

Washington Update

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What We Will Cover

- Tax Reform
- Regulatory Update
 - Fiduciary Rule
 - Small Business Administration
 - QNEC Guidance

Tax Reform

Tax Reform

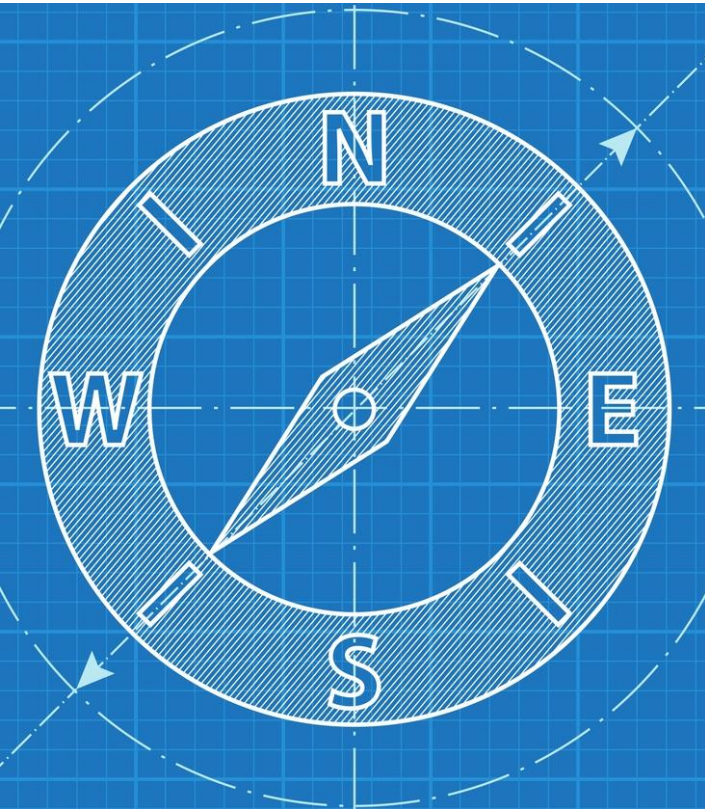
- Tax reform is a high priority for the new Congress and President Trump.
- Paul Ryan (R-WI), is once again Speaker of the House, and Kevin Brady (R-TX), is once again Chair of the House Ways and Means Committee. In the summer of 2016, they jointly unveiled their “blueprint” for tax reform which includes lower individual and capital gains tax rates.

Tax Reform

- On April 26th, the President formally announced the “principles” that will form the basis of his tax reform plan.
- At this point, no legislative language has been released for either the “blueprint” or the President’s plan.
- The initial draft of the tax reform bill expected from the House Ways and Means Committee will likely include provisions from both the “blueprint” and the President’s plan.



The “Blueprint” for Tax Reform



- Lower individual marginal tax rates with brackets of 12%, 25% and a maximum 33% rate;
- Lower capital gains, dividend and interest tax rates by providing a 50% deduction, effectively halving the marginal rates;
- Lower corporate tax rates of 20%;
- Elimination of the AMT and “death” tax; and
- A “Border Adjustment Tax” which many describe as an import tariff.

The Trump Plan for Tax Reform

- The President's tax reform plan includes the following:
 - Lower individual marginal tax rates with brackets of 10%, 25% and a maximum 35% rate;
 - Lower corporate tax rates of 15%;
 - Elimination of most personal deductions;
 - 100% increase in the standard deduction for joint filers; and
 - Elimination of the AMT and the "death tax".

Through “Way?”

- Both the “blueprint” and the President’s plan include a new tax rate for businesses that are organized as “pass-through entities” such as Sub-S corporations, partnerships, LLCs taxed as partnerships and sole proprietors.
- The “pass-through” tax rate would equal 25% under the “blueprint” and 15% under the President’s plan.
- The “pass-through” rate would only apply to the “business income” portion of the pass through entity’s income with the “compensation” portion being taxed at ordinary income rates.
- The **big question** is how to allocate the entity’s total income between these two categories.

“Pass” Tense?

- This means that the business income of these pass through entities will no longer be subject to the top individual tax rate (33% in the “blueprint” and 35% in the President’s plan).
- Additionally, once the 25% (blueprint) or 15% (Trump) “pass through” tax has been paid, the net amount remaining can be reinvested in assets that produce capital gains which are eligible for a maximum individual tax rate of 16.5% under the “blueprint” or 20% under the President’s plan.

Tax Reform

- By way of illustration, assume a 50-year old small business owner has \$50,000 that can either be contributed to a plan or paid out as “business income” and invested (after tax) for the next 16 years at a 4% return (taxed at capital gains rates).
- Applying the “blueprint’s” tax rates on pass through income to the above example (25% tax on pass through income and 16.5% capital gains tax on subsequent earnings) leaves a total accumulation of \$840,000 which is **\$46,000 more** than if contributed to a plan.
- Under the President’s plan, the small business owner would accumulate approximately **\$170,000 more** than if contributed to a plan.

Tax Reform

- The “blueprint” also includes “Universal Savings Accounts” as outlined in H.R 4094 (Rep. Dave Brat R-VA)) that was introduced, but not enacted, in the last Congress.
- Universal Savings Accounts:
 - \$5,500 limit (w/ COLA)
 - Anyone 18 or older is eligible
 - “Roth” type tax treatment (i.e. after-tax contribution, tax free distributions including earnings)

Budget Reconciliation Explained

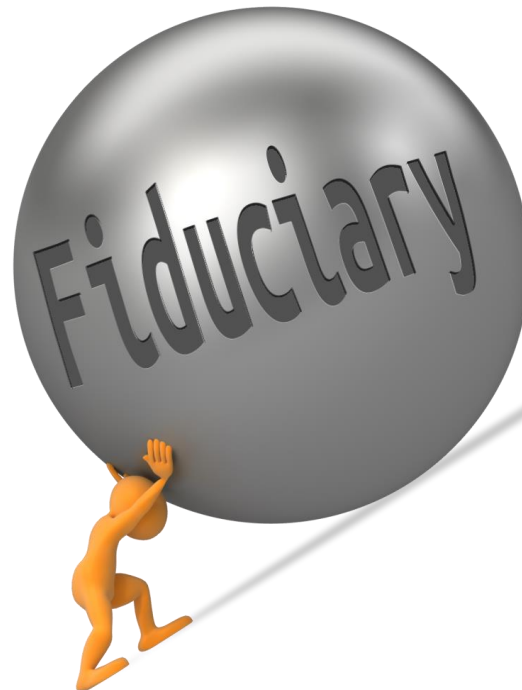
- Created by the 1974 Congressional Budget Act.
- Only process that avoids Senate filibuster.
- Has been used for major legislation such as COBRA, EGTRRA and welfare reform.
- “Byrd Rule” applies to provisions that do not “affect” revenue or lose revenue outside the 10-Year budget window.
- Revenue neutral budget bills avoid a 10 year “expiration date” such as we had with EGTRRA.

Tax Reform – Camp

- Double tax on contributions for top bracket earners.
- Roth-only above 50% 401k limit for large plans.
- 10 year freeze on cost of living increases:
 - 402(g) elective deferral;
 - 415 DB and DC; and
 - SIMPLE plans.
- Eliminate 403b and 457 Plans.
- Eliminate the “stretch” IRA.
- Would have raised \$250 billion in Revenue.

Regulatory Update

Fiduciary Regulation Update



Effective Date

- The Final Regulation became officially effective on June 7, 2016.
- With that said, however, the date on which the new rules actually were to be applied (the “Applicability Date”) was scheduled to be April 10, 2017.
- The BIC Exemption was likewise scheduled to become effective on April 10, 2017, with a “slimmed down” BIC exemption transition period from April 10, 2017, until January 1, 2018.

Effective Date

- On March 2, 2017, the DOL issued a proposed regulation to extend the Applicability Date by 60 days until June 9, 2017.
- The purpose of the delay is to provide time to examine the final regulation and related exemptions as directed by the President in a Memorandum dated February 3, 2017.
- ARA Comment letter recommended an extended delay until at least January 1, 2018, and a corresponding extension of BICE transitional relief until at least July 1, 2018.

Effective Date

- On April 7, 2017, the DOL issued a final regulation that extended the Applicability Date for 60 days until June 9, 2017.
- The BICE transitional period continues to expire on January 1, 2018. Significantly, however, the DOL modified the BICE to only require adherence to the “impartial conduct standards” during the transition period.
- On May 23, 2017, “Transition FAQs” releases by DOL confirmed the June 9 applicability date and related transitional relief.
- The DOL also indicated they will be soon be issuing an RFI to receive public input for new exemptions or regulatory changes.

TPA Issues/Questions

1. Adviser Relationships –

- TPA recommends adviser – is it for a fee?
- No “fee” but adviser regularly pays for business lunches or regularly refers clients to TPA?
- Affiliate of TPA provides fiduciary advice for a fee?

2. Platform Communications – (TPA does not pick investments from platform menu.) (FAQs Part II Q 18)

- TPA recommends platform provider and receives revenue sharing from provider for shareholder servicing?
- TPA provides a list of 3 platform providers that TPA works with without a recommendation (and receives revenue sharing)?
- TPA recommends platform but receives no revenue sharing (but what about lunch or referrals from PP)?

TPA Issues/Questions

3. Rollover/Distribution Issues –

- Employee of TPA firm answers call from a terminated participant who asks what distribution options are permitted under the terms of the plan; is it an eligible rollover distribution, and **where should the amount be rolled?** (FAQs Part II Q12 & 13)
- TPA recommends to plan sponsor a provider to receive “automatic rollovers” for terminated participants who are subject to mandatory cash-outs? What if the prototype plan has a blank to fill in the name of the “automatic rollover” provider? What if the “automatic rollover” provider’s name is “hardwired” into the prototype language? (FAQs Part II Q5)

SBA Comment Letter

SBA Comment Letter

- ARA works with many federal agencies in Washington, including the Small Business Administration (“SBA”).
- The SBA is charged with advocating for the interests of small businesses across the full spectrum of federal agencies (including the DOL and IRS).
- Under the Regulatory Flexibility Act, the promulgation of an economically significant regulation requires consideration of its potential impact on small businesses.
- Similarly, the Paperwork Reduction Act requires a federal agency to certify that it has considered and made efforts to reduce the burdens on small businesses when it seeks to collect information from the private sector.
- The SBA typically weighs in when these reviews are undertaken.

SBA Comment Letter

- It is anticipated that with the change in Administrations, the SBA will want to take a fresh look at its priorities with regard to advocating for small businesses.
- The ASPPA/ARA Government Affairs Committee recently provided to the SBA a memorandum recommending it weigh in on a number of existing and proposed regulatory initiatives that should be reconsidered for their potential detrimental impact on small businesses.

SBA Comment Letter

- The ASPPA/ARA recommendations included the following:
 - IRS should not require Form 5500 preparer information to be disclosed on the internet.
 - The DOL should permit self-correction under the Voluntary Fiduciary Correction Program.
 - The IRS Employee Plans Compliance Resolution System (EPCRS) should include expanded self-correction options for participant loan failures.
 - Electronic transmission of ERISA notices should be permitted as the default method.
 - The IRS, DOL and PBGC should substantially revise the proposal to “modernize” the Form 5500 and seek additional comment.

IRS Proposed Regulations on Funding QNECs and QMACs with Forfeitures

QNECS and Forfeitures

- In 2012, the IRS issued model language in the master and prototype LRMs stating that “forfeitures may not be used as ADP Test Safe Harbor Contributions.”
- ASPPA GAC submitted a comment letters on May 8, 2012 and July 8, 2013, to the IRS and Treasury Department on the use of forfeitures to fund safe harbor contributions.

QNECS and Forfeitures

- The concern is that the definitions of QNECs and QMACs in the Treasury Regulations might be read to require these contributions to be fully vested when first contributed to the plan rather than at the time of their reallocation from the forfeiture account .
- Although the regulation could be read that restrictively, there is no mandate for such a rule in the statute itself .

QNECS and Forfeitures

- To the contrary, such an interpretation is inconsistent with the purpose of the statutory provision, as well as the treatment of forfeitures within the context of other qualification requirements, and does not further any policy objective.
- The GAC comment letters argued the determination of whether an amount is nonforfeitable should be made at the time the forfeiture amount is reallocated to the accrued benefit of a participant.

QNECS and Forfeitures

- On January 18, 2017, the IRS published proposed regulations in the federal register.
- The proposal amends the regulation to follow the recommendations of ASPPA GAC. Specifically, that safe harbor amounts must be nonforfeitable when allocated to a participant's account (rather than at the time of contribution).
- The change is effective for plan years that begin on or after 90 days after publication as a final regulation. However, the proposal includes a “reliance” statement for periods preceding the effective date.

QUESTIONS???