

Reproduced with permission from Pension & Benefits Daily, 243 PBD, 12/20/2011. Copyright © 2011 by The Bureau of National Affairs, Inc. (800-372-1033) <http://www.bna.com>

Outlook 2012

Tax Reform Will Shape Pension Agenda; Significant Regulations Expected in 2012

Congress will pass no major retirement plan legislation in 2012, but the tax treatment of employment-based retirement benefits almost certainly will be part of any tax code overhaul in 2013—for which ideas and positions will become cemented in 2012—according to practitioners interviewed by BNA.

Practitioners who represent employer interests will continue, or step up, their efforts to defend existing tax deductions and tax deferrals for contributions to workplace retirement plans, motivated in some cases by a sense of urgency (206 PBD, 10/25/11; 38 BPR 2004, 11/1/11).

“We want to get in there before the ideas turn into cement,” ERISA Industry Committee President Mark J. Ugoretz told BNA Dec. 2.

Meanwhile, efforts to expand retirement coverage will be on hold in 2012 as employee benefit practitioners focus their efforts on preserving existing retirement benefits. “At the moment, we’re trying to hold onto where we are,” Ugoretz said.

One of the primary incentives for retirement saving, especially among middle-income earners, is its tax-favored status, Ugoretz said. “To the extent that you curtail that, people will not save,” he said.

Electronic disclosure and legislative relief from defined benefit plan funding rules enacted in 2006 with the Pension Protection Act (Pub. L. No. 109-280) also rank high on a list of concerns that employer groups said they will bring to Capitol Hill in 2012. In addition, major projects on the regulatory agendas at the departments of Labor and Treasury have prompted discussions about retirement security that will spill into 2012.

Spillover From 2011. The pension and retirement landscape in 2012 may look very similar to 2011, with a lot of issues spilling over into the new year, practitioners from across the industry said.

Edward Ferrigno, vice president of Washington affairs at the Plan Sponsor Council of America, formerly known as the Profit Sharing/401k Council of America, said in a Nov. 29 interview that he expects the next year will look a lot like the present one.

Ferrigno said he also expects the Department of Labor’s agenda to flow over into 2012 and beyond, especially its intended re-proposal of a regulation to expand the definition of a fiduciary. “I expect I’ll be doing pretty much exactly what I’ve been doing this year:

dealing with tax reform and dealing with DOL issues,” he said.

Tax Reform. If tax reform is taken up in 2012, the tax-favored treatment of employer-provided health insurance and retirement benefits could be reduced or eliminated to make room for reductions in overall individual and corporate tax rates, James A. Klein, president of the American Benefits Council, told BNA Dec. 6.

Tax breaks for retirement plans, including tax code Section 401(k) plans, are of particular interest to the Senate Finance Committee because they represent large tax expenditures, Karen Friedman, executive vice president and policy director at the Pension Rights Center in Washington, D.C., and Karen Ferguson, the center’s director, told BNA Nov. 30.

“The idea of some in Congress—and it was echoed by the fiscal commission—is to take some of those subsidies and redirect them to pay down the budget deficit,” Friedman said.

The Pension Rights Center is in favor of examining the idea of rolling back the amount of money people can contribute to their Section 401(k) plans, Friedman said. “If you look at the statistics, only a very teeny percentage of people actually contribute the maximum, and those people that are contributing tend to be higher income [earners] and the people that would be saving anyway,” she said.

The Pension Rights Center has proposed reducing Section 401(k) tax subsidies and using the revenue gained to create “a fairer retirement system,” Friedman said.

Pension Funding Relief. In the view of employers that sponsor large defined benefit plans, Ugoretz said, PPA created a funding regimen that relies on highly volatile contributions and has become a disincentive to keeping plans open to new participants. “It means that employers, in the short term, have to pile more and more money into their pension funds than is necessary to meet long term obligations,” he said.

Proposals are being circulated on Capitol Hill to change the PPA rules in ways that would ease the funding requirements on private-employer plans, Brian H. Graff, executive director and chief executive officer of the American Society of Pension Professionals and Actuaries, told BNA Nov. 23.

Graff said, however, that any congressional efforts to change the rules appear unlikely to occur before the November 2012 election.

The funding rules need to be stabilized through a longer-term interest rate that would be used to calculate pension liabilities, Kent A. Mason, a partner at Davis & Harman in Washington, D.C., told BNA Nov. 29.

“Instead of having interest rates rise and fall with every economic cycle, we need a long-term average of interest rates, like a 20- or 25-year average of interest rates, to sort of stabilize so that we don’t have ups and downs,” Mason said. Employers need a predictable base for determining their contributions to defined benefit plans, Mason said.

Electronic Disclosure. With respect to DOL’s electronic disclosure rules, widespread consensus exists in the retirement plan industry for updating the rules so that employers can use the most efficient electronic information technologies to communicate with employee benefit plan participants, Graff said.

The retirement industry has given up trying to bring DOL around to its position on electronic disclosure, Graff told BNA. “It’s going to require legislation. We’re convinced the department has gone about as far as it is going to go,” he said.

Some members of Congress will introduce bills in 2012, and there will be some debate on the topic, Graff said. Industry players, meanwhile, are “pretty much all in agreement as to what needs to get done,” he said.

Expanded Fiduciary Definition. Even if no major pension legislation is passed in 2012, benefit practitioners said they anticipate major regulatory action by DOL in 2012 on a proposed expansion of the definition of a fiduciary investment adviser under the Employee Retirement Income Security Act and further action by the Treasury Department on proposed hybrid plan regulations.

DOL’s Employee Benefits Security Administration withdrew its fiduciary proposal in September, saying that it would re-propose the regulation in early 2012 (182 PBD, 9/20/11; 38 BPR 1693, 9/20/11).

“I don’t know specifically what they are going to propose, but if they are going to greatly inhibit the ability of advisers to work with participants on rollovers, that’s going to be a huge fight, and there are enough signals to suggest that that is going to be a big issue,” Graff said.

Ugoretz said he expects the Obama administration to push hard to get the fiduciary regulation finalized before Election Day in November 2012.

Klein said he hoped that the pension community will be more comfortable with the re-proposal. He said he thinks the department has heard the concerns about the original proposal and that the new proposal will reflect that.

Mason, however, said he is not so sure that DOL will fully address concerns about the fiduciary rule’s treatment of individual retirement accounts.

Under the proposal that was withdrawn, Mason said, about 7 million IRA account owners could have lost access to investment professionals. “I hope that would be changed, but based on the statements I’ve heard, I’m concerned that it might not be,” he said.

ESOP Appraisers. DOL’s original fiduciary proposal would have treated appraisers as ERISA fiduciaries when they provided valuations of privately held stock in employee stock ownership plans. Practitioners who are opposed to appraisers being held to the standards of ERISA fiduciaries said they will continue their opposition in 2012.

“We have made it our No. 1 government advocacy project to oppose what the DOL is doing, and until they

come forward with something that does not make the appraisers fiduciaries, we will continue to be strongly opposed,” J. Michael Keeling, president and chief staff officer of the ESOP Association, told BNA Nov. 28.

Keeling said, however, that he is not optimistic DOL will change its position on ESOP valuations. “Based on what I read and my personal experience with leadership at the Department of Labor, my personal view is that the re-proposal won’t be that much different,” he said.

Hybrid Plan Regulations. Hybrid plan regulations released by Treasury and the Internal Revenue Service have generated controversy that will spill into 2012, as some practitioners push back against proposed rules that they said will discourage rather than encourage the formation of cash balance plans and other hybrid plan arrangements.

The proposed regulations ignore much of what Congress tried to do in PPA to promote cash balance and other hybrid plans, Ugoretz said. “We’ve been meeting lately with some of the Hill people to talk about that,” he said.

“I think we will be spending a fair amount of time talking about hybrid [rules] in 2012,” he added.

PBGC Proposals. The Pension Benefit Guaranty Corporation will continue to be in the spotlight in 2012 because of its record \$26 billion deficit and a proposal included in President Obama’s fiscal year 2012 budget to give the agency the authority to set its own premiums using a risk-based formula (31 PBD, 2/15/11; 38 BPR 354, 2/22/11), practitioners told BNA.

Mistrust of PBGC also appears to be growing among some employer groups, which have become increasingly public in their criticism of the agency’s proposals to increase flat-rate pension insurance premiums and to base variable-rate insurance premiums on employers’ creditworthiness.

“The PPA was, by and large, driven by a need to protect the PBGC,” Ugoretz said. It is clear now that the need “was overstated and unnecessary,” he told BNA.

“They have \$68 billion that will last them, even under their most conservative estimates, for the next 10 years—that’s their number, not mine,” Ugoretz said.

PBGC “cried wolf” in 2006, and the resulting funding rules under PPA have encouraged employers to freeze existing defined benefit plans rather than expand the number of defined benefit plans, Ugoretz said. PBGC’s latest premium proposals are another instance of crying wolf, he said, and are likely to result in a further retreat from providing pensions.

Meanwhile, PBGC premiums could increase in 2012, without congressional hearings, as Congress looks for new sources of revenue, Ugoretz said. “I’m very concerned that this could slip through,” he added.

Klein said there is a chance that, if PBGC does not get the authority to set premiums as it has proposed, Congress may indeed choose to increase premiums to raise revenue.

PBGC premiums are on Congress’s list of revenue raisers, but it is unclear how the premium issue will play out, Mason said.

Governmental Plans. Some miscellaneous legislation, including a bill related to governmental plans, might receive some attention in 2012 and be included in a package of other legislation, Louis T. Mazawey, a principal

at Groom Law Group in Washington, D.C., told BNA Nov. 29.

H.R. 2934, sponsored by Rep. Loretta Sanchez (D-Calif.), would change the tax code to permit current governmental plan participants to choose a lower defined benefit accrual in exchange for also being able to participate in a defined contribution plan, Mazawey said. "It's gotten a fair amount of bipartisan interest," he said.

Executive Compensation. An attorney whose practice includes executive compensation said he expects to see additional guidance in 2012 on income inclusion under tax code Section 409A and, based on that and guidance already issued, more enforcement activity.

"Everyone's been expecting that process to ramp up," Kurt L.P. Lawson, a partner at Hogan Lovells in Washington, D.C., told BNA Dec. 2. "I wouldn't be at all surprised if we start seeing more [audit] activity along those lines" in 2012, he said.

Tax issues will recede in 2012 as practitioners turn their attention to Section 953 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. No. 111-203), which requires companies to disclose the ratio of chief executive officer pay to employee pay.

The Securities and Exchange Commission is slated to propose rules under Section 953 by the end of 2011 and to adopt final rules by June 2012 (70 PBD, 4/12/11; 38 BPR 776, 4/19/11). Agency officials have expressed concern over whether the commission can deliver a "work-

able" rule by the December deadline (219 PBD, 11/14/11; 38 BPR 2089, 11/15/11).

Comments filed with SEC have suggested that there is little evidence that pay ratio disclosure would advance Dodd-Frank's goal of strengthening the relationship between pay and performance, while compensation analysts have said that the CEO-to-employee pay ratio defined in Dodd-Frank Act is difficult to calculate and interpret (146 PBD, 7/29/11; 38 BPR 1413, 8/2/11).

Unions support the new disclosure provision and have urged investors to write SEC and repudiate claims that the pay ratio calculation would be burdensome to calculate (239 PBD, 12/14/11).

Barring a repeal of Section 953 (121 PBD, 6/23/11; 38 BPR 1201, 6/28/11), the fight will continue into 2012, practitioners told BNA.

Executive compensation plans have received some congressional scrutiny, and that may continue into 2012, David Certner, AARP's legislative counsel and legislative policy director, told BNA Dec. 4. "It might be an issue later on if we get into a bigger tax reform debate," he said.

However, the primary policy focus of Congress and the Obama administration in 2012 is going to be on jobs, the economy, and the deficit, Certner said.

"Pension plans have certainly fallen pretty far down on the radar screen right now," he said.

BY FLORENCE OLSEN, KRISTEN RICAURTE-KNEBEL, AND
MARY HUGHES