul, but short on specifics. The details are being left to the so-called “Big Six” – a group of negotiators from the White House, the Senate, and the House of Representatives. However, several months of discussions have not resulted in anything more than a statement of principles from this group consisting of Treasury Secretary Steven Mnuchin, National Economic Council Director Gary Cohn, Senate Majority Leader Mitch McConnell (R-KY), Senate Finance Committee Chairman Orrin Hatch (R-UT), House Speaker Paul Ryan (R-WI), and House Ways and Means Committee Chairman Kevin Brady (R-TX).

The proponents of tax reform have talked in terms of lowering tax rates on individuals and on corporations, while simplifying the system as a means of generating greater economic growth and creating jobs. One important question will be the plan’s ultimate impact on high-income and middle-class taxpayers. The key, however, is what trade-offs will need to be made in order to pay for the cost of broad tax cuts. Hundreds of tax deductions and credits in the code are likely to be reshaped in the process.

The retirement savings community is particularly interested in whether there could be changes to the current system. For example, one proposal reportedly under consideration is taxing some or all contributions to employer-sponsored plans when the contributions are made, not at the point of withdrawal. Some retirement savings experts fear this action could deter younger, newer workers from participating in their company plans. Members of this population are often reluctant to sacrifice some of their take-home pay to retirement savings vehicles decades before they will need it.
Some fear taxing those contributions could exacerbate the trend. Others call those worries exaggerated.

Some in Washington have expressed concerns about the impact the tax proposal could have on federal coffers. Taxing contributions initially would be highly lucrative for the Treasury and could be used to offset cuts elsewhere in the tax code. However, the proposal becomes a huge money-loser for the federal government’s coffers years down the road, as retirees would be withdrawing those contributions and growth earnings tax-free. Also, special budgeting procedures known as “budget reconciliation” rules are likely to be used to get tax reform through the Senate. If this is the case, the potential revenue losses to the Treasury could require other revenue increases or politically risky spending cuts to avoid violating the rules. Those rules prevent filibusters and mean that the Senate could pass the bill with a simple majority, rather than the 60-vote supermajority typically needed for most legislation. The rules also prohibit the bill from increasing the federal deficit in the long-term, and that is where the cost of tax reform will come into play.

As of the writing of this article, Washington is still awaiting the specifics of the Republican tax proposal, so there is nothing definitive to report. However, if the proposal raises revenue from retirement savings incentives, expect that some people will want to use a portion of the revenue to bolster retirement security. Ideas under discussion include higher contribution levels and an expanded Saver’s Credit. In any case, expect the retirement savings industry to be an active voice in the debate ahead, particularly if these kinds of monumental changes appear in the proposal.

On the regulatory front, the DOL’s fiduciary rule continues to dominate news headlines. On August 31, the DOL proposed an 18-month delay in the fiduciary rule’s final compliance deadline and signaled that potentially significant changes to the rule could be in the works. The rule, which redefines who is a fiduciary and curbs conflicts of interest in the retirement savings space, was finalized last year. The first part of the rule went into effect in June, but significant portions of the rule – including new disclosure requirements and the launch of the “best interest contract” governing interactions between advisors and investors – were scheduled to take effect on January 1, 2018. The delay would push that final compliance deadline out to July 1, 2019. A final decision on the delay is expected in October.

Meanwhile, the DOL is also conducting an economic analysis of the impact of the rule pursuant to an executive memorandum from President Trump earlier this year. The study should be completed by the end of the year. That analysis could trigger revisions or even a full-scale rewrite of the regulation. Already, the DOL has indicated that it may roll back certain provisions of the regulation, including the mandatory arbitration waiver, which allows customers to use class-action lawsuits for breaches of fiduciary duty. The Department has already stated that it will not enforce the provision while the review is ongoing. Some reports have indicated that the DOL may use the delay to alter or eliminate the best-interest contract itself.
Ongoing debate over the fiduciary rule has passed the seven-year mark – an example of how nothing in Washington is final. While Congressional Republicans remain energized in their desire to construct a legislative solution to the investment advice issue, sharp partisan divisions make this approach a long shot for the time being. To muddy the crystal ball even further, DOL Secretary Alexander Acosta and Securities and Exchange Commission (SEC) Chairman Jay Clayton have publicly vowed to increase their agencies’ level of coordination on the issue, possibly including a new SEC rulemaking effort on the fiduciary standard.

**Regarding defined benefit plans**

Confusion continues to reign with regard to the 2018 mortality tables. In the waning days of the Obama administration, the IRS proposed the release of new tables for plan years beginning on or after January 1, 2018. Those regulations created a new mortality table for minimum funding of defined benefit plans. This change will likely increase the liabilities for most plans. However, the Trump administration designated this rule as “economically significant,” which triggers additional review by the White House’s Office of Management and Budget. A decision was still pending at the time of this article, and it was uncertain whether there would be adequate time for plan sponsors to make the necessary calculations and communicate accurate information to plan participants, should Congress decide this year. A number of organizations have been pushing the Treasury Department to delay the new tables by 18 months so that they would not apply to the 2018 plan year. It is worth noting that since the Pension Protection Act was signed into law in 2006, the latest that the IRS has issued mortality tables for the upcoming plan year was on September 29, 2007, for plan years beginning on or after January 1, 2008.

On a related note, relief may be coming for closed defined benefit plans. The issue arises in “soft-frozen” plans, where employees hired since the freeze are not eligible to participate, but employees already in the plan at the time it was frozen continue to accrue benefits. At the time of the freeze, the plan passes non-discrimination testing, but as time goes by, some plans no longer pass those tests, since many younger, lower-paid, non-participating employees have been hired. The Treasury Department could offer further regulatory relief, but there is no timetable for when that might happen. The House and Senate also proposed legislation last year to allow plans that were compliant at the time of the freeze to remain compliant, as long as the plan had not been amended in a discriminatory fashion. The bill passed the House, but stalled in the Senate, amidst election-year politics in 2016. This year, there is hope that the bill will be approved this fall, though nothing is certain.
As Vice President for Legislative and Regulatory Affairs, Townsend is responsible for analyzing legislative and regulatory proposals to determine how they would affect individual and institutional investors, and develops and executes strategies to communicate their interests to lawmakers, the media, employers and their employees, as well as individual investors. He specializes in tax issues, retirement savings, charitable giving issues, market structure issues, and financial literacy. He also speaks regularly to employee and client groups about how the political and policy environment in Washington affects investors.

Schwab Retirement Plan Services, Inc. created this communication for retirement plan sponsors and retirement plan consultants, advisors and other retirement plan service providers and fiduciaries only. Schwab Retirement Plan Services, Inc. is not a fiduciary to retirement plans or participants and only provides recordkeeping and related services.

©2017 Schwab Retirement Plan Services, Inc. All rights reserved. (0917-7B81) ELC84191-09 (09/17)