

**STATEMENT OF**

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**ON BEHALF OF**

**THE SAVINGS COALITION OF AMERICA**

**BEFORE THE**

**SUBCOMMITTEE ON SELECT REVENUE MEASURES  
OF THE  
COMMITTEE ON WAYS AND MEANS  
UNITED STATES HOUSE OF REPRESENTATIVES**

**AT THE HEARING ON**

**“THE ROLE OF INDIVIDUAL RETIREMENT ACCOUNTS  
IN OUR RETIREMENT SYSTEM”**

**WASHINGTON, D.C.  
JUNE 26, 2008**

Statement of  
The Savings Coalition of America  
U.S. House Ways and Means Select Revenue Measures Subcommittee Hearing on the “Role of  
Individual Retirement Accounts (IRAs) in Our Retirement System”  
June 26, 2008

Good morning. My name is Randy Hardock. I am the managing partner of the Washington, D.C. law firm of Davis & Harman LLP. I have been involved in retirement savings issues in Washington for over 25 years, including service as Tax Counsel with the Senate Committee on Finance from 1986-1993 and as Benefits Tax Counsel at the Department of the Treasury from 1993-1995.

I am here today on behalf of The Savings Coalition of America, a nonprofit organization that promotes public awareness of the importance of personal saving and supports incentives to increase personal saving by Americans. The members of the Savings Coalition represent a wide variety of private interests including engineering, consumer groups, home-building, realtors, tangible assets, trust companies, the health care industry, banking, financial services, education, insurance, securities and business groups. The Savings Coalition would like to thank the members of the Subcommittee for focusing on the role that the various types of individual retirement arrangements (“IRAs”) play in our retirement system, and for giving us the opportunity to comment today. A list of the members of the Savings Coalition is attached.

IRAs are a uniquely successful retirement savings vehicle that have become an essential pillar in America’s retirement savings strategy. IRAs ensure the portability of retirement savings when individuals change jobs, and they provide critical savings opportunities and incentives for individuals who do not have access to employment-based plans or who wish to supplement savings outside of the employment relationship. From the time when IRAs were first created in 1974, and at each step of their evolution since then, the House Committee on Ways and Means has led the way. We commend the members of this Subcommittee for continuing efforts to further improve the effectiveness of the IRAs in assisting even more Americans prepare for a financially secure retirement.

A report released earlier this month by the Government Accountability Office (“GAO”) expressed concern that many employees of small employers who lack access to employer-sponsored retirement savings plans are not adequately saving for their retirement. We agree. GAO suggested certain actions to encourage more small employers to offer IRAs to their employees through the workplace. Our testimony touches primarily on policy changes related to the GAO report, with a focus on ideas to improve retirement savings through the use of SIMPLE IRAs, SEP IRAs, and other payroll-deduction IRAs offered by employers.

As a general matter, we would emphasize at the outset that policy changes will only be successful in encouraging more employers to provide retirement savings opportunities in the workplace if those employers are provided with simple, low-cost, low-risk alternatives. In addition, some type of incentive for small business owners and decision-makers to create an IRA option for their employees will also be important.

**I. IRAs are one of the most successful mechanisms for building retirement security.**

Congress created the traditional deductible IRA in 1974. Since then new types of IRAs have evolved and the eligibility and contribution rules have been altered several times. In 1978, Congress established the Simplified Employee Pension (SEP) IRA – an employer-based IRA. Between 1982 and 1986, Congress made the traditional IRA “universal” by allowing all workers under age 70½ to make tax-deductible IRA contributions. Beginning in 1987, Congress eliminated the universality of tax-deductible IRA contributions, but permitted workers meeting certain income limits to make such contributions even if they were covered by employer-sponsored retirement plans. In addition, after-tax, or nondeductible, contributions were permitted. In 1996, Congress added the Savings Incentive Match Plan for Employees (the SIMPLE IRA), an account targeted to small businesses and also increased the permitted contribution to spousal IRAs. Congress further expanded the menu of offerings again in 1997 with the Roth IRA and raised the income limits for IRA contribution deductibility. In 2001, Congress raised contribution limits for IRAs and those provisions permanent in the 2006 Pension Protection Act.

Today, the IRA successfully fulfills two primary functions. One is to give individuals not covered by retirement plans at work an opportunity to save for retirement on their own in tax-deferred accounts. The other is to provide portability for retirement assets by giving retiring workers or individuals changing jobs a means to preserve employment-based retirement plan savings by allowing them to transfer, or roll over, plan balances into IRAs. The IRA has been tremendously successful in serving both of these intended purposes. As noted by the GAO report, the estimated \$3.5 trillion held in IRAs in 2004 exceeded the estimated assets held in employer-sponsored defined contribution plans (\$2.6 trillion) and in defined benefit plans (\$1.9 trillion).

Figure 1  
SIMPLE IRA Plans  
Thousands of plans, reported by a sample of mutual fund companies

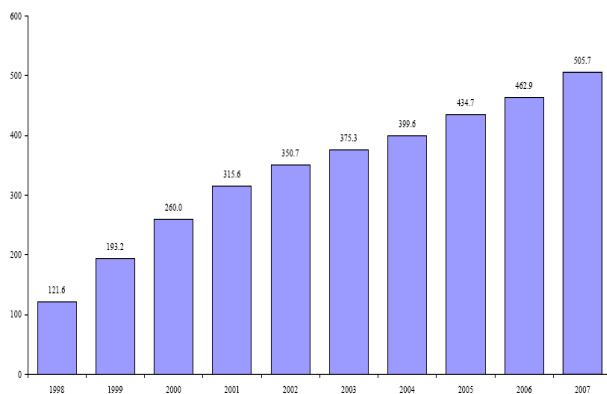
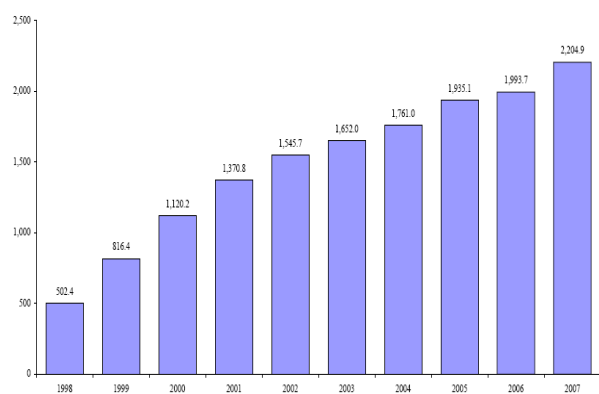


Figure 2  
SIMPLE IRA Participants  
Thousands of participants, reported by a sample of mutual fund companies



Efforts continue to further expand the utilization of the IRA by merging access to IRA accounts with the advantages of savings in an employment-based setting, including especially greater utilization of payroll-deduction mechanisms that have proven effective. SIMPLE IRA utilization, in particular, has grown steadily over the years. As reflected in Figures 1 and 2, below, a sample survey by the Investment Company Institute that was released earlier this week

indicates that at year-end 2007, at least 2,204,900 individuals participated in over 505,700 SIMPLE IRA plans, and that the number of such plans and the number of participants has increased each year since 1998.<sup>1</sup>

Data on payroll-deduction IRAs is not readily available, as indicated by the GAO. Still, financial institutions that are members of the Savings Coalition report anecdotally that relatively few small employers have adopted payroll-deduction IRAs for the reasons outlined below.

## **II. *Barriers still exist that discourage small employers from offering employer-sponsored IRAs and payroll-deduction IRAs to employees.***

IRAs already offer one of the easiest options for small employers to provide savings vehicles to their employees. SIMPLE IRAs and SEPs offer somewhat streamlined rules which make it easier for employers to offer those plans relative to the costs and burdens associated with 401(k) and similar employer-sponsored plans. Offering payroll-deduction IRAs can be an even lower-cost option for small employers, because they do not involve employer contributions, they impose only minor financial reporting requirements on employers, and they allow employers to select a single IRA provider (or let employees select their own provider). Currently, payroll-deduction IRAs also have fewer requirements for employee communications than SEP or SIMPLE IRAs, and they do not subject employers to certain fiduciary responsibilities and requirements that apply to employer-sponsored pensions under Title I of the Employee Retirement Income Security Act of 1974 (“ERISA”).

Although the growth of SIMPLE IRAs has been impressive, there remains a huge gap in employers providing any type of employment-based retirement savings option. The reasons are many, but based on the experience of our members most small employers will offer IRAs to employees only if they understand that they can do so simply, at a low cost, and at low risk. These employers are likely to proceed only if they are comfortable that they are not at risk of engendering lawsuits, having to deal with onerous government reporting or regulation, or exposing themselves to the potential for generating a new source of employee complaints.

There are a number of barriers that currently discourage small employers from offering employer-sponsored IRAs or payroll-deduction IRAs. The most important include:

- Administrative cost to small businesses;
- Concerns over potential liability;
- Inadequate incentives for decision-makers; and
- Limited employer and employee understanding of employer-sponsored IRAs and payroll-deduction IRAs.

The combination of these barriers discourage many employers from providing access to IRAs for their employees, thus limiting the effectiveness of IRAs in further facilitating retirement savings.

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<sup>1</sup> See *Investment Company Institute, Survey of a Segment of Member Mutual Fund Companies* (based on a survey of firms representing 75 percent of all SIMPLE mutual fund assets at year-end 2007).

*Cost Barriers* – The administrative cost associated with setting up and managing payroll-deduction IRAs may be a particularly high hurdle for many small employers without electronic payroll systems or who do not outsource payroll functions. Without electronic payroll systems or a reliable outside provider, small employers are subjected to higher management costs if they offer payroll-deduction IRAs. Costs are also influenced by the number of employees participating and the number of IRA providers to which an employer must remit contributions on behalf of employees.

*Liability Concerns* – Another barrier to widespread establishment of payroll-deduction IRAs is the concern of employers otherwise not subject to ERISA that they will become subject to ERISA fiduciary requirements by virtue of offering payroll-deduction IRAs. The Department of Labor (“DOL”) has already issued helpful guidance on this issue in the form of Interpretive Bulletin 99-1 (29 C.F.R. § 2509.99-1). DOL clarifies that employers can select a single IRA provider for employees and provides their interpretation on when employers are not subject to ERISA fiduciary responsibility. Still, many small employers do not understand the scope or meaning of DOL’s Interpretative Bulletin. Some believe that codification and clarification of the DOL’s existing guidance could reassure more employers that they may offer payroll-deduction IRAs without becoming subject to ERISA.

*Absence of Incentives* – Another roadblock to the adoption of payroll-deduction IRAs by small employers is that there are no added tax incentives for the employer that provides the option. This absence is particularly important in the case of small business decision-makers. In practice, a small business owner (or a senior manager of a small business) has no personal incentive to establish payroll-deduction IRAs for employees, since that decision-maker can obtain the identical IRA independently on an individual basis. Moreover, for many small business decision-makers, the IRA may offer little tax advantage in any event, since complex eligibility requirements make planning difficult.

Similarly, there are no employer tax advantages for offering a payroll-deduction IRA. With the limits on contributions to payroll-deduction IRAs much lower than those applicable to SEP and SIMPLE IRAs, some small employers likely conclude that payroll-deduction IRAs are not worth the effort and resources required to establish them. This is particularly true for employers with a workforce that is not requesting retirement savings options, especially employers with relatively low-wage workforces.

*Lack of Employer Education* – Finally, many small employers do not know about the advantages of payroll-deduction IRAs or even that they exist. DOL has issued educational materials regarding payroll-deduction IRAs, but in spite of DOL’s efforts, many employers are still unaware that payroll-deduction IRAs are available or that employer contributions are not required. More needs to be done to make offering IRAs an attractive, low-cost option for employers and to educate employers about how payroll-deduction and other IRAs work.

**III. *Adding new burdens or concerns could be counterproductive, discouraging small employers from offering IRA savings options for their employees.***

The GAO report recommends that Congress consider requiring certain actions by DOL to increase the direct oversight of payroll-deduction IRAs. While we feel that additional data on payroll-deduction IRAs would be helpful in analyzing the role of these IRAs in our retirement system, we strongly discourage any increased oversight or regulation that would impose new burdens on small employers or otherwise discourage them from making IRAs available to their employees.

For example, imposing reporting requirements on employers maintaining payroll-deduction IRAs would increase costs for all the employers offering those arrangements when the same data could be obtained through sampling methods that are less intrusive. Similarly, extending DOL's jurisdictional reach to payroll-deduction IRAs could subject those plans to ERISA regulation and would drive employers away from offering those types of arrangements. We note that Congress has long recognized that small employers historically have failed to provide retirement arrangements for their employees because of the administrative costs and burdens associated with establishing and maintaining such arrangements.<sup>2</sup>

We do believe that the Internal Revenue Service should be encouraged to share available information on these and other IRAs with DOL without requiring any additional information from employers, as GAO recommended. The Internal Revenue Service already collects considerable data on IRAs and that should be made available to DOL.

**IV. *Policy changes that would remove barriers and increase incentives for small employers to offer IRA savings access to their employees.***

There are several legislative changes that would make it easier and more attractive for employees without access to employer-sponsored retirement plans to contribute to IRAs offered by small employers. As noted above, it is important that legislation lessen the existing barriers that discourage small employers from offering employer-sponsored IRAs and payroll-deduction IRAs to employees. This can be accomplished by simplifying these arrangements and helping small employers make them available at a lower cost and with less risk of employee complaints, lawsuits and additional government regulation.

*Codification of DOL Interpretive Bulletin 99-1* – Incorporating DOL's Interpretive Bulletin 99-1 into statute or by some type of legislative reference could cause more employers to consider offering IRA savings access to their employees. That Interpretive Bulletin provides small employers with important safe harbor relief from ERISA Title I for payroll-deduction IRA programs that satisfy certain conditions. However, many small employers do not have an understanding of what an Interpretive Bulletin is and how much reliance can be placed on DOL's interpretation.

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<sup>2</sup> See, e.g., STAFF OF JT. COMM. ON TAXATION, 100TH CONG., GENERAL EXPLANATION OF THE TAX REFORM ACT OF 1986 664 (Comm. Print 1987).

At the same time, this safe harbor relief should be further clarified to give small employers (and financial institutions) greater comfort and flexibility to promote such programs without fear of being subject to the requirements of ERISA Title I that apply to employer-sponsored pensions. Similarly, employers should be given comfort that implementing a payroll-deduction mechanism that automatically defaults workers into contributing to an IRA will not subject the employer and the arrangement to ERISA Title I requirements. Our experience with 401(k) and similar retirement plans confirms that default enrollment can increase retirement plan participation significantly. We commend you, Chairman Neal and Mr. English for your efforts to promote default enrollment through IRAs and we look forward to working with you on those proposals. .

*Making SIMPLE IRAs Simpler* – One recent improvement with respect to IRAs that was originated in part by this Committee was the creation in 1996 of the Savings Incentive Match Plan for Employees, or SIMPLE IRA. SIMPLE IRAs are arrangements that merge the flexibility and attractiveness of the IRA with a more limited employer role that has proven attractive to small businesses. Finding ways to further streamline and improve employee access and participation in retirement plans through the workplace, including SIMPLE IRAs and other payroll-deduction arrangements, should be one of the next areas that Congress considers as we continue to better assist Americans in preparing for a more secure retirement.

Still, SIMPLE IRA rules should be made simpler. Changes that would make SIMPLE IRAs less complicated and more attractive include eliminating the current law rule prohibiting a small employer from making a mid-year move from a SIMPLE IRA plan to another retirement plan, eliminating the current law restrictions on rollovers from SIMPLE IRAs to traditional IRAs and qualified plans, and lowering the penalty tax on premature distributions from a SIMPLE IRA to that which applies under all other qualified retirement savings vehicles. These changes are included in H.R. 5160, The Small Businesses Add Value for Employees Act of 2008, which was introduced by Representative Kind, along with Representatives Hulshof and English, on January 29, 2008.

*Creating Incentives for Decision-Makers* – Small employers need more incentive to make IRAs available to their employees. They need incentives to educate their employees on the benefits of using IRAs to save for retirement and encourage employees to contribute to IRAs.

A reasonable start-up tax credit for small employers, like that which is available on a larger scale for other employers, would help encourage small employers to establish and offer IRAs to employees. In this regard, H.R. 5160 would provide a start-up credit equal to 50 percent of the start-up costs for new plans and would allow for a one-time \$25 tax credit for each employee who enrolls in the savings program.

In addition, H.R. 5160 proposes two new features that are designed to encourage more small employers to sponsor a SIMPLE. One feature is an increase in the SIMPLE IRA contribution limit to be on par with the limit for other defined contribution plans such as the 401(k). In addition, employers who sponsor a SIMPLE would also be able to make additional contributions to their employees “across the board.” Currently, employers are limited to either a

2 percent non-elective contribution or a 3 percent matching contribution. This added feature would provide more flexibility without increasing complexity.

Still, many small employers will remain unwilling to adopt payroll-deduction IRAs because the current income eligibility limits and phase outs often make the IRA an uncertain option for small business decision-makers. Today, eligibility for traditional deductible IRAs, Roth IRAs and spousal IRAs can be determined only after the taxpayer works through a complex maze of eligibility requirements that include a variety of income limitations and phase-outs. Which of the various eligibility limits applies depends, in part, on the type of IRA the individual wishes to establish and whether the individual (or the individual's spouse) actively participates in certain types of employment-based retirement plans.

Even with recent improvements, the fact remains that many middle-income Americans are still not eligible for a fully deductible IRA. Although the Roth IRA was wisely made available to a broader segment of the population, the application of income limits on Roth IRAs remains detrimental. The current income limits also impose a severe marriage penalty on certain couples. To make matters worse, many small business owners do not know their income until the end of the year, making IRA eligibility uncertain in advance and from year to year.

In sum, the current IRA eligibility limitations (which were initially included in the Tax Reform Act of 1986) do far more harm than good. Those limitations substantially impair the potential effectiveness of IRAs as a savings promoter and should be repealed. They also act as a substantial deterrent to the establishment of payroll-deduction IRAs.

Our experience has shown that the people who are harmed most by the income limits are not the wealthy. To the truly wealthy, the relatively small IRA tax advantage does little to effect their overall tax burden. The people who are harmed by the income limits are those who are stuck in the middle. These are people who do not necessarily have sophisticated tax planners and accountants giving them advice. They will only proceed in committing their money into an IRA if they are confident that they will not get tripped up by the rules. Some of these people will delay contributions to make sure they will qualify, and then later forget to make the contribution or spend the money before they get around to making a contribution. Others may qualify for a full or partial IRA this year, but still will not contribute because the contribution permitted this year is too small, or because they assume they won't qualify in the future and they don't want to start contributing if they are not sure they will be able to continue the process in future years. Still others are confused and believe they may have to withdraw the funds if their income goes up in the future.

The end result of today's complicated limits on IRA eligibility is that contributions are not made by many of those who are technically eligible (or partially eligible) under the rules in a given year. This same chilling effect has been in effect since Congress originally imposed income limits on deductible IRA eligibility in the 1986 Tax Reform Act. Before that the IRA was available to all Americans with earned income. The year after the income limits on IRAs went into effect, contributions by those who remained eligible dropped by 40%.

Restoring universal IRA eligibility -- the rule that was in effect before 1986 -- would help all Americans to save more. By eliminating the complexity in the current rules, Americans will be presented with a consistent and understandable pro-savings message -- a clear consensus path to follow toward retirement security. That message will be reinforced by the general media, financial press, financial planners, and word-of-mouth. As families gain confidence in the retirement savings vehicles available to them, more and more will commit to the consensus path. Without the complex income limits, we would see increased savings among all income classes. We would also see more small business decision-makers who would be willing to offer IRAs through the workplace.

*Educating Small Employers* -- It is not enough to remove the barriers that small employers face to offering IRAs to their employees. It is crucial that awareness by small employers and their employees of the availability and benefits of SIMPLE IRAs, SEP IRAs, and payroll-deduction IRAs be increased. In this regard, the Internal Revenue Service and the Small Business Administration can provide invaluable information and education to small employers and employees on these retirement savings options. At the same time, they should be providing additional information on the availability and advantages of the savers credit for their workers. We urge that they be directed to do so as part of their normal small business compliance outreach efforts.

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In conclusion, IRAs are uniquely positioned to address the concerns raised in the GAO report that many employees of small employers who lack access to employer-sponsored retirement savings plans are not adequately saving for their retirement. We believe that these employees can improve their retirement savings in employer-provided IRAs and payroll-deduction IRAs through policy changes like those discussed above that provide a simple, low-cost, low-risk option for employers.

Enhanced retirement savings incentives are the most effective investments we can make as a nation. Those investments will pay back many times over in increased retirement security for Americans, a stronger economy, and a reduced dependence on government resources by Americans during their retirement. For these reasons we urge the members of this Committee to continue your efforts to expand access to IRAs through the workplace and to strengthen IRAs overall.

Once again, the Savings Coalition commends this Subcommittee on the leadership it historically has shown on retirement issues. On behalf of the Coalition, I would like to thank the members of this Subcommittee for your time and consideration of this important issue.

***SAVINGS COALITION OF AMERICA  
MEMBER ORGANIZATIONS***

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