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RETIREMENT ENHANCEMENT AND SAVINGS ACT OF 2016

NOVEMBER 16, 2016.—Ordered to be printed

Mr. HATCH, from the Committee on Finance,
submitted the following

R E P O R T

[To accompany S. 3471]

The Committee on Finance, having considered an original bill, S. 3471, to amend the Internal Revenue Code of 1986 to encourage retirement savings, and for other purposes, having considered the same, reports favorably thereon and recommends that the bill do pass.

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I. LEGISLATIVE BACKGROUND

The Committee on Finance, having considered S. 3471, the Retirement Enhancement and Savings Act of 2016, a bill to amend the Internal Revenue Code of 1986 to encourage retirement savings, and for other purposes, having considered the same, reports favorably thereon and recommends that the bill do pass.

Background and need for legislative action

Background—Based on a proposal recommended by Chairman Hatch, the Committee on Finance marked up original legislation (the "Retirement Enhancement and Savings Act of 2016") on September 21, 2016, and, with a majority present, ordered the bill favorably reported.

Need for legislative action—While many Americans have accumulated significant amounts in tax-favored retirement savings vehicles, studies show that many Americans have little, if any, retirement savings. Workplace retirement plans provide an effective way for employees to save for retirement, but not all employees have access to a plan, and, of those who do, some do not participate. Moreover, the shift in recent decades from employer-sponsored defined benefit plans, under which the default form of benefits is an annuity, to defined contributions plans, which generally do not offer annuity benefits, creates the risk of employees outliving their retirement savings. The Committee believes that legislation is necessary to provide new incentives for employers to adopt retirement plans (including ways to reduce the costs associated with having a plan), new incentives for workers to contribute to workplace plans and individual retirement arrangements, and other measures to further retirement income security.

Issues relating to retirement savings were the focus of the report issued last year by the Committee's Savings & Investment Working Group,[1] one of the Committee's bipartisan Tax Reform Working Groups. Various bills, including bills sponsored by Committee Members, have included legislative proposals addressing retirement savings issues and other employee benefits issues, such as—

- S. 1270, 113th Cong., the Secure Annuities for Employee (or SAFE) Retirement Act of 2013, sponsored by Senator Hatch;
- S. 1970, 113th Cong., the Retirement Security Act of 2014, sponsored by Senators Collins and Nelson;
- S. 1979, 113th Cong., the USA Retirement Funds Act, sponsored by Senators Harkin and Brown;
- S. 2855, 113th Cong., the Retirement Security Preservation Act of 2014, sponsored by Senators Cardin and Portman;
- The Retirement Improvements and Savings Enhancements (or RISE) Act of 2016, a discussion draft issued by Senator Wyden on September 8, 2016;
- S. 324, 114th Cong., the Shrinking Emergency Account Losses (or SEAL) Act of 2015, sponsored by Senators Enzi and Nelson;

[1] The report is available at *http://www.finance.senate.gov/imo/media/doc/The%20Savings%20& %20Investment%20Bipartisan%20Tax%20Working%20Group%20Report.pdf.*

• S. 609, 114th Cong., the Volunteer Responder Incentive Protection Act of 2015, sponsored by Senators Schumer and Collins;
• S. 1317, 114th Cong., the Lifetime Income Disclosure Act, sponsored by Senators Isakson and Murphy;
• S. 3025, 114th Cong., the Graduate Student Savings Act of 2016, sponsored by Senators Warren and Lee;
• S. 3152, 114th Cong., the Empowering Employees through Stock Ownership Act, sponsored by Senators Warner and Heller;
• S. 3181, 114th Cong., the S Corporation Modernization Act of 2016, sponsored by Senators Thune, Cardin and Roberts; and
• S. 3307, 114th Cong. (an act to avoid duplicative annual reporting), sponsored by Senators Warner and Collins.

In addition, as noted below, the Committee has held hearings at which it received testimony regarding retirement savings. These legislative proposals and hearings and the Working Group report informed the content of this bill.

Hearings

On January 28, 2016, the Committee held a hearing on Helping Americans Prepare for Retirement: Increasing Access, Participation and Coverage in Retirement Savings Plans, which included testimony on various proposals to increase retirement savings and reduce administrative burdens relating to retirement plans.

On September 16, 2014, the Committee held a hearing on Retirement Savings 2.0: Updating Savings Policy for the Modern Economy, which included testimony on new approaches to increase retirement savings.

II. EXPLANATION OF PROVISIONS

TITLE I—EXPANDING AND PRESERVING RETIREMENT SAVINGS

A. Multiple-Employer Plans and Pooled Employer and Multiple-Employer Plan Reporting (secs. 101–102 of the bill, sec. 413 of the Code, and secs. 3 and 103–104 of ERISA)

PRESENT LAW

Retirement savings under the Code and ERISA

Tax-favored arrangements

The Internal Revenue Code ("Code") provides two general vehicles for tax-favored retirement savings: employer-sponsored plans and individual retirement arrangements ("IRAs"). Code provisions are generally within the jurisdiction of the Secretary of the Treasury ("Secretary"), through his or her delegate, the Internal Revenue Service ("IRS").

The most common type of tax-favored employer-sponsored retirement plan is a qualified retirement plan,[2] which may be a defined contribution plan or a defined benefit plan. Under a defined con-

[2] Sec. 401(a). A qualified annuity plan under section 403(a) is similar to and subject to requirements similar to those applicable to qualified retirement plans.

tribution plan, separate individual accounts are maintained for participants, to which accumulated contributions, earnings and losses are allocated, and participants' benefits are based on the value of their accounts.[3] Defined contribution plans commonly allow participants to direct the investment of their accounts, usually by choosing among investment options offered under the plan. Under a defined benefit plan, benefits are determined under a plan formula and paid from general plan assets, rather than individual accounts.[4] Besides qualified retirement plans, certain tax-exempt employers and public schools may maintain tax-deferred annuity plans.[5]

An IRA is generally established by the individual for whom the IRA is maintained.[6] However, in some cases, an employer may establish IRAs on behalf of employees and provide retirement contributions to the IRAs.[7] In addition, IRA treatment may apply to accounts maintained for employees under a trust created by an employer (or an employee association) for the exclusive benefit of employees or their beneficiaries, provided that the trust complies with the relevant IRA requirements and separate accounting is maintained for the interest of each employee or beneficiary (referred to herein as an "IRA trust").[8] In that case, the assets of the trust may be held in a common fund for the account of all individuals who have an interest in the trust.

ERISA

Retirement plans of private employers, including qualified retirement plans and tax-deferred annuity plans, are generally subject to requirements under the Employee Retirement Income Security Act of 1974 ("ERISA").[9] A plan covering only business owners (or business owners and their spouses)—that is, it covers no other employees—is exempt from ERISA.[10] Thus, a plan covering only self-employed individuals is exempt from ERISA. Tax-deferred annuity plans that provide solely for salary reduction contributions by employees may be exempt from ERISA.[11] IRAs are generally exempt from ERISA.

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[3] Sec. 414(i). Defined contribution plans generally provide for contributions by employers and may include a qualified cash or deferred arrangement under section 401(k) (commonly called a "section 401(k) plan"), under which employees may elect to contribute to the plan.

[4] Sec. 414(j).

[5] Sec. 403(b). Private and governmental employers that are exempt from tax under section 501(c)(3), including tax-exempt private schools, may maintain tax-deferred annuity plans. State and local governmental employers may maintain another type of tax–favored retirement plan, an eligible deferred compensation plan under section 457(b).

[6] Sections 219, 408 and 408A provide rules for IRAs. Under section 408(a)(2) and (n), only certain entities are permitted to be the trustee of an IRA. The trustee of an IRA generally must be a bank, an insured credit union, or a corporation subject to supervision and examination by the Commissioner of Banking or other officer in charge of the administration of the banking laws of the State in which it is incorporated. Alternatively, an IRA trustee may be another person who demonstrates to the satisfaction of the Secretary that the manner in which the person will administer the IRA will be consistent with the IRA requirements.

[7] Simplified employee pension ("SEP") plans under section 408(k) and SIMPLE IRA plans under section 408(p) are employer-sponsored retirement plans funded using IRAs for employees.

[8] Sec. 408(c).

[9] ERISA applies to employee welfare benefit plans, such as health plans, of private employers, as well as to employer-sponsored retirement (or pension) plans. Employer-sponsored welfare and pension plans are both referred to under ERISA as employee benefit plans. Under ERISA sec. 4(b)(1) and (2), governmental plans and church plans are generally exempt from ERISA.

[10] 29 C.F.R. sec. 2510.3–3(b)–(c).

[11] 29 C.F.R. sec. 2510.3–2(f).

The provisions of Title I of ERISA are under the jurisdiction of the Secretary of Labor.[12] Many of the requirements under Title I of ERISA parallel Code requirements for qualified retirement plans. Under ERISA, in carrying out provisions relating to the same subject matter, the Secretary (of the Treasury) and the Secretary of Labor are required to consult with each other and develop rules, regulations, practices, and forms which, to the extent appropriate for efficient administration, are designed to reduce duplication of effort, duplication of reporting, conflicting or overlapping requirements, and the burden of compliance by plan administrators, employers, and participants and beneficiaries.[13] In addition, interpretive jurisdiction over parallel Code and ERISA provisions relating to retirement plans is divided between the two Secretaries by Executive Order, referred to as the Reorganization Plan No. 4 of 1978.[14]

Multiple-employer plans under the Code

In general

Qualified retirement plans, either defined contribution or defined benefit plans, are categorized as single-employer plans or multiple-employer plans. A single-employer plan is a plan maintained by one employer. For this purpose, businesses and organizations that are members of a controlled group of corporations, a group under common control, or an affiliated service group are treated as one employer (referred to as "aggregation").[15]

A multiple-employer plan generally is a single plan maintained by two or more unrelated employers (that is, employers that are not treated as a single employer under the aggregation rules).[16] Multiple-employer plans are commonly maintained by employers in the same industry and are used also by professional employer organizations ("PEOs") to provide qualified retirement plan benefits to employees working for PEO clients.[17]

Application of Code requirements to multiple-employer plans and EPCRS

Some requirements are applied to a multiple-employer plan on a plan-wide basis.[18] For example, all employees covered by the plan are treated as employees of all employers participating in the plan for purposes of the exclusive benefit rule. Similarly, an employee's service with all participating employers is taken into account in applying the minimum participation and vesting requirements. In applying the limits on contributions and benefits, compensation, contributions and benefits attributable to all employers are taken into

[12] The provisions of Title I of ERISA are codified at 29 U.S.C 1001–734. Under Title IV of ERISA, defined benefit plans of private employers are generally covered by the Pension Benefit Guaranty Corporation's pension insurance program.

[13] ERISA sec. 3004.

[14] 43 Fed. Reg. 47713 (October 17, 1978).

[15] Secs. 414(b), (c), (m) and (o).

[16] Sec. 413(c). Multiple-employer status does not apply if the plan is a multiemployer plan, defined under sec. 414(f) as a plan maintained pursuant to one or more collective bargaining agreements with two or more unrelated employers and to which the employers are required to contribute under the collective bargaining agreement(s). Multiemployer plans are also known as Taft-Hartley plans.

[17] Rev. Proc. 2003–86, 2003–2 C.B. 1211, and Rev. Proc. 2002–21, 2002–1 C.B. 911, address the application of the multiple-employer plan rules to qualified defined contribution plans maintained by PEOs

[18] Sec. 413(c).

account.[19] Other requirements are applied separately, including the minimum coverage requirements, nondiscrimination requirements (both the general requirements and the special tests for section 401(k) plans) and the top-heavy rules.[20] However, the qualified status of the plan as a whole is determined with respect to all employers maintaining the plan, and the failure by one employer (or by the plan itself) to satisfy an applicable qualification requirement may result in disqualification of the plan with respect to all employers.[21]

Because of the complexity of the requirements for qualified retirement plans, errors in plan documents, as well as plan operation and administration, commonly occur. Under a strict application of these requirements, such an error would cause a plan to lose its tax-favored status, which would fall most heavily on plan participants because of the resulting current income inclusion of vested amounts under the plan. As a practical matter, therefore, the IRS rarely disqualifies a plan. Instead, the IRS has established the Employee Plans Compliance Resolution System ("EPCRS"), a formal program under which employers and other plan sponsors can correct compliance failures and continue to provide their employees with retirement benefits on a tax-favored basis.[22]

EPCRS has three components, providing for self-correction, voluntary correction with IRS approval, and correction on audit. The Self-Correction Program ("SCP") generally permits a plan sponsor that has established compliance practices and procedures to correct certain insignificant failures at any time (including during an audit), and certain significant failures generally within a two-year period, without payment of any fee or sanction. The Voluntary Correction Program ("VCP") permits an employer, at any time before an audit, to pay a limited fee and receive IRS approval of a correction. For a failure that is discovered on audit and corrected, the Audit Closing Agreement Program ("Audit CAP") provides for a sanction that bears a reasonable relationship to the nature, extent, and severity of the failure and that takes into account the extent to which correction occurred before audit.

Multiple-employer plans are eligible for EPCRS, and certain special procedures apply.[23] A VCP request with respect to a multiple-employer plan must be submitted to the IRS by the plan administrator, rather than an employer maintaining the plan, and must be made with respect to the entire plan, rather than a portion of the plan affecting any particular employer. In addition, if a failure applies to fewer than all of the employers under the plan, the plan administrator may choose to have a VCP compliance fee or audit CAP sanction calculated separately for each employer based on the participants attributable to that employer, rather than having the compliance fee calculated based on the participants of the entire plan. For example, the plan administrator may choose this option when the failure is attributable to the failure of an employer to provide the plan administrator with full and complete information.

[19] Treas. Reg. sec. 1.415–1(e).
[20] Treas. Reg. secs. 1.413–2(a)(3)(ii)–(iii) and 1.416–1, G–2.
[21] Treas. Reg. secs. 1.413–2(a)(3)(iv) and 1.416–1, G–2.
[22] Rev. Proc. 2016–51, 2016–42 I.R.B. 465.
[23] Section 10.11 of Rev. Proc. 2016–51.

ERISA

Fiduciary and bonding requirements

Among other requirements, ERISA requires a plan to be established and maintained pursuant to a written instrument (that is, a plan document) that contains certain terms.[24] The terms of the plan must provide for one or more named fiduciaries that jointly or severally have authority to control and manage the operation and administration of the plan.[25] Among other required plan terms are a procedure for the allocation of responsibilities for the operation and administration of the plan and a procedure for amending the plan and for identifying the persons who have authority to amend the plan. Among other permitted terms, a plan may provide also that any person or group of persons may serve in more than one fiduciary capacity with respect to the plan (including service both as trustee and administrator) and that a person who is a named fiduciary with respect to the control or management of plan assets may appoint an investment manager or managers to manage plan assets.

In general, a plan fiduciary is responsible for the investment of plan assets. However, ERISA section 404(c) provides a special rule in the case of a defined contribution plan that permits participants to direct the investment of their individual accounts.[26] Under the special rule, if various requirements are met, a participant is not deemed to be a fiduciary by reason of directing the investment of the participant's account and no person who is otherwise a fiduciary is liable for any loss, or by reason of any breach, that results from the participant's investments. Defined contribution plans that provide for participant-directed investments commonly offer a set of investment options among which participants may choose. The selection of investment options to be offered under a plan is subject to ERISA fiduciary requirements.

Under ERISA, any plan fiduciary or person that handles plan assets is required to be bonded, generally for an amount not to exceed $500,000.[27] In some cases, the maximum bond amount is $1 million, rather than $500,000.

Multiple-employer plan status under ERISA

Like the Code, ERISA contains rules for multiple-employer retirement plans.[28] However, a different concept of multiple-employer plan applies under ERISA.

Under ERISA, an employee benefit plan (whether a pension plan or a welfare plan) must be sponsored by an employer, by an employee organization, or by both.[29] The definition of employer is any person acting directly as an employer, or indirectly in the interest of an employer, in relation to an employee benefit plan, and includes a group or association of employers acting for an employer in such capacity.[30]

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[24] ERISA sec. 402.

[25] Fiduciary is defined in ERISA section 3(21), and named fiduciary is defined in ERISA section 402(a)(2).

[26] ERISA sec. 404(c). Under ERISA, a defined contribution plans is referred to also as an individual account plan.

[27] ERISA sec. 412.

[28] ERISA sec. 210(a).

[29] ERISA sec. 3(1) and (2).

[30] ERISA sec. 3(5).

These definitional provisions of ERISA are interpreted as permitting a multiple-employer plan to be established or maintained by a cognizable, bona fide group or association of employers, acting in the interests of its employer members to provide benefits to their employees.[31] This approach is based on the premise that the person or group that maintains the plan is tied to the employers and employees that participate in the plan by some common economic or representational interest or genuine organizational relationship unrelated to the provision of benefits. Based on the facts and circumstances, the employers that participate in the benefit program must, either directly or indirectly, exercise control over that program, both in form and in substance, in order to act as a bona fide employer group or association with respect to the program. However, an employer association does not exist where several unrelated employers merely execute participation agreements or similar documents as a means to fund benefits, in the absence of any genuine organizational relationship between the employers. In that case, each participating employer establishes and maintains a separate employee benefit plan for the benefit of its own employees, rather than a multiple-employer plan.

Form 5500 reporting

Under the Code, an employer maintaining a qualified retirement plan generally is required to file an annual return containing information required under regulations with respect to the qualification, financial condition, and operation of the plan.[32] ERISA requires the plan administrator of certain pension and welfare benefit plans to file annual reports disclosing certain information to the Department of Labor ("DOL").[33] These filing requirements are met by filing a completed Form 5500, Annual Return/Report of Employee Benefit Plan. Forms 5500 are filed with DOL, and information from Forms 5500 is shared with the IRS.[34] In the case of a multiple-employer plan, the annual report must include a list of participating employers and a good faith estimate of the percentage of total contributions made by the participating employers during the plan year. Certain small plans, that is, plans covering fewer than 100 participants, are eligible for simplified reporting requirements, which are met by filing Form 5500–SF, Short Form Annual Return/Report of Small Employee Benefit Plan.[35]

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[31] See, for example, Department of Labor Advisory Opinions 2012–04A, 2003–17A, 2001–04A, and 1994–07A, and other authorities cited therein.

[32] Sec. 6058. In addition, under section 6059, the plan administrator of a defined benefit plan subject to the minimum funding requirements is required to file an annual actuarial report. Under Code section 414(g) and ERISA section 3(16), plan administrator generally means the person specifically so designated by the terms of the plan document. In the absence of a designation, the plan administrator generally is (1) in the case of a plan maintained by a single employer, the employer, (2) in the case of a plan maintained by an employee organization, the employee organization, or (3) in the case of a plan maintained by two or more employers or jointly by one or more employers and one or more employee organizations, the association, committee, joint board of trustees, or other similar group of representatives of the parties that maintain the plan. Under ERISA, the party described in (1), (2) or (3) is referred to as the "plan sponsor."

[33] ERISA secs. 103 and 104. Under ERISA section 4065, the plan administrator of certain defined benefit plans must provide information to the PBGC.

[34] Information is shared also with the PBGC, as applicable. Form 5500 filings are also publicly released in accordance with section 6104(b) and Treas. Reg. sec. 301.6104(b)–1 and ERISA secs. 104(a)(1) and 106(a).

[35] ERISA sec. 104(b).

REASONS FOR CHANGE

A single, multiple-employer plan can provide economies of scale that result in lower administrative costs than apply to a group of separate plans covering the employees of different employers. However, concern that a violation by another participating employer may jeopardize the tax-favored status of the plan, or create liability for other employers, may discourage use of multiple-employer plans. In addition, under ERISA, a plan covering employees of unrelated employers might not be eligible for multiple-employer plan treatment. The Committee wishes to remove possible barriers to broader use of multiple-employer plans, including by providing simplified Form 5500 reporting in appropriate cases.

In the case of any multiple-employer plan that, in accordance with the Department of Labor's current interpretations of the definition of employer in section 3(5) of ERISA, is treated currently as a single plan under ERISA, the Committee does not intend to modify the existing definition and regulatory guidance thereunder, except insofar as specifically provided herein with respect to relief from disqualification (or other loss of tax-favored status) and simplified annual reports.

EXPLANATION OF PROVISION

In general

The provision amends the Code rules relating to multiple-employer plans to provide that certain plans (referred to herein as "covered multiple-employer plans") will not fail to meet the Code requirements applicable for tax-favored treatment merely because one or more employers of employees covered by the plan (referred to herein as "participating employers") fail to take the actions that are required of employers for the plan to meet such requirements. The provision applies to a multiple-employer qualified defined contribution plan or a plan that consists of IRAs (referred to herein as an "IRA plan"), including under an IRA trust,[36] that either (1) is sponsored by employers all of which have both a common interest other than having adopted the plan and control of the plan, or (2) in the case of a plan not described in (1), has a pooled plan provider (referred to herein as a "pooled provider plan").

In addition, under the provision, a qualified defined contribution plan that is established or maintained for the purpose of providing benefits to the employees of two or more employers and that meets certain requirements (a "pooled employer plan") is treated for purposes of ERISA as a single plan that is a multiple-employer plan.

Tax-favored status under the Code

In general

The provision provides relief from disqualification (or other loss of tax-favored status) of the entire plan merely because one or more participating employers fail to take actions required with respect to the plan.

[36] Under the provision, in applying the exclusive benefit requirement under section 408(c) to an IRA plan with an IRA trust covering employees of unrelated employers, all employees covered by the plan are treated as employees of all employers participating in the plan.

Relief under the provision does not apply to a plan unless the terms of the plan provide that, in the case of an employer failing to take required actions (referred to herein as a "noncompliant employer")—

- plan assets attributable to employees of the noncompliant employer will be transferred to a plan maintained only by that employer (or its successor), to a tax-favored retirement plan for each individual whose account is transferred,[37] or to any other arrangement that the Secretary determines is appropriate, unless the Secretary determines it is in the best interests of the employees to retain the assets in the plan, and
- the noncompliant employer (and not the plan with respect to which the failure occurred or any other participating employer) is, except to the extent provided by the Secretary, liable for any plan liabilities attributable to employees of the noncompliant employer.

In addition, in the case of a pooled provider plan, if the pooled plan provider does not perform substantially all the administrative duties required of the provider (as described below) for any plan year, the Secretary, in his or her discretion, may provide that the determination as to whether the plan meets the Code requirements for tax-favored treatment will be made in the same manner as would be made without regard to the relief under the provision.

Pooled plan provider

Under the provision, "pooled plan provider" with respect to a plan means a person that—

- is designated by the terms of the plan as a named fiduciary under ERISA, as the plan administrator, and as the person responsible to perform all administrative duties (including conducting proper testing with respect to the plan and employees of each participating employer) that are reasonably necessary to ensure that the plan meets the Code requirements for tax-favored treatment and the requirements of ERISA and to ensure that each participating employer takes actions as the Secretary or the pooled plan provider determines necessary for the plan to meet Code and ERISA requirements, including providing to the pooled plan provider any disclosures or other information that the Secretary may require or that the pooled plan provider otherwise determines is necessary to administer the plan or to allow the plan to meet Code and ERISA requirements,
- registers with the Secretary as a pooled plan provider and provides any other information that the Secretary may require, before beginning operations as a pooled plan provider,
- acknowledges in writing its status as a named fiduciary under ERISA and as the plan administrator, and
- is responsible for ensuring that all persons who handle plan assets or are plan fiduciaries are bonded in accordance with ERISA requirements.

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[37] For this purpose, a tax-favored retirement plan means an eligible retirement plan as defined in section 402(c)(8)(B), that is, an IRA, a qualified retirement plan, a tax-deferred annuity plan under section 403(b), or an eligible deferred compensation plan of a State or local government employer under section 457(b).

The provision specifies that the Secretary may perform audits, examinations, and investigations of pooled plan providers as may be necessary to enforce and carry out the purposes of the provision.

Guidance

The provision directs the Secretary to issue guidance that the Secretary determines appropriate to carry out the provision, including guidance (1) to identify the administrative duties and other actions required to be performed by a pooled plan provider, (2) that describes the procedures to be taken to terminate a plan that fails to meet the requirements to be a covered multiple-employer plan, including the proper treatment of, and actions needed to be taken by, any participating employer and plan assets and liabilities attributable to employees of that employer, and (3) to identify appropriate cases in which corrective action will apply with respect to noncompliant employers. For purposes of (3), the Secretary is to take into account whether the failure of an employer or pooled plan provider to provide any disclosures or other information, or to take any other action, necessary to administer a plan or to allow a plan to meet the Code requirements for tax-favored treatment has continued over a period of time that clearly demonstrates a lack of commitment to compliance. Any guidance issued by the Secretary under the provision will not apply to any action or failure occurring before the issuance of the guidance.

The provision also directs the Secretary, in consultation with the Secretary of Labor when appropriate, to publish model plan language that meets the Code and ERISA requirements under the provision and that may be adopted to be treated as a pooled provider plan and pooled employer plan under ERISA.

Pooled employer plans under ERISA

In general

As described above, under the provision, a pooled employer plan is treated for purposes of ERISA as a single plan that is a multiple-employer plan. "Pooled employer plan" is defined as a plan (1) that is a defined contribution plan established or maintained for the purpose of providing benefits to the employees of two or more employers, (2) that is a qualified retirement plan or an IRA plan, and (3) the terms of which meet the requirements described below. Pooled employer plan does not include a plan with respect to which all the participating employers have both a common interest other than having adopted the plan and control of the plan.

In order for a plan to be a pooled employer plan, the plan terms must—

- designate a pooled plan provider and provide that the pooled plan provider is a named fiduciary of the plan,
- designate one or more trustees (other than a participating employer)[38] to be responsible for collecting contributions to, and holding the assets of, the plan, and require the trustees to implement written contribution collection procedures that are reasonable, diligent, and systematic,
- provide that each participating employer retains fiduciary responsibility for the selection and monitoring, in accordance

[38] Any trustee must meet the requirements under the Code to be an IRA trustee.

with ERISA fiduciary requirements, of the person designated as the pooled plan provider and any other person who is also designated as a named fiduciary of the plan, and, to the extent not otherwise delegated to another fiduciary by the pooled plan provider (and subject to the ERISA rules relating to self–directed investments), the investment and management of the portion of the plan's assets attributable to the employees of that participating employer,

- provide that a participating employer, or a participant or beneficiary, is not subject to unreasonable restrictions, fees, or penalties with regard to ceasing participation, receipt of distributions, or otherwise transferring assets of the plan in accordance with applicable rules for plan mergers and transfers,
- require the pooled plan provider to provide to participating employers any disclosures or other information that the Secretary of Labor may require, including any disclosures or other information to facilitate the selection or monitoring of the pooled plan provider by participating employers, and require each participating employer to take any actions that the Secretary of Labor or pooled plan provider determines necessary to administer the plan or to allow for the plan to meet the ERISA and Code requirements applicable to the plan, including providing any disclosures or other information that the Secretary of Labor may require or that the pooled plan provider otherwise determines is necessary to administer the plan or to allow the plan to meet ERISA and Code requirements, and
- provide that any disclosure or other information required to be provided as described above may be provided in electronic form and will be designed to ensure only reasonable costs are imposed on pooled plan providers and participating employers.

Under the provision, however, a pooled employer plan does not include a plan established before January 1, 2016, unless the plan administrator elects that the plan will be treated as a pooled employer plan and the plan meets the requirements of ERISA applicable to a pooled employer plan established on or after such date.[39]

In the case of a fiduciary of a pooled employer plan or a person handling assets of a pooled employer plan, the maximum bond amount under ERISA is $1 million.

Pooled plan provider

The definition of pooled plan provider for ERISA purposes is generally similar to the definition under the Code portion of the provision, described above.[40] The ERISA definition requires a person to register as a pooled plan provider with the Secretary of Labor and provide any other information that the Secretary of Labor may require, before beginning operations as a pooled plan provider.

The provision specifies that the Secretary of Labor may perform audits, examinations, and investigations of pooled plan providers as may be necessary to enforce and carry out the purposes of the provision.

[39] A pooled employer plan also does not include a multiemployer plan.

[40] In determining whether a person meets the requirements to be a pooled plan provider with respect to a plan, all persons that are members of the same controlled group or group under common control and that perform services for the plan are treated as one person.

Guidance

The provision directs the Secretary of Labor to issue guidance that such Secretary determines appropriate to carry out the provision, including guidance (1) to identify the administrative duties and other actions required to be performed by a pooled plan provider, and (2) that requires, in appropriate cases of a noncompliant employer, plan assets attributable to employees of the noncompliant employer to be transferred to a plan maintained only by that employer (or its successor), to a tax-favored retirement plan for each individual whose account is transferred, or to any other arrangement that the Secretary of Labor determines in the guidance is appropriate,[41] and the noncompliant employer (and not the plan with respect to which the failure occurred or any other participating employer) to be liable for any plan liabilities attributable to employees of the noncompliant employer, except to the extent provided in the guidance. For purposes of (2), the Secretary of Labor is to take into account whether the failure of an employer or pooled plan provider to provide any disclosures or other information, or to take any other action, necessary to administer a plan or to allow a plan to meet the requirements of ERISA and the Code requirements for tax-favored treatment, has continued over a period of time that clearly demonstrates a lack of commitment to compliance. Any guidance issued by the Secretary of Labor under the provision will not apply to any action or failure occurring before the issuance of the guidance.

Form 5500 reporting

Under the provision, the Form 5500 of a pooled employer plan must include the identifying information for the person designated under the terms of the plan as the pooled plan provider. In addition, with respect to annual reports required under ERISA, the Secretary of Labor may by regulation prescribe simplified reporting for a multiple-employer plan that covers fewer than 1,000 participants, but only if no single participating employer has 100 or more participants covered by the plan.

EFFECTIVE DATE

The provision applies to years beginning after December 31, 2019, and to Forms 5500 for plan years beginning after December 31, 2019.

Nothing in the Code amendments made by the provision is to be construed as limiting the authority of the Secretary of the Treasury (or the Secretary's delegate) to provide for the proper treatment of a failure to meet any Code requirement with respect to any employer (and its employees) in a multiple-employer plan.

[41] The Secretary of Labor may waive the requirement to transfer assets to another plan or arrangement in appropriate circumstances if the Secretary of Labor determines it is in the best interests of the employees of the noncompliant employer to retain the assets in the pooled employer plan.

B. Removal of 10 Percent Cap From Automatic Enrollment Safe Harbor After First Plan Year (sec. 103 of the bill and sec. 401(k) of the Code)

PRESENT LAW

Section 401(k) plans

A qualified defined contribution plan may include a qualified cash or deferred arrangement, under which employees may elect to have contributions made to the plan (referred to as "elective deferrals") rather than receive the same amount as current compensation (referred to as a "section 401(k) plan").[42] The maximum annual amount of elective deferrals that can be made by an employee for a year is $18,000 (for 2016) or, if less, the employee's compensation.[43] For an employee who attains age 50 by the end of the year, the dollar limit on elective deferrals is increased by $6,000 (for 2016) (called catch-up contributions).[44] An employee's elective deferrals must be fully vested. A section 401(k) plan may also provide for employer matching and nonelective contributions.

Automatic enrollment

A section 401(k) plan must provide each eligible employee with an effective opportunity to make or change an election to make elective deferrals at least once each plan year.[45] Whether an employee has an effective opportunity is determined based on all the relevant facts and circumstances, including the adequacy of notice of the availability of the election, the period of time during which an election may be made, and any other conditions on elections.

Section 401(k) plans are generally designed so that an employee will receive cash compensation unless the employee affirmatively elects to make elective deferrals to the section 401(k) plan. Alternatively, a plan may provide that elective deferrals are made at a specified rate (referred to as a "default rate") when an employee becomes eligible to participate unless the employee elects otherwise (that is, affirmatively elects not to make contributions or to make contributions at a different rate). This plan design is referred to as automatic enrollment.

Nondiscrimination test and automatic enrollment safe harbor

An annual nondiscrimination test, called the actual deferral percentage test (the "ADP" test) applies to elective deferrals under a section 401(k) plan.[46] The ADP test generally compares the average rate of deferral for highly compensated employees to the average rate of deferral for nonhighly compensated employees and requires that the average deferral rate for highly compensated employees not exceed the average rate for nonhighly compensated employees by more than certain specified amounts. If a plan fails to

[42] Elective deferrals are generally made on a pretax basis and distributions attributable to elective deferrals are includible in income. However, a section 401(k) plan is permitted to include a "qualified Roth contribution program" that permits a participant to elect to have all or a portion of the participant's elective deferrals under the plan treated as after-tax Roth contributions. Certain distributions from a designated Roth account are excluded from income, even though they include earnings not previously taxed.

[43] Sec. 402(g).

[44] Sec. 414(v).

[45] Treas. Reg. sec. 1.401(k)–1(e)(2)(ii).

[46] Sec. 401(k)(3).

satisfy the ADP test for a plan year based on the deferral elections of highly compensated employees, the plan is permitted to distribute deferrals to highly compensated employees ("excess deferrals") in a sufficient amount to correct the failure. The distribution of the excess deferrals must be made by the close of the following plan year.[47]

The ADP test is deemed to be satisfied if a section 401(k) plan includes certain minimum matching or nonelective contributions under either of two plan designs ("401(k) safe harbor plan"), as well as certain required rights and features and satisfies a notice requirement.[48] One type of 401(k) safe harbor includes automatic enrollment.

An automatic enrollment safe harbor plan must provide that, unless an employee elects otherwise, the employee is treated as electing to make elective deferrals at a default rate equal to a percentage of compensation as stated in the plan and at least (1) three percent of compensation for the first year the deemed election applies to the participant, (2) four percent during the second year, (3) five percent during the third year, and (4) six percent during the fourth year and thereafter. Although an automatic enrollment safe harbor plan generally may provide for default rates higher than these minimum rates, the default rate cannot exceed 10 percent for any year.

REASONS FOR CHANGE

The 10-percent cap on the default rate that may be used under an automatic enrollment safe harbor plan reflects a concern that too high a default rate may cause employees to elect out and not contribute at all, thus undercutting the purpose of the safe harbor. An initial default rate that is too high may have that effect. However, such an effect is less likely with respect to automatic increases in default rates for years after default contributions have begun. In such a case, the cap may instead have the effect of limiting how much is contributed and, thus, also limiting retirement savings. The Committee therefore believes the cap should be removed for years after default contributions have begun.

EXPLANATION OF PROVISION

Under the provision, the 10-percent limitation on the default rates under an automatic enrollment safe harbor plan is removed after the first year that an employee's deemed election applies.

EFFECTIVE DATE

The provision applies to plan years beginning after December 31, 2016.

[47] Sec. 401(k)(8).

[48] Sec. 401(k)(12) and (13). If certain additional requirements are met, matching contributions under 401(k) safe harbor plan may also satisfy a nondiscrimination test applicable under section 401(m).

C. Rules Relating to Election of Safe Harbor 401(k) Status (sec. 104 of the bill and sec. 401(k) of the Code)

Present Law

Section 401(k) plans

A qualified defined contribution plan may include a qualified cash or deferred arrangement, under which employees may elect to have contributions made to the plan (referred to as "elective deferrals") rather than receive the same amount as current compensation (referred to as a "section 401(k) plan").[49] The maximum annual amount of elective deferrals that can be made by an employee for a year is $18,000 (for 2016) or, if less, the employee's compensation.[50] For an employee who attains age 50 by the end of the year, the dollar limit on elective deferrals is increased by $6,000 (for 2016) (called catch-up contributions).[51] An employee's elective deferrals must be fully vested. A section 401(k) plan may also provide for employer matching and nonelective contributions.

Automatic enrollment

A section 401(k) plan must provide each eligible employee with an effective opportunity to make or change an election to make elective deferrals at least once each plan year.[52] Whether an employee has an effective opportunity is determined based on all the relevant facts and circumstances, including the adequacy of notice of the availability of the election, the period of time during which an election may be made, and any other conditions on elections.

Section 401(k) plans are generally designed so that an employee will receive cash compensation unless the employee affirmatively elects to make elective deferrals to the section 401(k) plan. Alternatively, a plan may provide that elective deferrals are made at a specified rate when an employee becomes eligible to participate unless the employee elects otherwise (that is, affirmatively elects not to make contributions or to make contributions at a different rate). This plan design is referred to as automatic enrollment.

Nondiscrimination test

General rule and design-based safe harbors

An annual nondiscrimination test, called the actual deferral percentage test (the "ADP" test) applies to elective deferrals under a section 401(k) plan.[53] The ADP test generally compares the average rate of deferral for highly compensated employees to the average rate of deferral for nonhighly compensated employees and requires that the average deferral rate for highly compensated employees not exceed the average rate for nonhighly compensated employees by more than certain specified amounts. If a plan fails to satisfy the ADP test for a plan year based on the deferral elections

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[49] Elective deferrals are generally made on a pretax basis and distributions attributable to elective deferrals are includible in income. However, a section 401(k) plan is permitted to include a "qualified Roth contribution program" that permits a participant to elect to have all or a portion of the participant's elective deferrals under the plan treated as after-tax Roth contributions. Certain distributions from a designated Roth account are excluded from income, even though they include earnings not previously taxed.

[50] Sec. 402(g).

[51] Sec. 414(v).

[52] Treas. Reg. sec. 1.401(k)–1(e)(2)(ii).

[53] Sec. 401(k)(3).

of highly compensated employees, the plan is permitted to distribute deferrals to highly compensated employees ("excess deferrals") in a sufficient amount to correct the failure. The distribution of the excess deferrals must be made by the close of the following plan year.[54]

The ADP test is deemed to be satisfied if a section 401(k) plan includes certain minimum matching or nonelective contributions under either of two plan designs ("401(k) safe harbor plan"), described below, as well as certain required rights and features and satisfies a notice requirement.[55]

Safe harbor contributions

Under one type of 401(k) safe harbor plan ("basic 401(k) safe harbor plan"), the plan either (1) satisfies a matching contribution requirement ("matching contribution basic 401(k) safe harbor plan") or (2) provides for a nonelective contribution to a defined contribution plan of at least three percent of an employee's compensation on behalf of each nonhighly compensated employee who is eligible to participate in the plan ("nonelective basic 401(k) safe harbor plan"). The matching contribution requirement under the matching contribution basic 401(k) safe harbor requires a matching contribution equal to at least 100 percent of elective contributions of the employee for contributions not in excess of three percent of compensation, and 50 percent of elective contributions for contributions that exceed three percent of compensation but do not exceed five percent, for a total matching contribution of up to four percent of compensation. The required matching contributions and the three percent nonelective contribution under the basic 401(k) safe harbor must be immediately nonforfeitable (that is, 100 percent vested) when made.

Another safe harbor applies for a section 401(k) plan that include automatic enrollment ("automatic enrollment 401(k) safe harbor"). Under an automatic enrollment 401(k) safe harbor, unless an employee elects otherwise, the employee is treated as electing to make elective deferrals equal to a percentage of compensation as stated in the plan, not in excess of 10 percent and at least (1) three percent of compensation for the first year the deemed election applies to the participant, (2) four percent during the second year, (3) five percent during the third year, and (4) six percent during the fourth year and thereafter.[56] Under the automatic enrollment 401(k) safe harbor, the matching contribution requirement is 100 percent of elective contributions of the employee for contributions not in excess of one percent of compensation, and 50 percent of elective contributions for contributions that exceed one percent of compensation but do not exceed six percent, for a total matching contribution of up to 3.5 percent of compensation ("matching contribution automatic enrollment 401(k) safe harbor"). The rate of nonelective contribution under the automatic enrollment 401(k) safe harbor plan

[54] Sec. 401(k)(8).

[55] Sec. 401(k)(12) and (13). If certain additional requirements are met, matching contributions under a 401(k) safe harbor plan may also satisfy a nondiscrimination test applicable under section 401(m).

[56] These automatic increases in default contribution rates are required for plans using the safe harbor. Rev. Rul. 2009–30, 2009–39 I.R.B. 391, provides guidance for including automatic increases in other plans using automatic enrollment, including under a plan that includes an eligible automatic contribution arrangement.

is three percent, as under the basic 401(k) safe harbor ("nonelective contribution automatic enrollment 401(k) safe harbor"). However, under the automatic enrollment 401(k) safe harbors, the matching and nonelective contributions are allowed to become 100 percent vested only after two years of service (rather than being required to be immediately vested when made).

Safe harbor notice

The notice requirement for a 401(k) safe harbor plan is satisfied if each employee eligible to participate is given, within a reasonable period before any year, written notice of the employee's rights and obligations under the arrangement and the notice meets certain content and timing requirements ("safe harbor notice"). To meet the content requirements, a safe harbor notice must be sufficiently accurate and comprehensive to inform an employee of the employee's rights and obligations under the plan, and be written in a manner calculated to be understood by the average employee eligible to participate in the plan. A safe harbor notice must provide certain information, including the plan's safe harbor contributions, any other plan contributions, the type and amount of compensation that may be deferred under the plan, how to make cash or deferred elections, the plan's withdrawal and vesting provisions, and specified contact information. In addition, a safe harbor notice for an automatic enrollment 401(k) safe harbor must describe certain additional information items, including the deemed deferral elections under the plan if the employee does not make an affirmative election and how contributions will be invested.

Delay in adopting nonelective 401(k) safe harbor

Generally the plan provisions for the requirements that must be satisfied to be a 401(k) safe harbor plan must be adopted before the first day of the plan year and remain in effect for an entire 12-month plan year. However, in the case of a nonelective 401(k) safe harbor plan (but not the matching contribution 401(k) safe harbor), a plan may be amended after the first day of the plan year but no later than 30 days before the end of the plan year to adopt the safe harbor plan provisions including providing the 3 percent of compensation nonelective contribution. The plan must also provide a contingent and follow-up notice. The contingent notice must be provided before the beginning of the plan year and specify that the plan may be amended to include the safe harbor nonelective contribution and, if it is so amended, a follow-up notice will be provided. If the plan is amended, the follow-up notice must be provided no later than 30 days before the end of the plan year stating that the safe harbor nonelective contribution will be provided.

REASONS FOR CHANGE

A nonelective contribution 401(k) safe harbor plan is beneficial to employees because it provides employer contributions regardless of whether employees make contributions. However, some aspects of the current procedural rules relating to adoption of the nonelective contribution 401(k) safe harbor, intended to protect employees, may serve as a barrier. The Committee believes that more flexible rules, combined with employee protections, will better facilitate the adoption of nonelective contribution 401(k) safe harbor plans.

EXPLANATION OF PROVISION

In general

The provision makes a number of changes to the rules for the nonelective contribution 401(k) safe harbor.

Elimination of notice requirement

The provision eliminates the safe harbor notice requirement with respect to nonelective 401(k) safe harbor plans. However, the general rule under present law requiring a section 401(k) plan to provide each eligible employee with an effective opportunity to make or change an election to make elective deferrals at least once each plan year still applies. As described above, relevant factors used in determining if this requirement is satisfied include the adequacy of notice of the availability of the election and the period of time during which an election may be made.

Delay in adopting provisions for nonelective 401(k) safe harbor

Under the provision, a plan can be amended to become a nonelective 401(k) safe harbor plan for a plan year, that is, amended to provide the required nonelective contributions and thereby satisfy the safe harbor requirements, at any time before the 30th day before the close of the plan year.

Further, the provision allows a plan to be amended after the 30th day before the close of the plan year to become a nonelective contribution 401(k) safe harbor plan for the plan year if (1) the plan is amended to provide for a nonelective contribution of at least four percent of compensation (rather than at least three percent) for all eligible employees for that plan year and (2) the plan is amended no later than the last day for distributing excess contributions for the plan year, that is, by the close of the following plan year.

EFFECTIVE DATE

The provision applies to plan years beginning after December 31, 2016.

D. Increase in Credit Limitation for Small Employer Pension Plan Start-Up Costs (sec. 105 of the bill and sec. 45E of the Code)

PRESENT LAW

Present law provides a nonrefundable income tax credit for qualified start-up costs of an eligible small employer that adopts a new qualified retirement plan, SIMPLE IRA plan or SEP (referred to as an eligible employer plan), provided that the plan covers at least one nonhighly compensated employee.[57] Qualified start-up costs are expenses connected with the establishment or administration of the plan or retirement-related education for employees with respect to the plan. The credit is the lesser of (1) a flat dollar amount of $500 per year or (2) 50 percent of the qualified start-up costs. The credit applies for up to three years beginning with the year the

[57] A nonhighly compensated employee is an employee who is not a highly compensated employee as defined under section 414(q).

plan is first effective, or, at the election of the employer, with the year preceding the first plan year.

An eligible employer is an employer that, for the preceding year, had no more than 100 employees, each with compensation of $5,000 or more. In addition, the employer must not have had a plan covering substantially the same employees as the new plan during the three years preceding the first year for which the credit would apply. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[58] All eligible employer plans of an employer are treated as a single plan.

No deduction is allowed for the portion of qualified start-up costs paid or incurred for the taxable year equal to the amount of the credit.

REASONS FOR CHANGE

Studies show that small employers are less likely to offer retirement plans than large employers. The credit for small employer pension plan start-up costs is intended to encourage small employers to adopt plans. The Committee believes that increasing the amount of the credit will encourage more small employers to adopt plans.

EXPLANATION OF PROVISION

The provision changes the calculation of the flat dollar amount limit on the credit. The flat dollar amount for a taxable year is the greater of (1) $500 or (2) the lesser of (a) $250 multiplied by the number of nonhighly compensated employees of the eligible employer who are eligible to participate in the plan or (b) $5,000. As under present law, the credit applies for up to three years.

EFFECTIVE DATE

The provision applies to taxable years beginning after December 31, 2016.

E. SMALL EMPLOYER AUTOMATIC ENROLLMENT CREDIT (SEC. 106 OF THE BILL AND NEW SEC. 45S OF THE CODE)

PRESENT LAW

Small employer startup credit

Present law provides a nonrefundable income tax credit for qualified start-up costs of an eligible small employer that adopts a new qualified retirement plan, SIMPLE IRA plan or SEP (referred to as an eligible employer plan), provided that the plan covers at least one nonhighly compensated employee.[59] Qualified start-up costs are expenses connected with the establishment or administration of the plan or retirement-related education for employees with respect to the plan. The credit is the lesser of (1) a flat dollar amount of $500 per year or (2) 50 percent of the qualified start-up costs. The credit applies for up to three years beginning with the year the

[58] Sec. 52 (a) or (b) and 414(m) or (o).

[59] Sec. 45E. A nonhighly compensated employee is an employee who is not a highly compensated employee as defined under section 414(q).

plan is first effective, or, at the election of the employer, with the year preceding the first plan year.

An eligible employer is an employer that, for the preceding year, had no more than 100 employees with compensation of $5,000 or more. In addition, the employer must not have had a plan covering substantially the same employees as the new plan during the three years preceding the first year for which the credit would apply. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[60] All eligible employer plans of an employer are treated as a single plan.

No deduction is allowed for the portion of qualified start-up costs paid or incurred for the taxable year equal to the amount of the credit.

Automatic enrollment

A qualified defined contribution plan may include a qualified cash or deferred arrangement under which employees may elect to have plan contributions ("elective deferrals") made rather than receive cash compensation (commonly called a "section 401(k) plan"). A SIMPLE IRA plan is an employer-sponsored retirement plan funded with individual retirement arrangements ("IRAs") that also allows employees to make elective deferrals.[61] Section 401(k) plans and SIMPLE IRA plans may be designed so that the employee will receive cash compensation unless the employee affirmatively elects to make elective deferrals to the plan. Alternatively, a plan may provide that elective deferrals are made at a specified rate (when the employee becomes eligible to participate) unless the employee elects otherwise (i.e., affirmatively elects not to make contributions or to make contributions at a different rate). This alternative plan design is referred to as automatic enrollment.

REASONS FOR CHANGE

Studies show that automatic enrollment increases employee participation in section 401(k) and SIMPLE IRA plans, resulting in higher retirement savings. The Committee believes that providing a credit to small employers may encourage more employers to use an automatic enrollment design.

EXPLANATION OF PROVISION

Under the provision, an eligible employer is allowed a credit of $500 per year for up to three years for startup costs for new section 401(k) plans and SIMPLE IRA plans that include automatic enrollment, in addition to the plan start-up credit allowed under present law. An eligible employer is also allowed a credit of $500 per year for up to three years if it converts an existing plan to an automatic enrollment design.

EFFECTIVE DATE

The provision applies to taxable years beginning after December 31, 2016.

[60] Sec. 52 (a) or (b) and 414(m) or (o).
[61] Sec. 408(p).

F. CERTAIN TAXABLE NON-TUITION FELLOWSHIP AND STIPEND PAYMENTS TREATED AS COMPENSATION FOR IRA PURPOSES (SEC. 107 OF THE BILL AND SEC. 219 OF THE CODE)

PRESENT LAW

There are two general types of individual retirement arrangements ("IRAs"): traditional IRAs and Roth IRAs.[62] The total amount that an individual may contribute to one or more IRAs for a year is generally limited to the lesser of: (1) a dollar amount ($5,500 for 2016); and (2) the amount of the individual's compensation that is includible in gross income for the year.[63] In the case of an individual who has attained age 50 by the end of the year, the dollar amount is increased by $1,000. In the case of a married couple, contributions can be made up to the dollar limit for each spouse if the combined compensation of the spouses that is includible in gross income is at least equal to the contributed amount.

An individual may make contributions to a traditional IRA (up to the contribution limit) without regard to his or her adjusted gross income. An individual may deduct his or her contributions to a traditional IRA if neither the individual nor the individual's spouse is an active participant in an employer-sponsored retirement plan. If an individual or the individual's spouse is an active participant in an employer-sponsored retirement plan, the deduction is phased out for taxpayers with adjusted gross income over certain levels.[64]

Individuals with adjusted gross income below certain levels may make contributions to a Roth IRA (up to the contribution limit).[65] Contributions to a Roth IRA are not deductible.

As described above, an individual's IRA contributions generally cannot exceed the amount of his or her compensation that is includible in gross income. Subject to the rule for spouses, described above, an individual who has no includible compensation income generally is not eligible to make IRA contributions, even if the individual has other income that is includible in gross income.[66]

REASONS FOR CHANGE

Graduate and postdoctoral students often receive stipends and similar amounts that are not treated as compensation and thus cannot be the basis for IRA contributions. This delays the ability to accumulate tax-favored retirement savings, in some cases for a number of years. The Committee believes that treating such amounts as compensation for IRA contribution purposes will enable some graduate and postdoctoral students to begin saving for retirement.

EXPLANATION OF PROVISION

Under the provision, an amount that is includible in income and is paid to an individual to aid the individual in the pursuit of grad-

[62] Secs. 408 and 408A.

[63] Sec. 219(b)(2) and (5), as referenced in secs. 408(a)(1) and (b)(2)(B) and 408A(c)(2). Under section 4973, IRA contributions in excess of the applicable limit are generally subject to an excise tax of six percent per year until withdrawn.

[64] Sec. 219(g).

[65] Sec. 408A(c)(3).

[66] Under a special rule in section 219(f)(1), alimony that is includible in gross income under section 71 is treated as compensation for IRA contribution purposes.

uate or postdoctoral study or research, such as a fellowship, stipend or similar amount, is treated as compensation taken into account for IRA contribution purposes.

EFFECTIVE DATE

This provision applies for taxable years beginning after December 31, 2016.

G. REPEAL OF MAXIMUM AGE FOR TRADITIONAL IRA CONTRIBUTIONS (SEC. 108 OF THE BILL AND SEC. 219 OF THE CODE)

PRESENT LAW

Under present law, an individual may make deductible contributions to a traditional IRA up to the IRA contribution limit if neither the individual nor the individual's spouse is an active participant in an employer-sponsored retirement plan.[67] If an individual (or the individual's spouse) is an active participant in an employer-sponsored retirement plan, the deduction is phased out for taxpayers with adjusted gross income ("AGI") for the taxable year over certain indexed levels.[68] To the extent an individual cannot or does not make deductible contributions to a traditional IRA, the individual may make nondeductible contributions to a traditional IRA (without regard to AGI limits). Alternatively, subject to AGI limits, an individual may make nondeductible contributions to a Roth IRA.[69]

An individual who has attained age 70½ by the close of a year is not permitted to make contributions to a traditional IRA.[70] This restriction does not apply to contributions to a Roth IRA.[71] In addition, employees over age 70½ are not precluded from contributing to employer-sponsored plans.

REASONS FOR CHANGE

More and more older Americans are continuing to work past traditional retirement ages. This provides current income, as well as the potential for additional retirement savings. An individual working past age 70½ may contribute to an employer–sponsored retirement plan, if available, or to a Roth IRA, but not to a traditional IRA. The Committee wishes to remove this impediment to retirement savings.

EXPLANATION OF PROVISION

The provision repeals the prohibition on contributions to a traditional IRA by an individual who has attained age 70½.

EFFECTIVE DATE

The provision applies to contributions made for taxable years beginning after December 31, 2016.

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[67] Sec. 219.
[68] Sec. 219(g).
[69] Sec. 408(o). The annual contribution limit for IRAs is coordinated so that the maximum amount that can be contributed to all of an individual's IRAs (both traditional and Roth) for a taxable year is the lesser of a certain dollar amount ($5,500 for 2016) or the individual's compensation.
[70] Sec. 219(d)(1).
[71] Sec. 408A(c)(4).

H. Expansion of IRA Ownership of S Corporation Bank Stock (sec. 109 of the bill and secs. 1361 and 4975 of the Code)

PRESENT LAW

IRAs

An individual retirement account ("IRA") is a tax-exempt trust or account established for the exclusive benefit of an individual and his or her beneficiaries.[72] There are two general types of IRAs: traditional IRAs, to which both deductible and nondeductible contributions may be made, and Roth IRAs, contributions to which are not deductible. In general, amounts held in a traditional IRA are includible in income when withdrawn (except to the extent the withdrawal is a return of nondeductible contributions). Amounts held in a Roth IRA that are withdrawn as a qualified distribution are not includible in income; distributions from a Roth IRA that are not qualified distributions are includible in income to the extent attributable to earnings. A qualified distribution is a distribution that is made (1) after the five-taxable year period beginning with the first taxable year for which the individual made a contribution to a Roth IRA, and (2) after attainment of age 59½, on account of death or disability, or for first-time homebuyer expenses of up to $10,000.

S corporations and permissible shareholders

In general, an S corporation is not subject to corporate-level income tax on its items of income and loss.[73] Instead, an S corporation passes through its items of income and loss to its shareholders. The shareholders take into account separately their shares of these items on their individual income tax returns.

Only certain tax-exempt organizations are permitted to be shareholders of an S corporation, including qualified retirement plans. Under present law, an IRA, including a Roth IRA, is permitted to be a shareholder of an S corporation only if the S corporation is a bank and only to the extent of bank stock held by the IRA on October 22, 2004.[74] In the case of a tax-exempt S corporation shareholder, including an IRA, the shareholder's interest in the S corporation is treated as an unrelated trade or business and its share of S corporation items of income and loss (and gain or loss on disposition of the S corporation stock) is taken into account in determining its unrelated business taxable income.[75]

REASONS FOR CHANGE

The Committee wishes to remove the limit on individuals' ability to invest IRA assets in stock of an S corporation that is a bank.

EXPLANATION OF PROVISION

Under the provision, an IRA, including a Roth IRA, is permitted to be a shareholder of an S corporation that is a bank without regard to whether the IRA held the bank stock on October 22, 2004.

[72] Secs. 408 and 408A.
[73] The rules for S corporations are in Subchapter S of the Code, sections 1361–1379.
[74] This is the date of enactment of the American Jobs Creation Act, Pub. L. No. 108–357, which allowed an IRA to be a shareholder of an S corporation that is a bank. A related exemption under section 4975(d)(16) of the prohibited transaction rules allowed stock held by an IRA at the time a bank elected to become an S corporation to be sold to the IRA owner.
[75] Sec. 512(e). This rule does not apply to employee stock ownership plans.

Thus, any IRA is permitted to be a shareholder of any S corporation that is a bank.[76] As under present law, an IRA's interest in an S corporation is treated as an unrelated trade or business and its share of S corporation items of income and loss (and gain or loss on disposition of the S corporation stock) is taken into account in determining its unrelated business taxable income.

EFFECTIVE DATE

The provision is effective January 1, 2016.

I. EXTENDED ROLLOVER PERIOD FOR PLAN LOAN OFFSET AMOUNTS (SEC. 110 OF THE BILL AND SEC. 402(c) OF THE CODE)

PRESENT LAW

Taxation of retirement plan distributions

General rule

A distribution from a tax-favored employer-sponsored retirement plan (that is, a qualified retirement plan, section 403(b) plan, or a governmental section 457(b) plan) is generally includible in gross income, except to the extent that the distribution is a recovery of basis under the plan, or the amount of the distribution is contributed to an eligible retirement plan (that is, another tax-favored employer-sponsored retirement plan or an individual retirement arrangement ("IRA")) in a tax-free rollover. In the case of a distribution from a retirement plan to a participant under age 59½, the distribution (other than a distribution from a governmental section 457(b) plan) is also subject to a 10-percent early distribution tax, unless an exception applies.[77]

Rollovers

A distribution from a tax-favored employer-sponsored retirement plan that is an eligible rollover distribution may be rolled over to an eligible retirement plan. The rollover generally can be achieved by direct rollover (direct payment from the distributing plan to the recipient plan) or by contributing the distribution to the eligible retirement plan within 60 days of receiving the distribution ("60-day rollover"). Amounts that are rolled over are usually not included in gross income. Generally, any distribution of the balance to the credit of a participant is an eligible rollover distribution with exceptions, for example, certain periodic payments, required minimum distributions, and hardship distributions.[78]

Tax-favored employer-sponsored retirement plans are required to offer a direct rollover with respect to any eligible rollover distribution before paying the amount to the participant or beneficiary.[79]

[76] The provision also amends the exemption under section 4975(d)(16) of the prohibited transaction rules to allow stock held by an IRA at the time a bank elects to become an S corporation to be sold to the IRA owner.

[77] Sec. 72(t).

[78] Sec. 402(c)(4). Treas. Reg. sec. 1.402(c)–1 identifies certain other payments that are not eligible for rollover, including, for example, certain corrective distributions, loans that are treated as deemed distributions under section 72(p), and dividends on employer securities as described in section 404(k). In addition, pursuant to section 402(c)(11), any distribution to a beneficiary other than the participant's surviving spouse is only permitted to be rolled over to an IRA using a direct rollover; 60-day rollovers are not available to nonspouse beneficiaries.

[79] Sec. 401(a)(31). Unless a participant elects otherwise, a mandatory cash-out of more than $1,000 must be directly rolled over to an IRA chosen by the plan administrator or the payor.

If an eligible rollover distribution is not directly rolled over into an eligible retirement plan, the taxable portion of the distribution generally is subject to mandatory 20-percent income tax withholding.[80]

Plan loan as a deemed distribution

Tax-favored employer-sponsored retirement plans may provide loans to participants. Unless the loan satisfies certain requirements in both form and operation, the amount of a retirement plan loan is a deemed distribution from the retirement plan.[81] These requirements include the following: the amount of the loan must not exceed the lesser of 50 percent of the participant's account balance or $50,000; the terms of the loan must provide for a repayment period of not more than five years[82] and provide for level amortization of loan payments (with payments not less frequently than quarterly); and the terms of the loan must be legally enforceable. The rules do not limit the number of loans an employee may obtain from a plan.

If a plan participant ceases to make payments on a loan before it is repaid according to the required schedule, a deemed distribution of the outstanding loan balance generally occurs. This deemed distribution of an unpaid loan balance is generally taxed as though an actual distribution occurred, including being subject to a 10-percent early distribution tax, if applicable. However, a deemed distribution is not eligible for rollover to another eligible retirement plan.

Loan offset amount

A plan may also provide that, in certain circumstances, for example, when a participant terminates employment with the employer, a participant's obligation to repay a loan is accelerated and, if the loan is not repaid, the loan is cancelled and the amount in participant's account balance is offset by the amount attributable to the loan (that is, the amount of the unpaid loan balance), referred to as a plan loan offset. In the case of a plan loan offset, an actual distribution equal to the unpaid loan balance is considered to occur, rather than a deemed distribution as described above, and, unlike a deemed distribution, the amount of the distribution is eligible for tax-free rollover to another eligible retirement plan.[83] However, the plan is not required to offer a direct rollover with respect to a plan loan offset amount that is an eligible rollover distribution, and the plan loan offset amount is generally not subject to 20-percent income tax withholding.[84]

REASONS FOR CHANGE

A plan loan offset does not involve the current payment of funds to a participant. Thus, in order to roll over a plan offset amount, a participant must have other funds in that amount available. If a loan offset occurs at the time of a participant's termination of employment, the participant might not have funds immediately available for the rollover, particularly in the case of an involuntary ter-

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[80] Treas. Reg. sec. 1.402(c)–2, Q&A–1(b)(3).
[81] Sec. 72(p).
[82] Loans specifically for home purchases may be repaid over a longer period.
[83] Treas. Reg. sec.1.402(c)–2, A–9.
[84] Treas. Reg. sec. 1.401(a)(31)–1, A–16, and Treas. Reg. sec. 31.3405(c)–1, A–11.

mination. In addition, the participant may not know the precise date when the 60-day rollover period begins. The Committee believes that providing a longer rollover period with respect to plan loan offsets may result in more rollovers, thus preserving retirement savings.

EXPLANATION OF PROVISION

Under the provision, the period during which a qualified plan loan offset amount may be contributed to an eligible retirement plan as a rollover contribution is extended from 60 days after the date of the offset to the due date (including extensions) for filing the Federal income tax return for the taxable year in which the plan loan offset occurs (meaning the taxable year in which the amount is treated as distributed by the plan). The extended rollover period applies with respect to a rollover of all, or a portion, of a qualified plan loan offset amount. Under the provision, a qualified plan loan offset amount is a plan loan offset amount which is treated as distributed from a tax-favored employer-sponsored retirement plan to a participant or beneficiary solely by reason of either the termination of the plan, or the failure to meet the repayment terms of the loan from such plan because of the separation from service of the participant (whether due to layoff, cessation of business, termination of employment, or otherwise). As under present law, a loan offset amount under the provision is the amount by which a participant's accrued benefit under the plan is reduced to repay a loan from the plan.

EFFECTIVE DATE

The provision applies to loan offsets made in taxable years beginning after December 31, 2016.

J. Modification of Rules Relating to Hardship Withdrawals From Cash or Deferred Arrangements (sec. 111 of the bill and sec. 401(k) of the Code)

PRESENT LAW

A qualified defined contribution plan may include a qualified cash or deferred arrangement, under which employees may elect to have contributions made to the plan (referred to as "elective deferrals") rather than receive the same amount as current compensation (referred to as a "section 401(k) plan"). Amounts attributable to elective deferrals generally are subject to distribution restrictions. Such amounts cannot be distributed before the earliest of the employee's severance from employment, death, disability or attainment of age 59½, or termination of the plan. However, in certain circumstances, elective deferrals, but not associated earnings, can also be distributed on account of hardship.[85]

An employer may also make nonelective and matching contributions for employees under a section 401(k) plan. Elective deferrals, and matching contributions and after-tax employee contributions, are subject to special tests ("nondiscrimination tests") to prevent discrimination in favor of highly compensated employees. Nonelec-

[85] Sec. 401(k)(2)(B)(i)(IV). Under section 72(t), distributions on account of hardship may be subject to an additional 10-percent early distribution tax.

tive contributions and matching contributions that satisfy certain requirements ("qualified nonelective contributions and qualified matching contributions") may be used to enable the plan to satisfy these nondiscrimination tests. One of the requirements is that these contributions be subject to the same distribution restrictions as elective deferrals, except that these contributions (and attributable earnings) are not permitted to be distributed on account of hardship.

Applicable Treasury regulations provide that a distribution is made on account of hardship only if the distribution is made on account of an immediate and heavy financial need of the employee and is necessary to satisfy the heavy need.[86] Generally, the determination of whether these two requirements are met is based on the relevant facts and circumstances. However, a safe harbor applies under which a distribution may be deemed to be on account of hardship. One requirement of the safe harbor is that the employee represent that the need cannot be satisfied through currently available plan loans. This in effect requires an employee to take any available plan loan before receiving a hardship distribution. Another requirement is that the employee be prohibited from making elective deferrals and employee contributions to the plan and all other plans maintained by the employer for at least six months after receipt of the hardship distribution.

REASONS FOR CHANGE

The rules relating to hardship distributions contain fine distinctions that create complexity for employers and plan administrators. These distinctions may lead to inadvertent errors, correction of which increases plan costs, and may also cause confusion for employees. In addition, the rule prohibiting employees from making contributions for six months after receiving a hardship distribution impedes employees' ability to replace distributed funds. The Committee believes that the rules relating to hardship withdrawals should be more consistent and should not impede retirement savings.

EXPLANATION OF PROVISION

The provision allows earnings on elective deferrals under a section 401(k) plan, as well as qualified nonelective contributions and qualified matching contributions (and attributable earnings), to be distributed on account of hardship. Further, a distribution is not treated as failing to be on account of hardship solely because the employee does not take any available plan loan.

In addition, the Secretary of the Treasury is directed, within one year of the date of enactment, to revise the regulations relating to the hardship safe harbor to eliminate the requirement that an employee be prohibited from making elective deferrals and employee contributions for six months after the receipt of a hardship distribution. It is intended that an employee not be prevented for any period after the receipt of a hardship distribution from making elective deferrals and employee contributions.

[86] Treas. Reg. sec. 1.401(k)–1(d)(3).

EFFECTIVE DATE

The provision applies to plan years beginning after December 31, 2016.

K. Qualified Employer Plans Prohibited From Making Loans Through Credit Cards and Other Similar Arrangements (sec. 112 of the bill and sec. 72(p) of the Code)

PRESENT LAW

Qualified employer plans may provide loans to participants.[87] Unless the loan satisfies certain requirements in both form and operation as discussed above, the amount of a plan loan is a deemed distribution from the plan. These requirements include the following: the amount of the loan must not exceed the lesser of 50 percent of the participant's account balance or $50,000 (generally taking into account outstanding balances of previous loans); the terms of the loan must provide for a repayment period of not more than five years[88] and provide for level amortization of loan payments (with payments not less frequently than quarterly); and the terms of the loan must be legally enforceable. Subject to the limit on the amount of loans, which precludes any additional loan that would cause the limit to be exceeded, the rules relating to loans do not limit the number of loans an employee may obtain from a plan. Some arrangements have developed under which an employee can access plan loans through the use of a credit card or similar mechanism.

REASONS FOR CHANGE

The availability of plan loans may encourage employees to contribute to a retirement plan with the knowledge that funds may be accessed if needed. However, loans that are not repaid have the effect of depleting retirement savings. Easy access to plan loans through credit or debit cards and similar arrangements may lead to the use of retirement plan assets for routine or small purchases and, over time, result in an accumulated loan balance that an employee cannot repay. The Committee believes that appropriate limits should be placed on such arrangements.

EXPLANATION OF PROVISION

Under the provision, a plan loan that is made through the use of a credit card or similar arrangement generally does not meet the requirements for loan treatment and is therefore a deemed distribution. However, an exception applies to the extent a loan is provided through an electronic card system which, as of September 21, 2016, was available for use to provide loans under qualified employer plans. The exception does not apply to a loan resulting from a transaction of $1,000[89] or less or to a transaction with or on the

[87] A qualified employer plan is a qualified retirement plan under section 401(a) or 403(a), a tax-deferred annuity plan under section 403(b), or a plan established and maintained for its employees by the United States, a State or political subdivision, or an agency or instrumentality of any of the foregoing.

[88] Loans specifically for home purchases may be repaid over a longer period.

[89] For loans made in plan years beginning after December 31, 2017, this amount is increased to reflect cost-of-living increases, with any increase rounded down to the next lowest multiple of $50.

premises of a liquor store, casino, gaming establishment, or any retail establishment that provides adult-oriented entertainment.[90]

The provision directs the Government Accountability Office ("GAO") to conduct a study of the impact of loans provided through credit cards and similar arrangements on the use of retirement savings for purposes other than funding retirement (referred to as "leakage"). GAO is to report the results of its study within one year after enactment of the provision to the Chairman and Ranking Member of the Senate Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives. If the study shows that such loans, after implementation of the restrictions under the provision, result in greater leakage than other loans from retirement plans, the report must include recommendations to reduce leakage.

EFFECTIVE DATE

The provision applies to plan years beginning after December 31, 2016.

L. PORTABILITY OF LIFETIME INCOME OPTIONS (SEC. 113 OF THE BILL AND SECS. 401(a), 403(b) AND 457(d) OF THE CODE)

PRESENT LAW

Distribution restrictions for accounts under employer-sponsored plans

Types of plans and contributions

Tax-favored employer-sponsored retirement plans under which individual accounts are maintained for employees include qualified defined contribution plans, tax-deferred annuity plans (referred to as "section 403(b)" plans), and eligible deferred compensation plans of State and local government employers (referred to as "governmental section 457(b)" plans).

Contributions to a qualified defined contribution plan or section 403(b) plan may include some or all of the following types of contributions:

- pretax elective deferrals (that is, pretax contributions made at the election of an employee in lieu of receiving cash compensation),
- after-tax designated Roth contributions (that is, elective deferrals made on an after-tax basis to a Roth account under the plan),
- after-tax employee contributions (other than designated Roth contributions),
- pretax employer matching contributions (that is, employer contributions made as a result of an employee's elective deferrals, designated Roth contributions, or after-tax contributions), and
- pretax employer nonelective contributions (that is, employer contributions made without regard to whether an employee makes elective deferrals, designated Roth contributions, or after-tax contributions).

[90] These establishments are described by reference to section 408(a)(12)(A)(i), (ii) and (iii) of the Social Security Act.

Contributions to a governmental section 457(b) plan generally consist of pretax elective deferrals and, if provided for under the plan, designated Roth contributions.

Restrictions on in-service distributions

The terms of an employer-sponsored retirement plan generally determine when distributions are permitted. However, in some cases, statutory restrictions on distributions may apply.

Elective deferrals under a qualified defined contribution plan are subject to statutory restrictions on distribution before severance from employment, referred to as "in-service" distributions.[91] In-service distributions of elective deferrals (and related earnings) generally are permitted only after attainment of age 59½ or termination of the plan. In-service distributions of elective deferrals (but not related earnings) are also permitted in the case of hardship.

Other distribution restrictions may apply to contributions under certain types of qualified defined contribution plans. A profit-sharing plan generally may allow an in-service distribution of an amount contributed to the plan only after a fixed number of years (not less than two).[92] A money purchase pension plan generally may not allow an in-service distribution before attainment of age 62 (or attainment of normal retirement age under the plan if earlier) or termination of the plan.[93]

Elective deferrals under a section 403(b) plan are subject to in-service distribution restrictions similar to those applicable to elective deferrals under a qualified defined contribution plan, and, in some cases, other contributions to a section 403(b) plan are subject to similar restrictions.[94] Deferrals under a governmental section 457(b) plan are subject to in-service distribution restrictions similar to those applicable to elective deferrals under a qualified defined contribution plan, except that in-service distributions under a governmental section 457(b) plan apply until age 70½ (rather than age 59½).[95]

Distributions and rollovers

A distribution from an employer-sponsored retirement plan is generally includible in income except for any portion attributable to after-tax contributions, which result in basis.[96] Unless an exception applies, in the case of a distribution before age 59½ from a qualified retirement plan or a section 403(b) plan, any amount included in income is subject to an additional 10-percent tax, referred to as the "early withdrawal" tax.[97]

A distribution from an employer-sponsored retirement plan generally may be rolled over on a nontaxable basis to another such plan or to an individual retirement arrangement ("IRA"), either by a direct transfer to the recipient plan or IRA or by contributing the

[91] Sec. 401(k)(2)(B). Similar restrictions apply to certain other contributions, such as employer matching or nonelective contributions required under the nondiscrimination safe harbors under section 401(k).

[92] Rev. Rul. 71–295, 1971–2 C.B. 184, and Treas. Reg. sec. 1.401–1(b)(1)(ii). Similar rules apply to a stock bonus plan. Treas. Reg. sec. 1.401–1(b)(1)(iii).

[93] Sec. 401(a)(36) and Treas. Reg. secs. 1.401–1(b)(1)(i) and 1.401(a)–1(b).

[94] Secs. 403(b)(7)(A)(ii) and 403(b)(11).

[95] Sec. 457(d)(1)(A).

[96] Secs. 402(a), 403(b)(1) and 457(a)(1). Under section 402A(d), a qualified distribution from a designated Roth account under an employer-sponsored plan is not includible in income.

[97] Sec. 72(t).

distribution to the recipient plan or IRA within 60 days of receiving the distribution.[98] If the distribution from an employer-sponsored retirement plan consists of property, the rollover is accomplished by a transfer or contribution of the property to the recipient plan or IRA.

Investment of accounts under employer-sponsored plans

Qualified defined contribution plans, section 403(b) plans, and governmental section 457(b) plans commonly allow employees to direct the manner in which their accounts are invested. Employees may be given a choice among specified investment options, such as a choice of specified mutual funds, and, in some cases, may be able to direct the investment of their accounts in any product, instrument or investment offered in the market.

The investment options under a particular employer-sponsored retirement plan may change at times.[99] Similarly, a plan that allows employees to direct the investment of their accounts in any product, instrument or investment offered in the market may be amended to limit the investments that can be held in the plan. In these cases, employees may be required to change the investments held within their accounts without the option of receiving a distribution of the existing investment.

REASONS FOR CHANGE

The terms of some investments impose a charge or fee when the investment is liquidated, particularly if the investment is liquidated within a particular period after acquisition. For example, a lifetime income product, such as an annuity contract, may impose a surrender charge if the investment is discontinued. If an employee has to liquidate an investment held in an employer-sponsored retirement plan, for example, because of a change in investment options or a limit on investments held in the plan, the employee may be subject to such a charge or fee. Restrictions on in-service distributions may prevent the employee from avoiding such a charge or fee, and also from preserving the investment, through a distribution and rollover of the existing investment. The Committee wishes to allow distributions in such cases.

EXPLANATION OF PROVISION

Under the provision, if a lifetime income investment is no longer authorized to be held as an investment option under a qualified defined contribution plan, section 403(b) plan, or governmental section 457(b) plan, except as otherwise provided in guidance, the plan does not fail to satisfy the Code requirements applicable to the plan solely by reason of allowing (1) qualified distributions of a lifetime income investment, or (2) distributions of a lifetime income investment in the form of a qualified plan distribution annuity contract. Such a distribution must be made within the 90-day period ending

[98] Secs. 402(c), 402A(c)(3), 403(b)(8) and 457(e)(16).

[99] In the case of a plan subject to the Employee Retirement Income Security Act of 1974 ("ERISA"), a participant's exercise of control over the investment of the assets in his or her account by choosing among the investment options offered under the plan does not relieve a plan fiduciary from the duty to prudently select and monitor the investment options offered to participants. 29 C.F.R. sec. 2550.404c–1(d)(2)(iv) (2010); *Tibble v. Edison International,* No. 13–550, 135 S. Ct. 1823 (2015). The duty to monitor investment options may result in a change in the options offered.

on the date when the lifetime income investment is no longer authorized to be held as an investment option under the plan.

For purposes of the provision, a qualified distribution is a direct trustee-to-trustee transfer to another employer-sponsored retirement plan or IRA. A lifetime income investment is an investment option designed to provide an employee with election rights (1) that are not uniformly available with respect to other investment options under the plan and (2) that are to a lifetime income feature available through a contract or other arrangement offered under the plan (or under another employer-sponsored retirement plan or IRA through a direct trustee-to-trustee transfer to the other plan or IRA of the contract or other arrangement). A lifetime income feature is (1) a feature that guarantees a minimum level of income annually (or more frequently) for at least the remainder of the life of the employee or the joint lives of the employee and the employee's designated beneficiary, or (2) an annuity payable on behalf of the employee under which payments are made in substantially equal periodic payments (not less frequently than annually) over the life of the employee or the joint lives of the employee and the employee's designated beneficiary. Finally, a qualified plan distribution annuity contract is an annuity contract purchased for a participant and distributed to the participant by an employer-sponsored retirement plan.

EFFECTIVE DATE

The provision applies to plan years beginning after December 31, 2016.

M. TREATMENT OF CUSTODIAL ACCOUNTS ON TERMINATION OF SECTION 403(b) PLANS (SEC. 114 OF THE BILL AND SEC. 403(b) OF THE CODE)

PRESENT LAW

Tax-sheltered annuities (section 403(b) plans)

Section 403(b) plans are a form of tax-favored employer-sponsored plan that provide tax benefits similar to qualified retirement plans. Section 403(b) plans may be maintained only by (1) charitable tax-exempt organizations, and (2) educational institutions of State or local governments (that is, public schools, including colleges and universities). Many of the rules that apply to section 403(b) plans are similar to the rules applicable to qualified retirement plans, including section 401(k) plans. Employers may make nonelective or matching contributions to such plans on behalf of their employees, and the plan may provide for employees to make pre-tax elective deferrals, designated Roth contributions (held in designated Roth accounts)[100] or other after-tax contributions. Generally section 403(b) plans provide for contributions toward the purchase of annuity contracts or provide for contributions to be held in custodial accounts for each employee. In the case of contributions to custodial accounts under a section 403(b) plan, the amounts must be invested only in regulated investment company stock.[101] Contributions to a custodial account are not permitted to

[100] Sec. 402A.
[101] Sec. 403(b)(7).

be distributed before the employee dies, attains age 59½, has a severance from employment, or, in the case of elective deferrals, encounters financial hardship.

A section 403(b) plan is permitted to contain provisions for plan termination and that allow accumulated benefits to be distributed on termination.[102] In order for a plan termination to be effectuated, however, all plan assets must be distributed to participants.

Rollovers

A distribution from a section 403(b) plan that is an eligible rollover distribution may be rolled over to an eligible retirement plan (which include another 403(b) plan, a qualified retirement plan, and an IRA).[103] The rollover generally can be achieved by direct rollover (direct payment from the distributing plan to the recipient plan) or by contributing the distribution to the eligible retirement plan within 60 days of receiving the distribution ("60-day rollover").[104] Amounts that are rolled over are usually not included in gross income. Generally, a distribution of any portion of the balance to the credit of a participant is an eligible rollover distribution with exceptions, for example, certain periodic payments, required minimum distributions, and hardship distributions.[105]

Roth conversions

Distributions from section 403(b) plans may be rolled into a Roth IRA.[106] Distributions from these plans that are rolled over into a Roth IRA and that are not distributions from a designated Roth account must be included in gross income. Further, a section 403(b) plan that allows employees to make designated Roth contributions may also allow employees to elect to transfer amounts held in accounts that are not designated Roth accounts into designated Roth accounts, but the amount transferred must be included in income as though it were distributed.[107]

Approved nonbank trustees required for IRAs

An IRA can be a trust, a custodial account, or an annuity contract. The Code requires that the trustee or custodian of an IRA be a bank (which is generally subject to Federal or State supervision) or an IRS approved nonbank trustee, that an annuity contract be issued by an insurance company (which is subject to State supervision), and that an IRA trust or custodial account be created and organized in the United States.

In order for a trustee or custodian that is not a bank to be an IRA trustee or custodian, the entity must apply to the IRS for approval. Treasury Regulations list a number of factors that are

[102] Treas. Reg. sec. 1.403(b)–10(a).
[103] Sec. 403(b)(8). Similar rules apply to distributions from qualified retirement plans and governmental section 457(b) plans.
[104] Under section 402(c)(11), any distribution to a beneficiary other than the participant's surviving spouse is only permitted to be rolled over to an IRA using a direct rollover; 60-day rollovers are not available to nonspouse beneficiaries.
[105] Sec. 402(c)(4). Treas. Reg. sec. 1.402(c)–1 identifies certain other payments that are not eligible for rollover, including, for example, certain corrective distributions, loans that are treated as deemed distributions under section 72(p), and dividends on employer securities as described in section 404(k).
[106] Sec. 408A(d)(3). Similar rules apply to qualified retirement plans and governmental section 457(b) plans.
[107] Sec. 402A(d)(4). Similar rules apply to qualified retirement plans and governmental section 457(b) plans.

taken into account in approving an applicant to be a nonbank trustee.[108] The applicant must demonstrate fiduciary ability (ability to act within accepted rules of fiduciary conduct including continuity and diversity of ownership), capacity to account (experience and competence with other activities normally associated with handling of retirement funds), and ability to satisfy other rules of fiduciary conduct which includes a net worth requirement. Because it is an objective requirement that may be difficult for some applicants to satisfy, the net worth requirement is the most significant of the requirements for nonbank trustees.

To be approved, the entity must have a net worth of at least $250,000 at the time of the application. There is a maintenance rule that varies depending on whether the trustee is an active trustee or a passive trustee and that includes minimum dollar amounts and minimum amounts as a percentage of assets held in fiduciary accounts. A special rule is provided for nonbank trustees that are members of the Security Investor Protection Corporation ("SIPC").

REASONS FOR CHANGE

In general, assets of section 403(b) plans can be invested only in annuity contracts or mutual funds. Unlike most qualified defined contribution plans, under which assets are held in a trust, historically, assets associated with section 403(b) plans have often consisted of annuity contracts issued in the name of the particular participant or mutual funds held in a custodial account in the participant's name. In many cases, this prevents an employer from distributing these assets in order to effectuate a plan termination. The Committee wishes to provide a mechanism under which the plan termination may proceed while keeping assets that cannot otherwise be distributed in a tax-favored retirement savings vehicle.

EXPLANATION OF PROVISION

Under the provision, if an employer terminates a section 403(b) plan under which amounts are contributed to custodial accounts, and the person holding the assets of the accounts is an IRS approved nonbank trustee, then, as of the date of the termination, the custodial accounts are deemed to be IRAs. Only a custodial account under a section 403(b) plan that is a designated Roth account is treated as a Roth IRA upon termination of the section 403(b) plan.

EFFECTIVE DATE

The provision applies to plan terminations occurring after December 31, 2016.

N. CLARIFICATION OF RETIREMENT INCOME ACCOUNT RULES RELATING TO CHURCH-CONTROLLED ORGANIZATIONS (SEC. 115 OF THE BILL AND SEC. 403(b)(9) OF THE CODE)

PRESENT LAW

Assets of a tax-sheltered annuity plan ("section 403(b)" plan), generally must be invested in annuity contracts or mutual

[108] Treas. Reg. sec. 1.408–2(e).

funds.[109] However, the restrictions on investments do not apply to a retirement income account, which is a defined contribution program established or maintained by a church, or a convention or association of churches, to provide benefits under the plan to employees of a religious, charitable or similar tax-exempt organization.[110]

Certain rules prohibiting discrimination in favor of highly compensated employees, which apply to section 403(b) plans generally, do not apply to a plan maintained by a church or qualified church-controlled organization.[111] For this purpose, church means a church, a convention or association of churches, or an elementary or secondary school that is controlled, operated, or principally supported by a church or by a convention or association of churches, and includes a qualified church-controlled organization. A qualified church-controlled organization is any church-controlled tax-exempt organization other than an organization that (1) offers goods, services, or facilities for sale, other than on an incidental basis, to the general public, other than goods, services, or facilities that are sold at a nominal charge substantially less than the cost of providing the goods, services, or facilities, and (2) normally receives more than 25 percent of its support from either governmental sources, or receipts from admissions, sales of merchandise, performance of services, or furnishing of facilities, in activities that are not unrelated trades or businesses, or from both. Church-controlled organizations that are not qualified church-controlled organizations are generally referred to as "nonqualified church-controlled organizations."

In recent years, a question has arisen as to whether employees of nonqualified church-controlled organizations may be covered under a section 403(b) plan that consists of a retirement income account.

REASONS FOR CHANGE

The Committee wishes to clarify the individuals who may be covered by a retirement income account.

EXPLANATION OF PROVISION

The provision clarifies that a retirement income account may cover a duly ordained, commissioned, or licensed minister of a church in the exercise of his ministry, regardless of the source of his compensation; an employee of a tax-exempt organization, whether a civil law corporation or otherwise, that is controlled by or associated with a church or a convention or association of churches; and certain employees after separation from service with a church, a convention or association of churches, or an organization described above.[112]

[109] Sec. 403(b)(1)(A) and (7).
[110] Sec. 403(b)(9)(B), referring to organizations exempt from tax under section 501(c)(3). For this purpose, a church or a convention or association of churches includes an organization described in section 414(e)(3)(A), that is, an organization, the principal purpose or function of which is the administration or funding of a plan or program for the provision of retirement benefits or welfare benefits, or both, for the employees of a church or a convention or association of churches, provided that the organization is controlled by or associated with a church or a convention or association of churches.
[111] Sec. 403(b)(1)(D) and (12).
[112] These individuals are described in section 414(e)(3)(B).

EFFECTIVE DATE

The provision applies to years beginning before, on, or after the date of enactment of the provision.

TITLE II—ADMINISTRATIVE IMPROVEMENTS

A. PLAN ADOPTED BY FILING DUE DATE FOR YEAR MAY BE TREATED AS IN EFFECT AS OF CLOSE OF YEAR (SEC. 201 OF THE BILL AND SEC. 401(b) OF THE CODE)

PRESENT LAW

In order for a qualified retirement plan to be treated as maintained for a taxable year, the plan must be adopted by the last day of the taxable year.[113] However, the trust under the plan will not fail to be treated as in existence due to lack of corpus merely because it holds no assets on the last day of the taxable year.[114] Contributions made by the due date (plus extensions) of the tax return for the employer maintaining the plan for a taxable year are treated as contributed on account of that taxable year.[115] Thus a plan can be established on the last day of a taxable year even though the first contribution is not made until the due date of the employer's taxable year. Further, if the terms of a plan adopted during an employer's taxable year fail to satisfy the qualification requirements that apply to the plan for the year, the plan may also be amended retroactively by the due date (including extensions) of the employer's return, provided that the amendment is made retroactively effective.[116] However, this provision does not allow a plan to be adopted after the end of a taxable year and made retroactively effective, for qualification purposes, for the taxable year prior to the taxable year in which the plan was adopted by the employer.[117]

REASONS FOR CHANGE

An employer, particularly a small employer, might not know until after the end of a taxable year (the "preceding year") that its profits for the preceding year are sufficient to support the expenses and contributions associated with the establishment of a retirement plan. However, under present law, a plan established at that time can be effective only for the current year, not for the preceding year. The Committee believes that allowing a plan to be effective for the preceding year provides the opportunity for employees to receive contributions for that earlier year and begin to accumulate retirement savings.

EXPLANATION OF PROVISION

Under the provision, if an employer adopts a qualified retirement plan after the close of a taxable year but before the time prescribed by law for filing the return of the employer for the taxable year (including extensions thereof), the employer may elect to treat the plan as having been adopted as of the last day of the taxable year.

[113] Rev. Rul. 76–28; 1976–1 C.B. 106.
[114] Rev. Rul. 81–114; 1981–1 C.B. 207.
[115] Sec. 404(a)(6).
[116] Sec. 401(b).
[117] Treas. Reg. sec. 1.401(b)–1(a).

The provision does not override rules requiring certain plan provisions to be in effect during a plan year, such as the provision for elective deferrals under a qualified cash or deferral arrangement ("generally referred to as a 401(k) plan").[118]

EFFECTIVE DATE

The provision applies to plans adopted for taxable years beginning after December 31, 2016.

B. COMBINED ANNUAL REPORT FOR GROUP OF PLANS (SEC. 202 OF THE BILL, SEC. 6058 OF THE CODE, AND SEC. 104 OF ERISA)

PRESENT LAW

Under the Code, an employer maintaining a qualified retirement plan generally is required to file an annual return containing information required under regulations with respect to the qualification, financial condition, and operation of the plan.[119] ERISA requires the plan administrator of certain pension and welfare benefit plans to file annual reports disclosing certain information to the Department of Labor ("DOL").[120] These filing requirements are met by filing a completed Form 5500, Annual Return/Report of Employee Benefit Plan. Forms 5500 are filed with DOL, and information from Forms 5500 is shared with the IRS.[121] A separate Form 5500 is required for each plan.[122]

REASONS FOR CHANGE

Forms 5500 provide valuable information about plans to plan participants, administrative agencies, and the public, including researchers. However, the preparation of Form 5500 also involves administrative costs that increase plan expenses. The Committee believes that, in the case of identical plans (that is, plans with the same plan year, trustee, administrator and investments) maintained by unrelated employers, permitting a single Form 5500, containing information specific to each plan, rather than requiring a separate Form 5500 for each plan as under present law, can reduce aggregate administrative costs, making it easier for small employers to sponsor a retirement plan and thus improving retirement savings.

[118] Treas. Reg. sec. 1.401(k)–1(e)(2)(ii).

[119] Sec. 6058. In addition, under section 6059, the plan administrator of a defined benefit plan subject to the minimum funding requirements is required to file an annual actuarial report. Under Code section 414(g) and ERISA section 3(16), plan administrator generally means the person specifically so designated by the terms of the plan document. In the absence of a designation, the plan administrator generally is (1) in the case of a plan maintained by a single employer, the employer, (2) in the case of a plan maintained by an employee organization, the employee organization, or (3) in the case of a plan maintained by two or more employers or jointly by one or more employers and one or more employee organizations, the association, committee, joint board of trustees, or other similar group of representatives of the parties that maintain the plan. Under ERISA, the party described in (1), (2) or (3) is referred to as the "plan sponsor."

[120] ERISA secs. 103 and 104. Under ERISA section 4065, the plan administrator of certain defined benefit plans must provide information to the PBGC.

[121] Information is shared also with the PBGC, as applicable. Form 5500 filings are also publicly released in accordance with section 6104(b) and Treas. Reg. sec. 301.6104(b)–1 and ERISA secs. 104(a)(1) and 106(a).

[122] Under section 6011(a) and (e), the IRS is required to provide standards for electronically filed returns, but may not require a person to file a return electronically unless the person is required to file at least 250 returns during the calendar year ("250 return threshold for electronic filing"). Under Treas. Reg. sec. 301.6058–2, Form 5500 for a plan year must be filed electronically if the filer is required to file at least 250 tax returns (including information returns) during the calendar year that includes the first day of the plan year.

EXPLANATION OF PROVISION

The provision directs the IRS and DOL to work together to modify Form 5500 so that all members of a group of plans described below may file a single consolidated Form 5500. In developing the consolidated Form 5500, IRS and DOL may require it to include all information for each plan in the group as IRS and DOL determine is necessary or appropriate for the enforcement and administration of the Code and ERISA.[123]

For purposes of the provision, a group of plans is eligible for a consolidated Form 5500 if all the plans in the group (1) are defined contribution plans, (2) have the same trustee, the same named fiduciary (or named fiduciaries) under ERISA, and the same administrator, (3) use the same plan year, and (4) provide the same investments or investment options to participants and beneficiaries. A plan not subject to ERISA may be included in the group if the same person that performs each of the previous functions, as applicable, for all the other plans in the group performs each of the functions for the plan not subject to ERISA.

EFFECTIVE DATE

The consolidated Form 5500 is to be implemented not later than January 1, 2020, and shall be effective for returns and reports for plan years beginning after December 31, 2019.

C. DISCLOSURE REGARDING LIFETIME INCOME (SEC. 203 OF THE BILL AND SEC. 105 OF ERISA)

PRESENT LAW

ERISA requires the administrator of a defined contribution plan to provide benefit statements to participants.[124] In the case of a participant who has the right to direct the investment of the assets in his or her account, a benefit statement must be provided at least quarterly. Benefit statements must be provided at least annually to other participants.

Among other items, a benefit statement provided with respect to a defined contribution plan generally must include (1) the participant's total benefits accrued, that is, the participant's account balance, (2) the vested portion of the account balance or the earliest date on which the account balance will become vested, and (3) the value of each investment to which assets in the participant's account are allocated. A quarterly benefit statement provided to a participant who has the right to direct investments must provide additional information, including information relating to investment principles.

In May 2013, the Department of Labor issued an advance notice of proposed rulemaking providing rules under which a benefit provided to a defined contribution plan participant would include an estimated lifetime income stream of payments based on the participant's account balance.[125] However, information about lifetime in-

[123] Under the provision, for purposes of applying the 250 return threshold for electronic filing to Forms 5500 for plan years beginning after December 31, 2016, information regarding each plan for which information is provided on the Form 5500 is treated as a separate return.

[124] ERISA sec. 105. Benefits statements are required also with respect to defined benefit plans. A civil penalty may apply for a failure to provide a required benefit statement.

[125] 78 Fed. Reg. 26727 (May 8, 2013).

come that might be provided by funds in a defined contribution plan is not currently required to be included in a benefit statement.

REASONS FOR CHANGE

Retirees are generally eligible for annuity benefits under the Social Security system, but, for many retirees, additional income that will last for life is needed. Defined contribution plans provide a valuable source of retirement savings, but generally, unlike defined benefit plans, do not offer benefits in the form of annuities or other distribution forms that provide lifetime income. In addition, most plan participants do not understand how to correlate the funds in a defined contribute plan account with an annuity or other lifetime income form. The Committee wishes to require information on equivalent lifetime income to be included in benefit statements with respect to defined contribution plan accounts, in a manner that is both useful to participants and practicable for plan administrators.

EXPLANATION OF PROVISION

The provision requires a benefit statement provided to a defined contribution plan participant to include a lifetime income disclosure as described in the provision. However, the lifetime income disclosure is required to be included in only one benefit statement during any 12-month period.

A lifetime income disclosure is required to set forth the lifetime income stream equivalent of the participant's total account balance under the plan. The lifetime income stream equivalent to the account balance is the amount of monthly payments the participant would receive if the total account balance were used to provide lifetime income streams, based on assumptions specified in guidance prescribed by the Secretary of Labor (referred to as the "Secretary" in this explanation). The required lifetime income streams are (1) a qualified joint and survivor annuity for the participant and the participant's surviving spouse, based on assumptions specified in guidance, including the assumption that the participant has a spouse of equal age, and (2) a single life annuity. The lifetime income streams may have a term certain or other features to the extent permitted under guidance.

The Secretary is directed to issue, not later than a year after the provision is enacted, a model lifetime income disclosure, written in a manner to be understood by the average plan participant. The model must include provisions to (1) explain that the lifetime income stream equivalent is only provided as an illustration, (2) explains that the actual payments under the lifetime income stream that may be purchased with the account balance will depend on numerous factors and may vary substantially from the lifetime income stream equivalent in the disclosure, (3) explain the assumptions on which the lifetime income stream equivalent is determined, and (4) provides other similar explanations as the Secretary considers appropriate.

In addition, the Secretary is directed, not later than a year after the provision is enacted, (1) to prescribe assumptions that defined contribution plan administrators may use in converting account balances into lifetime income stream equivalents, and (2) issue interim final rules under the provision. In prescribing assumptions, the Secretary may prescribe a single set of specific assumptions (in which case the Secretary may issue tables or factors that facilitate conversions of account balances) or ranges of permissible assumptions. To the extent that an account balance is or may be invested in a lifetime income stream, the prescribed assumptions are to allow, to the extent appropriate, plan administrators to use the amounts payable under the lifetime income stream as a lifetime income stream equivalent.

Under the provision, no plan fiduciary, plan sponsor, or other person has any liability under ERISA solely by reason of the provision of lifetime income stream equivalents that are derived in accordance with the assumptions and guidance under the provision and that include the explanations contained in model disclosure. This protection applies without regard to whether the lifetime income stream equivalent is required to be provided.

EFFECTIVE DATE

The requirement to provide a lifetime income disclosure applies with respect to benefit statements provided more than 12 months after the latest of the issuance by the Secretary of (1) interim final rules, (2) the model disclosure, or (3) prescribed assumptions.

D. FIDUCIARY SAFE HARBOR FOR SELECTION OF LIFETIME INCOME PROVIDER (SEC. 204 OF THE BILL AND SEC. 404 OF ERISA)

PRESENT LAW

ERISA imposes certain standards of care with respect to the actions of a plan fiduciary. Specifically, a fiduciary is required to discharge its duties with respect to the plan solely in the interest of the participants and beneficiaries, for the exclusive purpose of providing benefits to participants and beneficiaries and defraying reasonable administration expenses of the plan, with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with relevant matters would use in the conduct of an enterprise of a like character and with like aims (the "prudent man" requirement), by diversifying plan investments so as to minimize the risk of large losses unless, under the circumstances, it is clearly prudent not to do so, and in accordance with plan documents and governing instruments insofar as the documents and instruments are consistent with ERISA.

Department of Labor regulations provide a safe harbor for a fiduciary to satisfy the prudent man requirement in selecting an annuity provider and a contract for benefit distributions from a defined contribution plan.[126]

REASONS FOR CHANGE

Unlike defined benefit plans, defined contribution plans generally do not offer benefits in the form of annuities or other distribution forms that provide lifetime income, which, under a defined contribution plan, generally must be provided through a contract issued by an insurance company. In the case of a defined contribution plan subject to ERISA, the selection of a lifetime income pro-

[126] 29 C.F.R. sec. 2550.404a–4.

vider (such as an insurance company) is a fiduciary act. Uncertainty about the applicable fiduciary standard may discourage plan sponsors and administrators from offering lifetime income benefit options under a defined contribution plan.

EXPLANATION OF PROVISION

The provision specifies measures that a plan fiduciary may take with respect to the selection of an insurer and a guaranteed retirement income contract in order to assure that the fiduciary meets the prudent man requirement. The measures under the provision are an optional means by which a fiduciary will be considered to satisfy the prudent man requirement with respect to the selection of insurers and guaranteed retirement income contracts and do not establish minimum requirements or the exclusive means for satisfying the prudent man requirement.

For purposes of the provision, an insurer is an insurance company, insurance service or insurance organization qualified to do business in a State and includes affiliates of those entities to the extent the affiliate is licensed to offer guaranteed retirement income contracts. A guaranteed retirement income contract is an annuity contract for a fixed term or a contract (or provision or feature thereof) designed to provide a participant guaranteed benefits annually (or more frequently) for at least the remainder of the life of the participant or joint lives of the participant and the participant's designated beneficiary as part of a defined contribution plan.

With respect to the selection of an insurer and a guaranteed retirement income contract (as defined below), the prudent man requirement will be deemed met if a fiduciary—

- engages in an objective, thorough and analytical search for the purpose of identifying insurers from which to purchase guaranteed retirement income contracts,
- with respect to each insurer identified through the search, considers the financial capability of the insurer to satisfy its obligations under the guaranteed retirement income contract and considers the cost (including fees and commissions) of the guaranteed retirement income contract offered by the insurer in relation to the benefits and product features of the contract and administrative services to be provided under the contract, and
- on the basis of the foregoing, concludes that, at the time of the selection (as described below), the insurer is financially capable of satisfying its obligations under the guaranteed retirement income contract and that the cost (including fees and commissions) of the selected guaranteed retirement income contract is reasonable in relation to the benefits and product features of the contract and the administrative services to be provided under the contract.

A fiduciary will be deemed to satisfy the requirements above with respect to the financial capability of the insurer if—

- the fiduciary obtains written representations from the insurer that it is licensed to offer guaranteed retirement income contracts; that the insurer, at the time of selection and for each of the immediately preceding seven years operates under a certificate of authority from the Insurance Commissioner of its domiciliary State that has not been revoked or suspended, has filed audited financial statements in accordance with the laws of its domiciliary State under applicable statutory accounting principles, maintains (and has maintained) reserves that satisfy all the statutory requirements of all States where the insurer does business, and is not operating under an order of supervision, rehabilitation, or liquidation; and that the insurer undergoes, at least every five years, a financial examination (within the meaning of the law of its domiciliary State) by the Insurance Commissioner of the domiciliary State (or representative, designee, or other party approved thereby);

- in the case that, following the issuance of the insurer representations described above, there is any change that would preclude the insurer from making the same representations at the time of issuance of the guaranteed retirement income contract, the insurer is required to notify the fiduciary, in advance of the issuance of any guaranteed retirement income contract, that the fiduciary can no longer rely on one or more of the representations; and
- the fiduciary has not received such a notification and has no other facts that would cause it to question the insurer representations.

The provision specifies that nothing in these requirements is to be construed to require a fiduciary to select the lowest cost contract. Accordingly, a fiduciary may consider the value, including features and benefits of the contract and attributes of the insurer in conjunction with the contract's cost. For this purpose, attributes of the insurer that may be considered include, without limitation, the issuer's financial strength.

For purposes of the provision, the time of selection may be either the time that the insurer and contract are selected for distribution of benefits to a specific participant or beneficiary or the time that the insurer and contract are selected to provide benefits at future dates to participants or beneficiaries, provided that the selecting fiduciary periodically reviews the continuing appropriateness of its conclusions with respect to the insurer's financial capability and cost, taking into account the considerations described above.[127] A fiduciary will be deemed to have conducted a periodic review of the financial capability of the insurer if the fiduciary obtains the written representations described above on an annual basis unless, in the interim, the fiduciary has received notification from the insurer that representations cannot be relied on or the fiduciary otherwise becomes aware of facts that would cause it to question the representations.

A fiduciary that satisfies the requirements of the provision is not liable following the distribution of any benefit, or the investment by or on behalf of a participant or beneficiary pursuant to the selected guaranteed retirement income contract, for any losses that may result to the participant or beneficiary due to an insurer's inability to satisfy its financial obligations under the terms of the contract.

[127] However, a fiduciary is not required to review the appropriateness of its conclusions following the purchase of any contract or contracts for specific participants or beneficiaries.

EFFECTIVE DATE

The provision is effective on the date of enactment.

E. Modification of Nondiscrimination Rules to Protect Older, Longer Service Participation (sec. 205 of the bill and sec. 401(a)(4) of the Code)

PRESENT LAW

In general

Qualified retirement plans are subject to nondiscrimination requirements, under which the group of employees covered by a plan ("plan coverage") and the contributions or benefits provided to employees, including benefits, rights, and features under the plan, must not discriminate in favor of highly compensated employees.[128] The timing of plan amendments must also not have the effect of discriminating significantly in favor of highly compensated employees. In addition, in the case of a defined benefit plan, the plan must benefit at least the lesser of (1) 50 employees and (2) the greater of 40 percent of all employees and two employees (or one employee if the employer has only one employee), referred to as the "minimum participation" requirements.[129] These nondiscrimination requirements are designed to help ensure that qualified retirement plans achieve the goal of retirement security for both lower and higher paid employees.

For nondiscrimination purposes, an employee generally is treated as highly compensated if the employee (1) was a five-percent owner of the employer at any time during the year or the preceding year, or (2) had compensation for the preceding year in excess of $120,000 (for 2016).[130] Employees who are not highly compensated are referred to as nonhighly compensated employees.

Nondiscriminatory plan coverage

Whether plan coverage of employees is nondiscriminatory is determined by calculating a plan's ratio percentage, that is, the ratio of the percentage of nonhighly compensated employees covered under the plan to the percentage of highly compensated employees covered. For this purpose, certain portions of a defined contribution plan are treated as separate plans to which the plan coverage requirements are applied separately, referred to as mandatory disaggregation. Specifically, the following, if provided under a plan, are treated as separate plans: the portion of a plan consisting of employee elective deferrals, the portion consisting of employer matching contributions, the portion consisting of employer nonelective contributions, and the portion consisting of an employee stock

[128] Secs. 401(a)(3)–(5) and 410(b). Detailed rules are provided in Treas. Reg. secs. 1.401(a)(4)–1 through –13 and secs. 1.410(b)–2 through –10. In applying the nondiscrimination requirements, certain employees, such as those under age 21 or with less than a year of service, generally may be disregarded. In addition, employees of controlled groups and affiliated service groups under the aggregation rules of section 414(b), (c), (m) and (o) are treated as employed by a single employer.

[129] Sec. 401(a)(26).

[130] Section 414(q). At the election of the employer, employees who are highly compensated based on the amount of their compensation may be limited to employees who were among the top 20 percent of employees based on compensation.

ownership plan ("ESOP").[131] Subject to mandatory disaggregation, different qualified retirement plans may otherwise be aggregated and tested together as a single plan, provided that they use the same plan year. The plan determined under these rules for plan coverage purposes generally is also treated as the plan for purposes of applying the other nondiscrimination requirements.

A plan's coverage is nondiscriminatory if the ratio percentage, as determined above, is 70 percent or greater. If a plan's ratio percentage is less than 70 percent, a multi-part test applies, referred to as the average benefit test. First, the plan must meet a "nondiscriminatory classification requirement," that is, it must cover a group of employees that is reasonable and established under objective business criteria and the plan's ratio percentage must be at or above a level specified in the regulations, which varies depending on the percentage of nonhighly compensated employees in the employer's workforce. In addition, the average benefit percentage test must be satisfied.

Under the average benefit percentage test, in general, the average rate of employer–provided contributions or benefit accruals for all nonhighly compensated employees under all plans of the employer must be at least 70 percent of the average contribution or accrual rate of all highly compensated employees.[132] In applying the average benefit percentage test, elective deferrals made by employees, as well as employer matching and nonelective contributions, are taken into account. Generally, all plans maintained by the employer are taken into account, including ESOPs, regardless of whether plans use the same plan year.

Under a transition rule applicable in the case of the acquisition or disposition of a business, or portion of a business, or a similar transaction, a plan that satisfied the plan coverage requirements before the transaction is deemed to continue to satisfy them for a period after the transaction, provided coverage under the plan is not significantly changed during that period.[133]

Nondiscriminatory contributions or benefit accruals

In general

There are three general approaches to testing the amount of benefits under qualified retirement plans: (1) design-based safe harbors under which the plan's contribution or benefit accrual formula

[131] Elective deferrals are contributions that an employee elects to have made to a defined contribution plan that includes a qualified cash or deferred arrangement (referred to as "section 401(k) plan") rather than receive the same amount as current compensation. Employer matching contributions are contributions made by an employer only if an employee makes elective deferrals or after-tax employee contributions. Employer nonelective contributions are contributions made by an employer regardless of whether an employee makes elective deferrals or after-tax employee contributions. Under section 4975(e)(7), an ESOP is a defined contribution plan, or portion of a defined contribution plan, that is designated as an ESOP and is designed to invest primarily in employer stock.

[132] Contribution and benefit rates are generally determined under the rules for nondiscriminatory contributions or benefit accruals, described below. These rules are generally based on benefit accruals under a defined benefit plan, other than accruals attributable to after-tax employee contributions, and contributions allocated to participants' accounts under a defined contribution plan, other than allocations attributable to after-tax employee contributions. (Under these rules, contributions allocated to a participants accounts are referred to as "allocations," with the related rates referred to as "allocation rates," but "contribution rates" is used herein for convenience.) However, as discussed below, benefit accruals can be converted to actuarially equivalent contributions, and contributions can be converted to actuarially equivalent benefit accruals.

[133] Sec. 410(b)(6)(C).

satisfies certain uniformity standards, (2) a general test, described below, and (3) cross-testing of equivalent contributions or benefit accruals. Employee elective deferrals and employer matching contributions under defined contribution plans are subject to special testing rules and generally are not permitted to be taken into account in determining whether other contributions or benefits are nondiscriminatory.[134]

The nondiscrimination rules allow contributions and benefit accruals to be provided to highly compensated and nonhighly compensated employees at the same percentage of compensation.[135] Thus, the various testing approaches described below are generally applied to the amount of contributions or accruals provided as a percentage of compensation, referred to as a contribution rate or accrual rate. In addition, under the "permitted disparity" rules, in calculating an employee's contribution or accrual rate, credit may be given for the employer paid portion of Social Security taxes or benefits.[136] The permitted disparity rules do not apply in testing whether elective deferrals, matching contributions, or ESOP contributions are nondiscriminatory.

The general test is generally satisfied by measuring the rate of contribution or benefit accrual for each highly compensated employee to determine if the group of employees with the same or higher rate (a "rate" group) is a nondiscriminatory group, using the nondiscriminatory plan coverage standards described above. For this purpose, if the ratio percentage of a rate group is less than 70 percent, a simplified standard applies, which includes disregarding the reasonable classification requirement, but requires satisfaction of the average benefit percentage test.

Cross-testing

Cross-testing involves the conversion of contributions under a defined contribution plan or benefit accruals under a defined benefit plan to actuarially equivalent accruals or contributions, with the resulting equivalencies tested under the general test. However, employee elective deferrals and employer matching contributions under defined contribution plans are not permitted to be taken into account for this purpose, and cross-testing of contributions under a defined contribution plan, or cross-testing of a defined contribution plan aggregated with a defined benefit plan, is permitted only if certain threshold requirements are satisfied.

In order for a defined contribution plan to be tested on an equivalent benefit accrual basis, one of the following three threshold conditions must be met:

- The plan has broadly available allocation rates, that is, each allocation rate under the plan is available to a nondiscriminatory group of employees (disregarding certain permitted additional contributions provided to employees as a replacement for benefits under a frozen defined benefit plan, as discussed below);

[134] Secs. 401(k) and (m), the latter of which applies also to after-tax employee contributions under a defined contribution plan.

[135] For this purpose, under section 401(a)(17), compensation generally is limited to $265,000 per year (for 2016).

[136] See sections 401(a)(5)(C) and (D) and 401 (l) and Treas. Reg. section 1. 401(a)(4)–7 and 1.401(l)–1 through –6 for rules for determining the amount of contributions or benefits that can be attributed to the employer-paid portion of Social Security taxes or benefits.

- The plan provides allocations that meet prescribed designs under which allocations gradually increase with age or service or are expected to provide a target level of annuity benefit; or
- The plan satisfies a minimum allocation gateway, under which each nonhighly compensated employee has an allocation rate of (a) at least one-third of the highest rate for any highly compensated employee, or (b) if less, at least five percent.

In order for an aggregated defined contribution and defined benefit plan to be tested on an aggregate equivalent benefit accrual basis, one of the following three threshold conditions must be met:

- The plan must be primarily defined benefit in character, that is, for more than fifty percent of the nonhighly compensated employees under the plan, their accrual rate under the defined benefit plan exceeds their equivalent accrual rate under the defined contribution plan;
- The plan consists of broadly available separate defined benefit and defined contribution plans, that is, the defined benefit plan and the defined contribution plan would separately satisfy simplified versions of the minimum coverage and nondiscriminatory amount requirements; or
- The plan satisfies a minimum aggregate allocation gateway, under which each nonhighly compensated employee has an aggregate allocation rate (consisting of allocations under the defined contribution plan and equivalent allocations under the defined benefit plan) of (a) at least one-third of the highest aggregate allocation rate for any nonhighly compensated employee, or (b) if less, at least five percent in the case of a highest nonhighly compensated employee's rate up to 25 percent, increased by one percentage point for each five-percentage-point increment (or portion thereof) above 25 percent, subject to a maximum of 7.5 percent.

Benefits, rights, and features

Each benefit, right, or feature offered under the plan generally must be available to a group of employees that has a ratio percentage that satisfies the minimum coverage requirements, including the reasonable classification requirement if applicable, except that the average benefit percentage test does not have to be met, even if the ratio percentage is less than 70 percent.

Multiple-employer and section 403(b) plans

A multiple-employer plan generally is a single plan maintained by two or more unrelated employers, that is, employers that are not treated as a single employer under the aggregation rules for related entities.[137] The plan coverage and other nondiscrimination requirements are applied separately to the portions of a multiple-employer plan covering employees of different employers.[138]

[137] Sec. 413(c). Multiple-employer status does not apply if the plan is a multi-employer plan, defined under sec. 414(f) as a plan maintained pursuant to one or more collective bargaining agreements with two or more unrelated employers and to which the employers are required to contribute under the collective bargaining agreement(s). Multi-employer plans are also known as Taft-Hartley plans.

[138] Treas. Reg. sec. 1.413–2(a)(3)(ii)–(iii).

Certain tax-exempt charitable organizations may offer their employees a tax-deferred annuity plan ("section 403(b) plan).[139] The nondiscrimination requirements, other than the requirements applicable to elective deferrals, generally apply to section 403(b) plans of private tax-exempt organizations. For purposes of applying the nondiscrimination requirements to a section 403(b) plan, subject to mandatory disaggregation, a qualified retirement plan may be combined with the section 403(b) plan and treated as a single plan.[140] However, a section 403(b) plan and qualified retirement plan may not be treated as a single plan for purposes of applying the nondiscrimination requirements to the qualified retirement plan.

Closed and frozen defined benefit plans

A defined benefit plan may be amended to limit participation in the plan to individuals who are employees as of a certain date. That is, employees hired after that date are not eligible to participate in the plan. Such a plan is sometimes referred to as a "closed" defined benefit plan (that is, closed to new entrants). In such a case, it is common for the employer also to maintain a defined contribution plan and to provide employer matching or nonelective contributions only to employees not covered by the defined benefit plan or at a higher rate to such employees.

Over time, the group of employees continuing to accrue benefits under the defined benefit plan may come to consist more heavily of highly compensated employees, for example, because of greater turnover among nonhighly compensated employees or because increasing compensation causes nonhighly compensated employees to become highly compensated. In that case, the defined benefit plan may have to be combined with the defined contribution plan and tested on a benefit accrual basis. However, under the regulations, if none of the threshold conditions is met, testing on a benefits basis may not be available. Notwithstanding the regulations, recent IRS guidance provides relief for a limited period, allowing certain closed defined benefit plans to be aggregated with a defined contribution plan and tested on an aggregate equivalent benefits basis without meeting any of the threshold conditions.[141] When the group of employees continuing to accrue benefits under a closed defined benefit plan consists more heavily of highly compensated employees, the benefits, rights, and features provided under the plan may also fail the tests under the existing nondiscrimination rules.

In some cases, if a defined benefit plan is amended to cease future accruals for all participants, referred to as a "frozen" defined benefit plan, additional contributions to a defined contribution plan may be provided for participants, in particular for older participants, in order to make up in part for the loss of the benefits they expected to earn under the defined benefit plan ("make-whole" contributions). As a practical matter, testing on a benefit accrual basis may be required in that case, but may not be available because the defined contribution plan does not meet any of the threshold conditions.

[139] Sec. 403(b). These plans are available to employers that are tax-exempt under section 501(c)(3), as well as to educational institutions of State or local governments.

[140] Treas. Reg. sec. 1.410(b)–7(f).

[141] Notice 2014–5, 2014–2 I.R.B. 276, extended by Notice 2016–57 (released September 19, 2016). Proposed regulations revising the nondiscrimination requirements for closed plans were also issued earlier this year, subject to various conditions. 81 Fed. Reg. 4976 (January 29, 2016).

REASONS FOR CHANGE

Some employers sponsoring defined benefit plans have determined that it is no longer feasible financially to continue the plans in their current form and have therefore closed their plans to new entrants. Existing employees continue to earn benefits under the plan, consistent with their expectations as to retirement income, which is particularly important for employees close to retirement. However, without greater flexibility in the nondiscrimination rules, employers may be forced to freeze their defined benefit plans, thus preventing employees from earning their expected benefits. When a defined benefit plan is frozen, make-whole contributions can offset some of the resulting benefit loss for employees. However, in that case, too, greater flexibility in the nondiscrimination rules is needed. The Committee wishes to provide such flexibility in order to protect benefits for older, longer-service employees.

EXPLANATION OF PROVISION

Closed or frozen defined benefit plans

In general

The provision provides nondiscrimination relief with respect to benefits, rights, and features for a closed class of participants ("closed class"),[142] and with respect to benefit accruals for a closed class, under a defined benefit plan that meets the requirements described below (referred to herein as an "applicable" defined benefit plan). In addition, the provision treats a closed or frozen applicable defined benefit plan as meeting the minimum participation requirements if the plan met the requirements as of the effective date of the plan amendment by which the plan was closed or frozen.

If a portion of an applicable defined benefit plan eligible for relief under the provision is spun off to another employer, and if the spun-off plan continues to satisfy any ongoing requirements applicable for the relevant relief as described below, the relevant relief for the spun-off plan will continue with respect to the other employer.

Benefits, rights, or features for a closed class

Under the provision, an applicable defined benefit plan that provides benefits, rights, or features to a closed class does not fail the nondiscrimination requirements by reason of the composition of the closed class, or the benefits, rights, or features provided to the closed class, if (1) for the plan year as of which the class closes and the two succeeding plan years, the benefits, rights, and features satisfy the nondiscrimination requirements without regard to the relief under the provision, but taking into account the special testing rules described below,[143] and (2) after the date as of which the class was closed, any plan amendment modifying the closed class or the benefits, rights, and features provided to the closed class

[142] References under the provision to a closed class of participants and similar references to a closed class include arrangements under which one or more classes of participants are closed, except that one or more classes of participants closed on different dates are not aggregated for purposes of determining the date any such class was closed.

[143] Other testing options available under present law are also available for this purpose.

does not discriminate significantly in favor of highly compensated employees.

For purposes of requirement (1) above, the following special testing rules apply:

- In applying the plan coverage transition rule for business acquisitions, dispositions, and similar transactions, the closing of the class of participants is not treated as a significant change in coverage;
- Two or more plans do not fail to be eligible to be a treated as a single plan solely by reason of having different plan years;[144] and
- Changes in employee population are disregarded to the extent attributable to individuals who become employees or cease to be employees, after the date the class is closed, by reason of a merger, acquisition, divestiture, or similar event.

Benefit accruals for a closed class

Under the provision, an applicable defined benefit plan that provides benefits to a closed class may be aggregated, that is, treated as a single plan, and tested on a benefit accrual basis with one or more defined contribution plans (without having to satisfy the threshold conditions under present law) if (1) for the plan year as of which the class closes and the two succeeding plan years, the plan satisfies the plan coverage and nondiscrimination requirements without regard to the relief under the provision, but taking into account the special testing rules described above,[145] and (2) after the date as of which the class was closed, any plan amendment modifying the closed class or the benefits provided to the closed class does not discriminate significantly in favor of highly compensated employees.

Under the provision, defined contribution plans that may be aggregated with an applicable defined benefit plan and treated as a single plan include the portion of one or more defined contribution plans consisting of matching contributions, an ESOP, or matching or nonelective contributions under a section 403(b) plan. If an applicable defined benefit plan is aggregated with the portion of a defined contribution plan consisting of matching contributions, any portion of the defined contribution plan consisting of elective deferrals must also be aggregated. In addition, the matching contributions are treated in the same manner as nonelective contributions, including for purposes of permitted disparity.

Applicable defined benefit plan

An applicable defined benefit plan to which relief under the provision applies is a defined benefit plan under which the class was closed (or the plan frozen) before September 21, 2016, or that meets the following alternative conditions: (1) taking into account any predecessor plan, the plan has been in effect for at least five years as of the date the class is closed (or the plan is frozen) and (2) under the plan, during the five-year period preceding that date, (a) for purposes of the relief provided with respect to benefits, rights,

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[144] This rule applies also for purposes applying the plan coverage and other nondiscrimination requirements to an applicable defined benefit plan and one or more defined contributions that, under the provision, may be treated as a single plan as described below.

[145] Other testing options available under present law are also available for this purpose.

and features for a closed class, there has not been a substantial increase in the coverage or value of the benefits, rights, or features, or (b) for purposes of the relief provided with respect to benefit accruals for a closed class or the minimum participation requirements, there has not been a substantial increase in the coverage or benefits under the plan.

For purposes of (2)(a) above, a plan is treated as having a substantial increase in coverage or value of benefits, rights, or features only if, during the applicable five-year period, either the number of participants covered by the benefits, rights, or features on the date the period ends is more than 50 percent greater than the number on the first day of the plan year in which the period began, or the benefits, rights, and features have been modified by one or more plan amendments in such a way that, as of the date the class is closed, the value of the benefits, rights, and features to the closed class as a whole is substantially greater than the value as of the first day of the five-year period, solely as a result of the amendments.

For purposes of (2)(b) above, a plan is treated as having had a substantial increase in coverage or benefits only if, during the applicable five-year period, either the number of participants benefiting under the plan on the date the period ends is more than 50 percent greater than the number of participants on the first day of the plan year in which the period began, or the average benefit provided to participants on the date the period ends is more than 50 percent greater than the average benefit provided on the first day of the plan year in which the period began. In applying this requirement, the average benefit provided to participants under the plan is treated as having remained the same between the two relevant dates if the benefit formula applicable to the participants has not changed between the dates and, if the benefit formula has changed, the average benefit under the plan is considered to have increased by more than 50 percent only if the target normal cost for all participants benefiting under the plan for the plan year in which the five-year period ends exceeds the target normal cost for all such participants for that plan year if determined using the benefit formula in effect for the participants for the first plan year in the five-year period by more than 50 percent.[146] In applying these rules, a multiple-employer plan is treated as a single plan, rather than as separate plans separately covering the employees of each participating employer.

In applying these standards, any increase in coverage or value, or in coverage or benefits, whichever is applicable, is generally disregarded if it is attributable to coverage and value, or coverage and benefits, provided to employees who (1) became participants as a result of a merger, acquisition, or similar event that occurred during the 7-year period preceding the date the class was closed, or (2) became participants by reason of a merger of the plan with another

[146] Under the funding requirements applicable to defined benefit plans, target normal cost for a plan year (defined in section 430(b)(1)(A)(i)) is generally the sum of the present value of the benefits expected to be earned under the plan during the plan year plus the amount of plan-related expenses to be paid from plan assets during the plan year. Under the provision, in applying this average benefit rule to certain defined benefit plans maintained by cooperative organizations and charities, referred to as CSEC plans (defined in section 414(y)), which are subject to different funding requirements, the CSEC plan's normal cost under section 433(j)(1)(B) is used instead of target normal cost.

plan that had been in effect for at least five years as of the date of the merger and, in the case of benefits, rights, or features for a closed class, under the merger, the benefits, rights, or features under one plan were conformed to the benefits, rights, or features under the other plan prospectively.

Make-whole contributions under a defined contribution plan

Under the provision, a defined contribution plan is permitted to be tested on an equivalent benefit accrual basis (without having to satisfy the threshold conditions under present law) if the following requirements are met:

- The plan provides make-whole contributions to a closed class of participants whose accruals under a defined benefit plan have been reduced or ended ("make-whole class");
- For the plan year of the defined contribution plan as of which the make-whole class closes and the two succeeding plan years, the make-whole class satisfies the nondiscriminatory classification requirement under the plan coverage rules, taking into account the special testing rules described above;
- After the date as of which the class was closed, any amendment to the defined contribution plan modifying the make-whole class or the allocations, benefits, rights, and features provided to the make-whole class does not discriminate significantly in favor of highly compensated employees; and
- Either the class was closed before September 21, 2016, or the defined benefit plan is an applicable defined benefit plan under the alternative conditions applicable for purposes of the relief provided with respect to benefit accruals for a closed class.

With respect to one or more defined contribution plans meeting the requirements above, in applying the plan coverage and nondiscrimination requirements, the portion of the plan providing make-whole or other nonelective contributions may also be aggregated and tested on an equivalent benefit accrual basis with the portion of one or more other defined contribution plans consisting of matching contributions, an ESOP, or matching or nonelective contributions under a section 403(b) plan. If the plan is aggregated with the portion of a defined contribution plan consisting of matching contributions, any portion of the defined contribution plan consisting of elective deferrals must also be aggregated. In addition, the matching contributions are treated in the same manner as nonelective contributions, including for purposes of permitted disparity.

Under the provision, "make-whole contributions" generally means nonelective contributions for each employee in the make-whole class that are reasonably calculated, in a consistent manner, to replace some or all of the retirement benefits that the employee would have received under the defined benefit plan and any other plan or qualified cash or deferred arrangement under a section 401(k) plan if no change had been made to the defined benefit plan and other plan or arrangement.[147] However, under a special rule, in the case of a defined contribution plan that provides benefits,

[147] For this purpose, consistency is not required with respect to employees who were subject to different benefit formulas under the defined benefit plan.

rights, or features to a closed class of participants whose accruals under a defined benefit plan have been reduced or eliminated, the plan will not fail to satisfy the nondiscrimination requirements solely by reason of the composition of the closed class, or the benefits, rights, or features provided to the closed class, if the defined contribution plan and defined benefit plan otherwise meet the requirements described above but for the fact that the make-whole contributions under the defined contribution plan are made in whole or in part through matching contributions.

If a portion of a defined contribution plan eligible for relief under the provision is spun off to another employer, and if the spun-off plan continues to satisfy any ongoing requirements applicable for the relevant relief as described above, the relevant relief for the spun-off plan will continue with respect to the other employer.

EFFECTIVE DATE

The provision is generally effective on the date of enactment of the provision, without regard to whether any plan modifications referred to in the provision are adopted or effective before, on, or after the date of enactment. However, at the election of a plan sponsor, the provision will apply to plan years beginning after December 31, 2013. For purposes of the provision, a closed class of participants under a defined benefit plan is treated as being closed before September 21, 2016, if the plan sponsor's intention to create the closed class is reflected in formal written documents and communicated to participants before that date. In addition, a plan does not fail to be eligible for the relief under the provision solely because (1) in the case of benefits, rights, or features for a closed class under a defined benefit plan, the plan was amended before the date of enactment to eliminate one or more benefits, rights, or features and is further amended after the date of enactment to provide the previously eliminated benefits, rights, or features to a closed class of participants, or (2) in the case of benefit accruals for a closed class under a defined benefit plan or application of the minimum benefit requirements to a closed or frozen defined benefit plan, the plan was amended before the date of the enactment to cease all benefit accruals and is further amended after the date of enactment to provide benefit accruals to a closed class of participants. In either case, the relevant relief applies only if the plan otherwise meets the requirements for the relief, and, in applying the relevant relief, the date the class of participants is closed is the effective date of the later amendment.

F. MODIFICATION OF PBGC PREMIUMS FOR CSEC PLANS (SEC. 206 OF THE BILL AND SEC. 4006 OF ERISA)

PRESENT LAW

Qualified retirement plans, including defined benefit plans, are categorized as single-employer plans or multiple-employer plans.[148]

[148] A third type of plan is a multiemployer plan, defined under sec. 414(f) as a plan maintained pursuant to one or more collective bargaining agreements with two or more unrelated employers and to which the employers are required to contribute under the collective bargaining agreement(s). Multiemployer plans are also known as Taft-Hartley plans. Multiemployer plans are subject to different minimum funding requirements from those applicable to single-employer and multiple-employer plans, as well as to different PBGC premium and benefit guarantee structures.

A single-employer plan is a plan maintained by one employer.[149] A multiple-employer plan generally is a single plan maintained by two or more unrelated employers (that is, employers that are not treated as a single employer under the aggregation rules).[150]

Defined benefit plans maintained by private employers are generally subject to minimum funding requirements.[151] Historically, single-employer and multiple-employer defined benefit plans have been subject to the same minimum funding requirements. However, when the funding requirements for single-employer plans were substantially revised by the Pension Protection Act of 2006,[152] effective 2008, a delayed effective date was provided for certain multiple-employer plans in order to allow time for further congressional consideration of appropriate rules for these plans. Such consideration resulted in the enactment in 2014 of the Cooperative and Small Employer Charity Pension Flexibility Act ("CSEC Act"),[153] which provides specific funding rules for certain multiple-employer plans, referred to as CSEC plans.[154]

Private defined benefit plans are also covered by the Pension Benefit Guaranty Corporation ("PBGC") insurance program, under which the PBGC guarantees the payment of certain plan benefits, and plans are required to pay annual premiums to the PBGC.[155] Single-employer and multiple-employer plans, including CSEC plans, are subject to the same PBGC premium requirements, consisting of flat-rate, per participant premiums and variable rate premiums, based on the unfunded vested benefits under the plan.[156] For 2016, flat-rate premiums are $64 per participant, and variable rate premiums are $30 for each $1,000 of unfunded vested benefits, subject to a limit of $500 multiplied by the number of plan participants.[157] For this purpose, unfunded vested benefits under a plan for a plan year is the excess (if any) of (1) the plan's funding target for the plan year, determined by taking into account only vested benefits and using specified interest rates, over (2) the fair market value of plan assets.

Under the funding rules applicable to single-employer plans, a plan's funding target is the present value of all benefits accrued or earned under the plan as of the beginning of the plan year, determined using certain specified actuarial assumptions, including specified interest rates and mortality. A single-employer plan's funding target is a factor taken into account in determining required contributions for the plan. Although a CSEC plan's funding target is used under present law to determine variable rate premiums, it does not apply in determining required contributions for

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[149] For this purpose, businesses and organizations that are members of a controlled group of corporations, a group under common control, or an affiliated service group are treated as one employer (referred to as "aggregation"). Secs. 414(b), (c), (m) and (o).

[150] Sec. 413(c). multiple-employer status does not apply if the plan is a multiemployer plan.

[151] Secs. 412 and 430–433 and ERISA secs. 301–306. Unless a funding waiver is obtained, an employer may be subject to a two-tier excise tax under section 4971 if the funding requirements are not met.

[152] Pub. L. No. 109–280.

[153] Pub. L. No. 113–197.

[154] As defined in section 414(y) and ERISA section 210(f), CSEC plans include defined benefit plans maintained by certain cooperative organizations, such as rural electric or telephone cooperatives, or by certain tax-exempt organizations.

[155] Title IV of ERISA.

[156] The same PBGC benefit guarantee structure also applies to single-employer and multiple-employer plans.

[157] These premium rates have been increased several times by legislation since 2005 and are subject to automatic increases to reflect inflation (referred to as "indexing").

a CSEC plan. Instead, a CSEC plan's funding liability applies, which is the present value of all benefits accrued or earned under the plan as of the beginning of the plan year, determined using reasonable actuarial assumptions chosen by the plan's actuary.

REASONS FOR CHANGE

In 2014, Congress passed legislation resulting in different sets of funding rules for three types of pension plans: single-employer, multiemployer and CSEC plans. In line with this change, the Committee believes that the three types of pension plans also should have individualized rules for calculating PBGC premiums.

EXPLANATION OF PROVISION

Under the provision, for CSEC plans, flat-rate premiums are $19 per participant, and variable rate premiums are $9 for each $1,000 of unfunded vested benefits.[158] In addition, for purposes of determining a CSEC plan's variable rate premiums, unfunded vested benefits for a plan year is the excess (if any) of (1) the plan's funding liability, determined by taking into account only vested benefits, over (2) the fair market value of plan assets.

EFFECTIVE DATE

The provision applies to plan years beginning after December 31, 2015.

TITLE III—BENEFITS RELATING TO THE UNITED STATES TAX COURT

A. PROVISIONS RELATING TO JUDGES OF THE TAX COURT (SECS. 301–302 OF THE BILL AND SEC. 7447 OF THE CODE)

PRESENT LAW

In general

The United States Tax Court ("Tax Court") is established by the Congress pursuant to Article I of the U.S. Constitution (an "Article I" court).[159] The salary of a Tax Court judge is the same salary as received by a U.S. District Court judge.[160] As discussed below, judges of the Tax Court are provided also with some benefits that correspond to benefits provided to U.S. District Court judges, including specific retirement and survivor benefit programs for Tax Court judges.[161]

Retirement and survivors benefits

A Tax Court judge may be covered under the Federal Employees Retirement System ("FERS") or, depending on when the judge began Federal employment, the Civil Service Retirement System ("CSRS"). FERS and CSRS provide annuity benefits to a retired employee and, in some cases, to survivors of a deceased employee. Employees covered by FERS are also covered by the Social Security

[158] These are the premium rates that applied to single-employer and multiple-employer plans in 2005 and are not subject to indexing.
[159] Sec. 7441.
[160] Sec. 7443(c).
[161] Secs. 7447 and 7448.

program.[162] Employees covered by FERS and CSRS may contribute to the Thrift Savings Plan ("TSP"). Employees covered by FERS (but not CSRS) generally are also eligible for agency contributions (that is, nonelective contributions and matching contributions). A Tax Court judge is eligible to contribute to the Thrift Savings Plan, but is not eligible for agency contributions, regardless of which Federal retirement plan the judge is covered by.

A Tax Court judge may elect at any time while serving as a Tax Court judge to be covered by a "retired pay" program of the Tax Court rather than under another Federal retirement program, such as FERS or CSRS.[163] A Tax Court judge may also elect to participate in a plan providing annuity benefits for the judge's surviving spouse and dependent children (the "Tax Court survivors' annuity plan").[164] Generally, benefits under the Tax Court survivors' annuity plan are payable only if the judge has performed at least five years of service and made contributions to the plan for at least five years of service.[165]

The rules governing the retired pay plan for Tax Court judges and the Tax Court survivors' annuity plan provide for coordination between CSRS and the retired pay or survivors' annuity plan when a judge covered by CSRS elects into those plans. For example, if a judge covered by CSRS elects retired pay, the accumulated CSRS contributions previously made by the judge are refunded to the judge with interest. However, the rules do not address coordination with FERS.

Limit on outside earned income of a judge receiving retired pay

Under the retired pay plan for Tax Court judges, retired judges generally receive retired pay equal to the salary of an active judge and must be available for recall to perform judicial duties as needed by the court for up to 90 days a year (unless the judge consents to a longer period). However, retired judges may elect to freeze the amount of their retired pay, and those who do so are not available for recall.

Retired Tax Court judges on recall are subject to the limitations on outside earned income that apply to active Federal employees under the Ethics in Government Act of 1978. Retired Tax Court judges who elect to freeze the amount of their retired pay (thus making themselves unavailable for recall) are not subject to the limitations on outside earned income.

REASONS FOR CHANGE

The benefit programs for Tax Court judges are intended to accord with similar programs applicable to District Court judges.[166] However, over time, differences have developed between the benefits provided to Tax Court judges and to District Court judges and similar judges in certain other Article I courts. The Committee be-

[162] Wages of employees covered by Social Security are subject to old-age, survivors and disability insurance ("OASDI") taxes under the Federal Insurance Contributions Act ("FICA"), consisting of employer and portions, each at a rate of 6.2 percent of covered wages up to the OASDI wage base ($118,500 for 2016). Wages up to the OASDI wage base are taken into account in determining Social Security benefits.

[163] Secs. 7447. Retired pay is generally equal to the salary of an active Tax Court judge.

[164] Sec. 7448. Special trial judges may also elect into the Tax Court survivors' annuity plan.

[165] For this purpose, a judge may make contributions with respect to service performed before electing to participate in the plan.

[166] See, for example, S. Rep. No. 91–552, at 303 (1969).

lieves that, as a general matter, parity should exist between the benefits provided to Tax Court judges and those provided to District Court judges and judges in other Article I courts. Thus, the benefits provided to Tax Court judges should be updated to reflect benefits currently provided to these other Federal judges. Moreover, the Committee believes that exempting from the limitation on outside earned income compensation received by retired Tax Court judges for teaching will encourage such judges to remain available for recall by the court.

EXPLANATION OF PROVISIONS

Retirement and survivors benefits

The provision allows a Tax Court judge who is covered by FERS to receive agency contributions to the TSP, similar to other employees covered by FERS. If a judge covered by FERS elects retired pay, rather than FERS benefits, the judge's retired pay is offset by the amount of previous TSP distributions attributable to agency contributions (without regard to earnings on the agency contributions) made during years of service as a Tax Court judge while covered by FERS.

Under the provision, benefits under the survivors' annuity plan are payable if a Tax Court judge has performed at least 18 months of service and made contributions for at least 18 months (rather than five years). In addition, benefits under the survivors' annuity plan are payable if a Tax Court judge is assassinated before the judge has performed 18 months of service and made contributions for 18 months.[167]

The provision amends the rules governing the retired pay plan for Tax Court judges and the Tax Court survivors' annuity plan to provide for coordination between FERS and those plans when a judge covered by FERS elects into those plans, similar to coordination with CSRS under present law.

Limit on outside earned income of a judge receiving retired pay

Under the provision, compensation earned by a retired Tax Court judge for teaching is not treated as outside earned income for purposes of limitations under the Ethics in Government Act of 1978.

EFFECTIVE DATE

The provisions are effective on the date of enactment, except that the provision relating to TSP contributions applies to basic pay earned while serving as a Tax Court judge and the provision relating to outside earned income of a judge receiving retired pay applies to any individual serving as a retired Tax Court judge on or after the date of enactment.

[167] These changes apply also to special trial judges who elect into the Tax Court survivors' annuity plan.

B. Provisions Relating to Special Trial Judges of the Tax Court (secs. 303–305 of the bill and secs. 7443A and new 7443B and 7443C of the Code)

PRESENT LAW

The chief judge of the Tax Court may appoint special trial judges to handle certain cases.[168] Special trial judges serve for an indefinite term. Special trial judges receive a salary of 90 percent of the salary of a Tax Court judge. Special trial judges do not have authority to impose punishment in the case of contempt of the authority of the Tax Court.[169]

Special trial judges generally are covered by the benefit programs that apply to Federal executive branch employees, including CSRS or FERS (depending on when the judge began Federal employment). Special trial judges may contribute to TSP, and those covered by FERS are also eligible for agency contributions. Special trial judges covered by FERS are also covered by the Social Security program. Special trial judges may also elect to participate in the Tax Court survivors' annuity plan. An election into the Tax Court survivors' annuity plan must be made not later than six months after the later of the date the special trial judge takes office or the date the judge marries.

Special trial judges are required to be covered by a leave program under which they earn annual and sick leave during their period of employment. At termination of employment, a lump–sum payment is made to the special trial judge for unused annual leave, and unused sick leave is credited as additional service for certain purposes under CSRS or FERS. Group-term life insurance is available to Federal employees, including special trial judges, under the Federal Employees Group Life Insurance ("FEGLI") program. Under changes made to the FEGLI program in 1999, higher premiums apply to older employees than to younger employees ("age-based premiums").

REASONS FOR CHANGE

Special trial judges of the Tax Court perform a role similar to that of magistrate judges in courts established under Article III of the U.S. Constitution ("Article III" courts). However, disparities exist between the positions of magistrate judges of Article III courts and special trial judges of the Tax Court. For example, magistrate judges of Article III courts are appointed for a specific term, are subject to removal only in limited circumstances, and are eligible for coverage under special retirement and survivor benefit programs. The Committee believes that special trial judges of the Tax Court and magistrate judges of Article III courts should receive comparable treatment as to the status of the position, salary, and benefits. This will better enable the Tax Court to attract and retain qualified persons to serve in this capacity.

[168] Sec. 7443A.
[169] Sec. 7456(c) deals with contempt authority.

EXPLANATION OF PROVISIONS

Magistrate judges of the Tax Court

Under the provision, the position of special trial judge of the Tax Court is renamed as magistrate judge of the Tax Court ("magistrate judge"). Magistrate judges are appointed (or reappointed) to serve for eight–year terms and are subject to removal in limited circumstances. A magistrate judge receives a salary of 92 percent of the salary of a Tax Court judge.

Contempt authority

Under the provision, magistrate judges have the authority to impose punishment in the case of contempt of the authority of the Tax Court, subject to a limit on the sentence that may be imposed.

Leave, FEGLI and survivors' annuity plan

Under the provision, magistrate judges are not required to be covered by a leave program. Existing leave balances will be maintained and made available if a magistrate judge changes to a Federal position covered by a leave program. Otherwise, at separation from Federal employment, a lump–sum payment will be made to the magistrate judge for unused annual leave, and unused sick leave will be credited as additional service for certain purposes under CSRS or FERS.

In the case of magistrate judges age 65 or older, the provision allows the Tax Court to pay the portion of FEGLI premiums attributable to increases resulting from the 1999 FEGLI changes.

Under the provision, a magistrate judge may elect to participate in the Tax Court survivors' annuity plan at any time while serving as a magistrate judge.

Retirement plan for magistrate judges

In general

The provision establishes a new retirement plan for magistrate judges, under which a magistrate judge may elect to receive a retirement annuity from the Tax Court in lieu of benefits under CSRS or FERS. A magistrate judge who elects to be covered by the retirement program generally receives a refund of contributions (with interest) made to CSRS or FERS. A magistrate judge who elects to be covered by the retirement program may contribute to the TSP, but not receive agency contributions. The judge's retired pay is offset by the amount of previous TSP distributions attributable to agency contributions (without regard to earnings on the agency contributions) made during years of service as a Tax Court judge while covered by FERS. A special trial judge covered by the retirement program is not covered by the Social Security program.

Under the new plan, a magistrate judge may retire at age 65 with 14 years of service and receive an annuity equal to his or her salary at the time of retirement. For this purpose, service may include service performed as a special trial judge or a magistrate judge, with coordination of total benefits. The provision also provides for payment of a reduced annuity in the case a magistrate judge with at least eight years of service or in the case of disability or failure to be reappointed after serving at least one full term.

A magistrate judge receiving a retirement annuity is entitled to cost-of-living increases based on cost-of-living increases in benefits paid under CSRS. However, such an increase cannot cause the retirement annuity to exceed the current salary of a magistrate judge. A magistrate judge's retirement annuity is subject to freezing or suspension if the retired magistrate judge practices law or accepts other Federal employment.

Contributions of one percent of salary are withheld from the salary of a magistrate judge who elects to participate in the retirement annuity program. Such contributions must be made also with respect to prior service for which the magistrate judge elects credit under the retirement annuity program. No contributions are required after 14 years of service or retirement before 14 years of service. A lump sum refund of the magistrate judge's contributions (with interest) is made if no annuity is payable, for example, if the magistrate judge dies before retirement.

Establishment of Tax Court Judicial Officers' Retirement Fund

The provision establishes the Tax Court Judicial Officers' Retirement Fund (the "Fund"), which is appropriated for the payment of annuities, refunds, and other payments under the retirement annuity program. Contributions withheld from a magistrate judge's salary are deposited in the Fund. In addition, the provision requires there to be deposited into the Fund, by the end of each fiscal year, amounts required to reduce the Fund's unfunded liability to zero. For this purpose, the Fund's unfunded liability means the estimated excess, actuarially determined on an annual basis, of the present value of benefits payable from the Fund over the sum of (1) the present value of contributions to be withheld from the future salary of the magistrate judges and (2) the balance in the Fund as of the date the unfunded liability is determined.

Recall of retired magistrate judges

Under the provision, a retired magistrate judge may be recalled to perform services for up to 90 days a year. A retired magistrate judge who is receiving an annuity under the retirement plan for magistrate judges and is recalled is to be paid the difference between the annuity and the current rate of salary for magistrate judges. For years after any year in which the retired judge was recalled, the retirement annuity is increased to the rate of salary for magistrate judges during the last year in which the judge was recalled.

EFFECTIVE DATE

The provisions are generally effective on the date of enactment of the provisions. In addition, the provision relating to the position of magistrate judge, terms of appointment, salary, contempt authority, and leave apply to individuals serving as special trial judges as of the day before the date of enactment. Any individual serving as special trial judges as of the day before the date of enactment is deemed to be appointed as a magistrate judge on the date of enactment.

TITLE IV—OTHER BENEFITS

A. BENEFITS FOR VOLUNTEER FIREFIGHTERS AND EMERGENCY MEDICAL RESPONDERS (SEC. 401 OF THE BILL AND SEC. 139B OF THE CODE)

PRESENT LAW

Benefits for volunteer firefighters and emergency medical responders

In general, a reduction in property tax by persons who volunteer their services as emergency responders under a State law program is includible in gross income.[170] However, for taxable years beginning after December 31, 2007, and before January 1, 2011, an exclusion applied for any qualified State or local tax benefit and any qualified reimbursement payment provided to members of qualified volunteer emergency response organizations.[171]

A qualified volunteer emergency response organization is a volunteer organization that is organized and operated to provide firefighting or emergency medical services for persons in a State or a political subdivision and is required (by written agreement) by the State or political subdivision to furnish firefighting or emergency medical services in the State or political subdivision.

A qualified State or local tax benefit is any reduction or rebate of certain taxes provided by a State or local government on account of services performed by individuals as members of a qualified volunteer emergency response organization. These taxes are limited to State or local income taxes, State or local real property taxes, and State or local personal property taxes. A qualified reimbursement payment is a payment provided by a State or political subdivision thereof on account of reimbursement for expenses incurred in connection with the performance of services as a member of a qualified volunteer emergency response organization. The amount of excludible qualified reimbursement payments is limited to $30 for each month during which a volunteer performs services.

Itemized deductions

Individuals are allowed itemized deductions for (1) State and local income taxes, real property taxes, and personal property taxes, and (2) subject to certain limitations, contributions to charitable organizations, including unreimbursed expenses incurred in performing volunteer services for such an organization.[172]

The amount of State or local taxes taken into account in determining the deduction for taxes is reduced by the amount of any excludible qualified State or local tax benefit. Similarly, expenses paid or incurred by an individual in connection with the performance of services as a member of a qualified volunteer emergency response organization are taken into account for purposes of the charitable deduction only to the extent the expenses exceed the amount of any excludible qualified reimbursement payment.

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[170] IRS Chief Counsel Advice 200302045 (December 3, 2002).

[171] Sec. 139B. Under section 3121(a)(23), the exclusion applied also for purposes of taxes under the Federal Insurance Contributions Act ("FICA").

[172] Secs. 164(a) and 170.

REASONS FOR CHANGE

Emergency response volunteers provide valuable services to their communities. In return, communities sometimes provide tax discounts or rebates and modest stipends to cover volunteer expenses. The Committee wishes to relieve the administrative and financial burden associated with applying Federal tax to these benefits by reinstating the exclusion for a limited period and increasing the exclusion for expense reimbursements.

Explanation of Provision

The provision reinstates for one year the exclusions for qualified State or local tax benefits and qualified reimbursement payments provided to members of qualified volunteer emergency response organizations. The provision also increases the exclusion for qualified reimbursement payments to $50 for each month during which a volunteer performs services. Under the provision, the exclusions for qualified State or local tax benefits and qualified reimbursement payments do not apply for taxable years beginning after December 31, 2017.

EFFECTIVE DATE

The provision is effective for taxable years beginning after December 31, 2016. As described above, the exclusions do not apply for taxable years beginning after December 31, 2017. Thus, the exclusions apply only for taxable years beginning during 2017.

B. Treatment of Qualified Equity Grants (sec. 402 of the bill and secs. 83, 3401 and 6051 of the Code)

PRESENT LAW

Income tax treatment of employer stock transferred to an employee

Specific rules apply to property, including employer stock, transferred to an employee in connection with the performance of services.[173] These rules govern the amount and timing of income inclusion by the employee and the amount and timing of the employer's compensation deduction.

Under these rules, an employee generally must recognize income for the taxable year in which the employee's right to the stock is transferable or is not subject to a substantial risk of forfeiture (referred to herein as "substantially vested"). Thus, if the employee's right to the stock is substantially vested when the employee receives the stock, income is recognized for the taxable year in which received. If the employee's right to the stock is not substantially vested at the time of receipt, in general, income is recognized for the taxable year in which the employee's right becomes substantially vested.[174] The amount includible in the employee's income is

[173] Sec. 83. Section 83 applies generally to transfers of any property, not just employer stock, in connection with the performance of services by any service provider, not just an employee. However, the provision described herein applies only with respect to certain employer stock transferred to employees.

[174] Under section 83(b), if an employee's right to the stock is not substantially vested at the time of receipt (nonvested stock), the employee may nevertheless elect within 30 days of receipt to recognize income for the taxable year of receipt, referred to as a "section 83(b)" election. Under Treas. Reg. sec. 1.83–2, the employee makes an election by filing with the Internal Revenue Service a written statement that includes the fair market value of the property at the time

Continued

the excess of the fair market value of the stock (at the time of receipt if substantially vested at that time or, if not, at the time of substantial vesting) over the amount, if any, paid by the employee for the stock.

In general, an employee's right to stock or other property is subject to a substantial risk of forfeiture if the employee's right to full enjoyment of the property is subject to a condition, such as the future performance of substantial services.[175] An employee's right to stock or other property is transferable if the employee can transfer an interest in the property to any person other than the transferor of the property.[176] Thus, generally, employer stock transferred to an employee by an employer is not transferable merely because the employee can sell it back to the employer.

In the case of stock transferred to an employee, the employer is allowed a deduction (to the extent a deduction for a business expense is otherwise allowable) equal to the amount included in the employee's income as a result of receipt of the stock.[177] The deduction is allowed for the employer's taxable year in which or with which ends the taxable year for which the amount is included in the employee's income.

These rules do not apply to the grant to an employee of a nonqualified option on employer stock unless the option has a readily ascertainable fair market value.[178] Instead, these rules apply to the receipt of employer stock by the employee on exercise of the option. That is, if the right to the stock is substantially vested on receipt, income recognition applies for the taxable year of receipt. If the right to the stock is not substantially vested on receipt, the timing of income inclusion is determined under the rules applicable to the receipt of nonvested stock. In either case, the amount includible in income by the employee is the excess of the fair market value of the stock as of the time of income inclusion, less the exercise price paid by the employee and the amount, if any, paid by the employee for the option. The employer's deduction is also determined under these rules.

In some cases, the transfer of employer stock to an employee may be in settlement of restricted stock units. Restricted stock unit ("RSU") is a term used for an arrangement under which an employee has the right to receive at a specified time in the future an amount determined by reference to the value of one or more shares of employer stock. An employee's right to receive the future amount may be subject to a condition, such as continued employment for a certain period or the attainment of certain performance goals. The payment to the employee of the amount due under the arrangement is referred to as settlement of the RSU. The arrangement may provide for the settlement amount to be paid in cash or in employer stock (or either). The receipt of employer stock in settlement of an RSU is subject to the same rules as other receipts

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of receipt and the amount (if any) paid for the property. The employee must also provide a copy of the statement to the employer.

[175] See section 83(c)(1) and Treas. Reg. sec. 1.83–3(c) for the definition of substantial risk of forfeiture.

[176] Treas. Reg. sec. 1.83–3(d). In addition, under section 83(c)(2), the right to stock is transferable only if any transferee's right to the stock would not be subject to a substantial risk of forfeiture.

[177] Sec. 83(h).

[178] See section 83(e)(3) and Treas. Reg. sec. 1.83–7. A nonqualified option is an option on employer stock that is not a statutory option, discussed below.

of employer stock with respect to the timing and amount of income inclusion by the employee and the employer's deduction.

Employment taxes and reporting

Employment taxes generally consist of taxes under the Federal Insurance Contributions Act ("FICA"), tax under the Federal Unemployment Tax Act ("FUTA"), and income taxes required to be withheld by employers from wages paid to employees ("income tax withholding").[179] Unless an exception applies under the applicable rules, compensation provided to an employee constitutes wages subject to these taxes.

FICA imposes tax on employers and employees, generally based on the amount of wages paid to an employee during the year. The tax imposed on the employer and on the employee is each composed of two parts: (1) the Social Security or old age, survivors, and disability insurance ("OASDI") tax equal to 6.2 percent of covered wages up to the OASDI wage base ($118,500 for 2016); and (2) the Medicare or hospital insurance ("HI") tax equal to 1.45 percent of all covered wages.[180] The employee portion of FICA tax generally must be withheld and remitted to the Federal government by the employer. FICA tax withholding applies regardless of whether compensation is provided in the form of cash or a noncash form, such as a transfer of property (including employer stock) or in–kind benefits.[181]

FUTA imposes a tax on employers of six percent of wages up to the FUTA wage base of $7,000.

Income tax withholding generally applies when wages are paid by an employer to an employee, based on graduated withholding rates set out in tables published by the Internal Revenue Service ("IRS").[182] Like FICA tax withholding, income tax withholding applies regardless of whether compensation is provided in the form of cash or a noncash form, such as a transfer of property (including employer stock) or in–kind benefits.

An employer is required to furnish each employee with a statement of compensation information for a calendar year, including taxable compensation, FICA wages, and withheld income and FICA taxes.[183] In addition, information relating to certain nontaxable items must be reported, such as certain retirement and health plan contributions. The statement, made on Form W–2, Wage and Tax

[179] Secs. 3101–3128 (FICA), 3301–3311 (FUTA), and 3401–3404 (income tax withholding). Instead of FICA taxes, railroad employers and employees are subject, under the Railroad Retirement Tax Act ("RRTA"), sections 3201–3241, to taxes equivalent to FICA taxes with respect to compensation as defined for RRTA purposes. Sections 3501–3510 provide additional rules relating to all these taxes.

[180] The employee portion of the HI tax under FICA (not the employer portion) is increased by an additional tax of 0.9 percent on wages received in excess of a threshold amount. The threshold amount is $250,000 in the case of a joint return, $125,000 in the case of a married individual filing a separate return, and $200,000 in any other case.

[181] Under section 3501(b), employment taxes with respect to noncash fringe benefits are to be collected (or paid) by the employer at the time and in the manner prescribed by the Secretary of the Treasury ("Treasury"). Announcement 85–113, 1985–31 I.R.B. 31, provides guidance on the application of employment taxes with respect to noncash fringe benefits.

[182] Sec. 3402. Specific withholding rates apply in the case of supplemental wages.

[183] Secs. 6041 and 6051.

Statement, must be provided to each employee by January 31 of the succeeding year.[184]

Statutory options

Two types of statutory options apply with respect to employer stock: incentive stock options ("ISOs") and options provided under an employee stock purchase plan ("ESPP").[185] Stock received pursuant to a statutory option is subject to special rules, rather than the rules for nonqualified options, discussed above. No amount is includible in an employee's income on the grant or exercise of a statutory option.[186] In addition, no deduction is allowed to the employer with respect to the option or the stock transferred to an employee on exercise.

If a holding requirement is met with respect to the stock received on exercise of a statutory option and the employee later disposes of the stock, the employee's gain generally is treated as capital gain rather than ordinary income. Under the holding requirement, the employee must not dispose of the stock within two years after the date the option is granted or one year after the date the option is exercised. If a disposition occurs before the end of the required holding periods (a "disqualifying disposition"), statutory option treatment no longer applies. Instead, the income realized on the disqualifying disposition, up to the amount of income that would have applied if the option had been a nonqualified option, is includible in income by the employee as compensation received in the taxable year in which the disposition occurs and a corresponding deduction is allowable to the employer for the taxable year in which the disposition occurs.

Employment taxes do not apply with respect to the grant of a statutory option, the receipt of stock pursuant to the option, or a disqualifying disposition of the stock.[187]

Nonqualified deferred compensation

Compensation is generally includible in an employee's income when paid to the employee. However, in the case of a nonqualified deferred compensation plan,[188] unless the arrangement meets certain requirements, the amount of deferred compensation is includible in income for the taxable year when earned (or, if later, when not subject to a substantial risk of forfeiture) even if payment will not occur until a later year.[189] In general, under these requirements, the time when nonqualified deferred compensation will be

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[184] Employers send Form W–2 information to the Social Security Administration, which records information relating to Social Security and Medicare and forwards the Form W–2 information to the IRS. Employees include a copy of Form W–2 with their income tax returns.

[185] Sections 421–424 govern statutory options. Section 423(b)(5) requires that, under the terms of an ESPP, all employees granted options generally must have the same rights and privileges.

[186] Under section 56(b)(3), this income tax treatment with respect to stock received on exercise of an ISO does not apply for purposes of the alternative minimum tax under section 55.

[187] Secs. 3121(a)(22), 3306(b)(19), and the last sentence of section 421(b).

[188] Compensation earned by an employee is generally paid to the employee shortly after being earned. However, in some cases, payment is deferred to a later period, referred to as "deferred compensation." Deferred compensation may be provided through a plan that receives tax–favored treatment, such as a qualified retirement plan under section 401(a). Deferred compensation provided through a plan that is not eligible for tax–favored treatment is referred to as "nonqualified" deferred compensation.

[189] Section 409A and the regulations thereunder provide rules for nonqualified deferred compensation.

paid must be specified at the time of deferral with limits on further deferral after the time for payment.

Nonqualified options on employer stock may be structured so as not to be considered nonqualified deferred compensation and thus not subject to these rules.[190] An arrangement providing RSUs is considered a nonqualified deferred compensation plan and is subject to these rules, including the limits.

REASONS FOR CHANGE

Employer stock may provide a valuable form of employee compensation. In some cases, the receipt of employer stock with a high fair market value may result in compensation income, and a related tax liability, disproportionately large in comparison to an employee's regular salary or wages. In the case of publicly traded employer stock, an employee may sell some of the stock to provide funds to cover that tax liability. However, that approach often is not available in the case of a closely held company that restricts the transferability of its stock. This may make employer stock a less attractive form of compensation. In the case of stock options, the inability to pay the tax liability that would result from the stock received on exercise of the option may mean employees let options lapse, thus losing compensation they have already earned. The Committee wishes to address these situations by allowing employees to elect to defer recognition of income attributable to stock received on exercise of an option or settlement of an RSU until an opportunity to sell some of the stock arises, but in no event longer than five years from the date that the employee's right to the stock becomes substantially vested.

EXPLANATION OF PROVISION

In general

The provision allows a qualified employee to elect to defer, for income tax purposes, the inclusion in income of the amount of income attributable to qualified stock transferred to the employee by the employer.[191] An election to defer income inclusion ("inclusion deferral election") with respect to qualified stock must be made no later than 30 days after the first time the employee's right to the stock is substantially vested.[192] Absent an inclusion deferral election under the provision, the income is includable for the taxable year in which the qualified employee's right to the qualified stock is substantially vested under present law.

If an employee elects to defer income inclusion, the income must be included in the employee's income for the taxable year that includes the earliest of (1) the first date the qualified stock becomes transferable, including, solely for this purpose, transferable to the employer;[193] (2) the date the employee first becomes an excluded

[190] Treas. Reg. sec. 1.409A–1(b)(5). In addition, statutory option arrangements are not nonqualified deferred compensation arrangements.

[191] The provision does not apply to income with respect to nonvested stock that is includible as a result of a section 83(b) election.

[192] An inclusion deferral election is made in a manner similar to the manner in which a section 83(b) election is made. Thus, as in the case of a section 83(b) election under present law, the employee must provide a copy of the inclusion deferral election to the employer.

[193] Thus, for this purpose, the qualified stock is considered transferable if the employee has the ability to sell the stock to the employer (or any other person).

employee (as described below); (3) the first date on which any stock of the employer becomes readily tradable on an established securities market;[194] (4) the date five years after the date the employee's right to the stock becomes substantially vested; and (5) the date on which the employee revokes his or her inclusion deferral election.[195]

An employee may not make an inclusion deferral election for a year with respect to qualified stock if, in the preceding calendar year, the corporation purchased any of its outstanding stock unless at least 25 percent of the total dollar amount of the stock so purchased is stock with respect to which an inclusion deferral election is in effect ("deferral stock") and the determination of which individuals from whom deferral stock is purchased is made on a reasonable basis.[196] For purposes of this requirement, stock purchased from an individual is not treated as deferral stock (and the purchase is not treated as a purchase of deferral stock) if, immediately after the purchase, the individual holds any deferral stock with respect to which an inclusion deferral election has been in effect for a longer period than the election with respect to the purchased stock. Thus, in general, in applying the purchase requirement, an individual's deferral stock with respect to which an inclusion deferral election has been in effect for the longest periods must be purchased first. A corporation that has deferral stock outstanding as of the beginning of any calendar year and that purchases any of its outstanding stock during the calendar year must report on its income tax return for the taxable year in which, or with which, the calendar year ends the total dollar amount of the outstanding stock purchased during the calendar year and such other information as the Secretary may require for purposes of administering this requirement.

A qualified employee may make an inclusion deferral election with respect to qualified stock attributable to a statutory option.[197] In that case, the option is not treated as a statutory option and the rules relating to statutory options and related stock do not apply. In addition, an arrangement under which an employee may receive qualified stock is not treated as a nonqualified deferred compensation plan solely because of an employee's inclusion deferral election or ability to make an election.

Deferred income inclusion applies also for purposes of the employer's deduction of the amount of income attributable to the qualified stock. That is, if an employee makes an inclusion deferral election, the employer's deduction is deferred until the employer's taxable year in which or with which ends the taxable year of the employee for which the amount is included in the employee's income as described in (1)–(5) above.

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[194] An established securities market is determined for this purpose by the Secretary, but does not include any market unless the market is recognized as an established securities market for purposes of another Code provision.

[195] An inclusion deferral election is revoked at the time and in the manner as the Secretary provides.

[196] This requirement is met if the stock purchased by the corporation includes all the corporation's outstanding deferral stock.

[197] For purposes of the requirement that an ESPP provide employees with the same rights and privileges, the rules of the provision apply in determining which employees have the right to make an inclusion deferral election with respect to stock received under the ESPP.

Qualified employee and qualified stock

Under the provision, a qualified employee means an individual who is not an excluded employee and who agrees, in the inclusion deferral election, to meet the requirements necessary (as determined by the Secretary) to ensure the income tax withholding requirements of the employer corporation with respect to the qualified stock (as described below) are met. For this purpose, an excluded employee with respect to a corporation is any individual (1) who was a one-percent owner of the corporation at any time during the 10 preceding calendar years,[198] (2) who is, or has been at any prior time, the chief executive officer or chief financial officer of the corporation or an individual acting in either capacity, (3) who is a family member of an individual described in (1) or (2),[199] or (4) who has been one of the four highest compensated officers of the corporation for any of the 10 preceding taxable years.[200]

Qualified stock is any stock of a corporation if—

- an employee receives the stock in connection with the exercise of an option or in settlement of an RSU, and
- the option or RSU was granted by the corporation to the employee in connection with the performance of services and in a year in which the corporation was an eligible corporation (as described below).

However, qualified stock does not include any stock if, at the time the employee's right to the stock becomes substantially vested, the employee may sell the stock to, or otherwise receive cash in lieu of stock from, the corporation.

A corporation is an eligible corporation with respect to a calendar year if (1) no stock of the employer corporation (or any predecessor) is readily tradable on an established securities market during any preceding calendar year,[201] and (2) the corporation has a written plan under which, in the calendar year, not less than 80 percent of all employees who provide services to the corporation in the United States (or any U.S. possession) are granted stock options, or restricted stock units ("RSUs"), with the same rights and privileges to receive qualified stock ("80-percent requirement").[202] For this purpose, in general, the determination of rights and privileges with respect to stock is determined in a similar manner as provided under the present–law ESPP rules.[203] However, employees will not fail to be treated as having the same rights and privileges to receive qualified stock solely because the number of shares available to all employees is not equal in amount, provided that the number of shares available to each employee is more than a de minimis amount. In addition, rights and privileges with respect to

[198] One-percent owner status is determined under the top-heavy rules for qualified retirement plans, that is, section 416(i)(1)(B)(ii).

[199] In the case of one-percent owners, this results from application of the attribution rules of section 318 under section 416(i)(1)(B)(i)(II). Family members are determined under section 318(a)(1) and generally include an individual's spouse, children, grandchildren and parents.

[200] Highest paid employee status is determined at the close of the corporation's taxable year.

[201] This requirement continues to apply up to the time an inclusion deferral election is made. That is, under the provision, no inclusion deferral election may be made with respect to qualified stock if any stock of the corporation is readily tradable on an established securities market at any time before the election is made.

[202] In applying the requirement that 80 percent of employees receive stock options or RSUs, excluded employees and part-time employees are not taken into account. For this purpose, part-time employee is defined as under section 4980E(d)(4), that is, an employee customarily employed for fewer than 30 hours per week.

[203] Sec. 423(b)(5).

the exercise of a stock option are not treated for this purpose as the same as rights and privileges with respect to the settlement of an RSU.[204]

For purposes of the provision, corporations that are members of the same controlled group are treated as one corporation.

Notice, withholding and reporting requirements

Under the provision, a corporation that transfers qualified stock to a qualified employee must provide a notice to the qualified employee at the time (or a reasonable period before) the employee's right to the qualified stock is substantially vested (and income attributable to the stock would be includible absent an inclusion deferral election). The notice must (1) certify to the employee that the stock is qualified stock, and (2) notify the employee (a) that the employee may elect to defer income inclusion with respect to the stock and (b) that, if the employee makes an inclusion deferral election, the amount of income required to be included at the end of the deferral period will be based on the value of the stock at the time the employee's right to the stock is substantially vested, notwithstanding whether the value of the stock has declined during the deferral period, and the amount of income to be included at the end of the deferral period will be subject to withholding as provided under the provision, as well as of the employee's responsibilities with respect to required withholding. Failure to provide the notice may result in the imposition of a penalty of $100 for each failure, subject to a maximum penalty of $50,000 for all failures during any calendar year.

An inclusion deferral election applies only for income tax purposes. The application of FICA and FUTA are not affected. The provision includes specific income tax withholding and reporting requirements with respect to income subject to an inclusion deferral election.

For the taxable year for which income subject to an inclusion deferral election is required to be included in income by the employee (as described above), the amount required to be included in income is treated as wages with respect to which the employer is required to withhold income tax at a rate not less than the highest income tax rate applicable to individual taxpayers.[205] The employer must report on Form W–2 the amount of income covered by an inclusion deferral election (1) for the year of deferral and (2) for the year the income is required to be included in income by the employee. In addition, for any calendar year, the employer must report on Form W–2 the aggregate amount of income covered by inclusion deferral elections, determined as of the close of the calendar year.

EFFECTIVE DATE

The provision generally applies with respect to stock attributable to options exercised or RSUs settled after December 31, 2016. Under a transition rule, until the Secretary (or the Secretary's del-

[204] Under a transition rule, in the case of a calendar year beginning before January 1, 2017, the 80-percent requirement is applied without regard to whether the rights and privileges with respect to the qualified stock are the same.

[205] That is, the maximum rate of tax in effect for the year under section 1. The provision specifies that qualified stock is treated as a noncash fringe benefit for income tax withholding purposes.

egate) issues regulations or other guidance implementing the 80-percent and employer notice requirements under the provision, a corporation will be treated as complying with those requirements (respectively) if it complies with a reasonable good faith interpretation of the requirements. The penalty for a failure to provide the notice required under the provision applies to failures after December 31, 2016.

TITLE V—REVENUE PROVISIONS

A. MODIFICATIONS TO REQUIRED MINIMUM DISTRIBUTION RULES (SEC. 501 OF THE BILL AND SEC. 401(a)(9) OF THE CODE)

PRESENT LAW

In general

Minimum distribution rules apply to tax-favored employer-sponsored retirement plans and IRAs.[206] Employer-sponsored retirement plans are of two general types: defined benefit plans, under which benefits are determined under a plan formula and paid from general plan assets, rather than individual accounts; and defined contribution plans, under which benefits are based on a separate account for each participant, to which are allocated contributions, earnings and losses.

In general, under the minimum distribution rules, distribution of minimum benefits must begin to an employee (or IRA owner) no later than a required beginning date and a minimum amount must be distributed each year (sometimes referred to as "lifetime" minimum distribution requirements). These lifetime requirements do not apply to a Roth IRA.[207] Minimum distribution rules also apply to benefits payable with respect to an employee (or IRA owner) who has died (sometimes referred to as "after-death" minimum distribution requirements). The regulations provide a methodology for calculating the required minimum distribution from an individual account under a defined contribution plan or from an IRA.[208] In the case of annuity payments under a defined benefit plan or an annuity contract, the regulations provide requirements that the stream of annuity payments must satisfy.

Failure to comply with the minimum distribution requirement results in an excise tax imposed on the individual who was required to take the distributions equal to 50 percent of the required minimum amount not distributed for the year.[209] The excise tax may be waived in certain cases. For employer-sponsored retirement plans, satisfying the minimum distribution requirement under the plan terms and in operation is also a requirement for tax-favored treatment.

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[206] Secs. 401(a)(9), 403(b)(1), 408(a)(6), 408(b)(3), and 457(d)(2). Tax-favored employer-sponsored retirement plans include qualified retirement plans and annuities under sections 401(a) and 403(a), tax-deferred annuity plans under section 403(b), and governmental eligible deferred compensation plans under section 457(b). Minimum distribution requirements also apply to eligible deferred compensation plans under section 457(b) of tax-exempt employers.

[207] Sec. 408A(c)(5).

[208] Reflecting the directive in section 823 of the Pension Protection Act of 2006 (Pub. L. No. 109–280), pursuant to Treas. Reg. sec. 1.401(a)(9)–1, A–2(d), a governmental plan within the meaning of section 414(d) or a governmental eligible deferred compensation plan is treated as having complied with the statutory minimum distribution rules if the plan complies with a reasonable and good faith interpretation of those rules.

[209] Sec. 4974.

Required beginning date

For traditional IRAs, the required beginning date is April 1 following the calendar year in which the employee (or IRA owner) attains age 70½. For employer-sponsored retirement plans, for an employee other than an employee who is a five-percent owner in the year the employee attains age 70½, the required beginning date is April 1 after the later of the calendar year in which the employee attains age 70½ or retires. For an employee who is a five-percent owner under an employer-sponsored tax-favored retirement plan in the year the employee attains age 70½, the required beginning date is the same as for IRAs even if the employee continues to work past age 70½.

Lifetime rules

While an employee (or IRA owner) is alive, distributions of the individual's interest are required to be made (in accordance with regulations) over the life or life expectancy of the employee (or IRA owner), or over the joint lives or joint life expectancy of the employee (or IRA owner) and a designated beneficiary.[210] For defined contribution plans and IRAs, the required minimum distribution for each year is determined by dividing the account balance as of the end of the prior year by a distribution period which, while the employee (or IRA owner) is alive, is the factor for the employee (or IRA owner's) age from the uniform lifetime table included in the Treasury regulations.[211] The distribution period for annuity payments under a defined benefit plan or annuity contract (to the extent not limited to the life of the employee (or IRA owner) or the joint lives of the employee (or IRA owner) and a designated beneficiary) is generally subject to the same limitations as apply to individual accounts.

After-death rules

Payments over a distribution period

The after-death minimum distributions rules vary depending on (i) whether an employee (or IRA owner) dies on or after the required beginning date or before the required beginning date, and (ii) whether there is a designated beneficiary for the benefit.[212] Under the regulations, a designated beneficiary is an individual

[210] Sec. 401(a)(9)(A).

[211] Treas. Reg. sec. 1.401(a)(9)–5. This table is based on the joint life and last survivor expectancy of the individual and a hypothetical beneficiary 10 years younger. For an individual with a spouse as designated beneficiary who is more than 10 years younger (and thus the number of years in the couple's joint life and last survivor expectancy is greater than the uniform lifetime table), the joint life expectancy and last survivor expectancy of the couple (calculated using the table in the regulations) is used. For this purpose and other special rules that apply to the surviving spouse as beneficiary, a former spouse to whom all or a portion of an employee's benefit is payable pursuant to a qualified domestic relations order (within the meaning of section 414(p)) is treated as the spouse (including a surviving spouse) of the employee for purposes of section 401(a)(9).

[212] In the case of amounts for which the employee or IRA owner's surviving spouse is the beneficiary, the surviving spouse generally is permitted to do a tax-free rollover of such amounts into an IRA (or account of a tax-favored employer-sponsored plan of the spouse's employer) established in the surviving spouse's name as IRA owner or employee. The rules applicable to the rollover account, including the minimum distribution rules, are the same rules that apply to an IRA owner or employee. In the case of an IRA for which the spouse is sole beneficiary, this can be accomplished by simply renaming the IRA as an IRA held by the spouse as IRA owner rather than as a beneficiary.

designated as a beneficiary under the plan or IRA.[213] Similar to the lifetime rules, for defined contribution plans and IRAs ("individual accounts"), the required minimum distribution for each year after the death of the employee (or IRA owner) is generally determined by dividing the account balance as of the end of the prior year by a distribution period.

If an employee (or IRA owner) dies on or after the required beginning date, the basic statutory rule is that the remaining interest must be distributed at least as rapidly as under the method of distribution being used before death.[214] Under the regulations, for individual accounts, this rule is also interpreted as requiring the minimum required distribution to be calculated using a distribution period. If there is no designated beneficiary, the distribution period is equal to the remaining years of the employee's (or IRA owner's) life, as of the year of death.[215] If there is a designated beneficiary, the distribution period (if longer) is the beneficiary's life expectancy calculated using the life expectancy table in the regulations, determined in the year after the year of death.[216]

If an employee (or IRA owner) dies before the required beginning date and any portion of the benefit is payable to a designated beneficiary, the statutory rule is that distributions are generally required to begin within one year of the employee's (or IRA owner's) death (or such later date as prescribed in regulations) and are permitted to be paid (in accordance with regulations) over the life or life expectancy of the designated beneficiary. If the beneficiary of the employee (or IRA owner) is the individual's surviving spouse, distributions are not required to commence until the year in which the employee (or IRA owner) would have attained age 70½. If the surviving spouse dies before the employee (or IRA owner) would have attained age 70½, the after-death rules apply after the death of the spouse as though the spouse were the employee (or IRA owner). Under the regulations, for individual accounts, the required minimum distribution for each year is determined using a distribution period and the period is measured by the designated beneficiary's life expectancy, calculated in the same manner as if the individual died on or after the required beginning date.[217]

In cases where distribution after death is based on life expectancy (either the remaining life expectancy of the employee (or IRA owner) or a designated beneficiary), the distribution period generally is fixed at the employee's (or IRA owner's) death and then reduced by one for each year that elapses after the year in which it is calculated. If the designated beneficiary dies during the distribution period, distributions continue to the subsequent beneficiaries over the remaining years in the distribution period.[218]

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[213] Treas. Reg. sec. 1.401(a)(9)–4, A–1. The individual need not be named as long as the individual is identifiable under the terms of the plan (or IRA). There are special rules for multiple beneficiaries and for trusts named as beneficiary (where the beneficiaries of the trust are individuals). However, the fact that an interest under a plan or IRA passes to a certain individual under a will or otherwise under State law does not make that individual a designated beneficiary unless the individual is designated as a beneficiary under the plan or IRA.

[214] Sec. 401(a)(9)(B)(i).

[215] Treas. Reg. sec. 1.401(a)(9)–5, A–5(a)(2).

[216] Treas. Reg. sec. 1.401(a)(9)–5, A–5(a)(1).

[217] Treas. Reg. sec. 1.401(a)(9)–5, A–5(b).

[218] If the distribution period is based on the surviving spouse's life expectancy (whether the employee or IRA owner's death is before or after the required beginning date), the spouse's life

Continued

The distribution period for annuity payments under a defined benefit plan or annuity contract (to the extent not limited to the life of a designated beneficiary) is generally subject to the same limitations as apply to individual accounts.

Five-year rule

If an employee (or IRA owner) dies before the required beginning date and there is no designated beneficiary, then the entire remaining interest of the employee (or IRA owner) must generally be distributed by the end of the fifth calendar year following the individual's death.[219]

Defined benefit plans and annuity distributions

The regulations provide rules for the amount of annuity distributions from a defined benefit plan, or from an annuity purchased by the plan from an insurance company, that are paid over life or life expectancy. Annuity distributions are generally required to be nonincreasing with certain exceptions, which include, for example, (i) increases to the extent of certain specified cost-of-living indices, (ii) a constant percentage increase (for a qualified defined benefit plan, the constant percentage cannot exceed five percent per year), (iii) certain accelerations of payments, and (iv) increases to reflect when an annuity is converted to a single life annuity after the death of the beneficiary under a joint and survivor annuity or after termination of the survivor annuity under a qualified domestic relations order.[220] If distributions are in the form of a joint and survivor annuity and the survivor annuitant both is not the surviving spouse and is younger than the employee (or IRA owner), the survivor annuity benefit is limited to a percentage of the life annuity benefit for the employee (or IRA owner). The survivor benefit as a percentage of the benefit of the primary annuitant is required to be smaller (but not required to be less than 52 percent) as the difference in the ages of the primary annuitant and the survivor annuitant become greater.

Plan amendment and anti-cut-back requirements

Present law provides a remedial amendment period during which, under certain circumstances, a qualified retirement plan may be amended retroactively in order to comply with the qualification requirements.[221] In general, plan amendments to reflect changes in the law generally must be made by the time prescribed by law for filing the income tax return of the employer for the employer's taxable year in which the change in law occurs. The Secretary may extend the time by which plan amendments need to be made.

The Code and ERISA generally prohibit plan amendment that reduce accrued benefits, including amendments that eliminate or re-

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expectancy generally is recalculated each year while the spouse is alive and then fixed the year after the spouse's death.

[219] Section 401(a)(9)(B)(ii) provides that the entire interest must be distributed within five years of the employee's death. Treas. Reg. sec. 1.401(a)(9)–3, A–2, provides that this requirement is satisfied if the entire interest is distributed by the end of the fifth calendar year following the employee's death. There are provisions in the regulations allowing a designated beneficiary to take advantage of the five-year rule. See Treas. Reg. secs. 1.401(a)(9)–4, A–4, and 1.4974–2, A–7(b).

[220] Treas. Reg. sec. 1.401(a)(9)–6, A–14.

[221] Sec. 401(b).

duce optional forms of benefit with respect to benefits already accrued except to the extent prescribed in regulations.[222] This prohibition on the reduction of accrued benefits is commonly referred to as the "anti-cut-back rule."

REASONS FOR CHANGE

The tax subsidy for retirement savings is intended to encourage the accumulation of funds that will provide adequate income during retirement. Because of the uncertainty as to how much income will be needed during retirement, individuals may accumulate more than is actually needed during the individual's lifetime (and surviving spouse's lifetime, if applicable), leaving some amount to other surviving beneficiaries. Present law generally allows other beneficiaries to withdraw inherited amounts from a tax-favored account or plan over the beneficiary's lifetime, thus allowing funds to remain in tax-favored form long after the original purpose of adequate retirement income has been served. In some cases, the inherited amount may be so large that tax-favored retirement savings includes an estate-planning element, rather than just providing retirement income security. The Committee believes that the tax subsidy for retirement savings should be limited once the needs of the individual and surviving spouse, and certain other beneficiaries, have been met.

EXPLANATION OF PROVISION

Change in after-death rules for defined contribution plans and IRAs

The provision changes the after-death required minimum distribution rules applicable to defined contribution plans and IRAs, as described below. However, the provision applies only to the extent that the amount of an individual's aggregate account balances under all IRAs and defined contributions plans, determined as of the date of death, exceeds $450,000 (indexed for inflation). Thus for example if an individual dies with aggregate account balances of $600,000, as of the date of death, present law continues to apply to $450,000, and the provision applies to the remaining $150,000.

If an employee has multiple defined contribution plan accounts and IRAs, the $450,000 threshold is allocated among the accounts as provided in regulations. If the individual has more than one beneficiary, the portion of the amount above $450,000 that is subject to the provision with respect to each beneficiary is the amount that is the same proportion of the excess as the portion of the total to which the individual is entitled. The result is the same whether or not the beneficiary is an eligible beneficiary (as described below). Thus, under the example above, if the individual has two beneficiaries, one who is an eligible designated beneficiary, as discussed below, and one who is not an eligible designated beneficiary, each with a right to 50 percent of the aggregate amount, then present law applies for determining required minimum distributions for each beneficiary with respect to $225,000 and the provision applies to $75,000.

The provision does not apply for determining after-death required minimum distributions from defined benefit plans.

[222] Sec. 411(d)(6) and ERISA sec. 204(g).

Expansion of five-year after-death rule for defined contributions plans

In general

Under the provision, the five-year rule is the general rule for all distributions after death (regardless of whether the employee (or IRA owner) dies before, on, or after the required beginning date) unless the designated beneficiary is an eligible beneficiary as defined in the provision. Thus, in the case of an ineligible beneficiary, distribution of the employee (or IRA owner's) entire benefit is required to be distributed by the end of the fifth calendar year following the year of the employee or IRA owner's death.

Eligible beneficiaries

For eligible beneficiaries, an exception to the five-year rule (for death before the required beginning date under present law) applies whether or not the employee (or IRA owner) dies before, on, or after the required beginning date. The exception (similar to present law) generally allows distributions over life or life expectancy of an eligible beneficiary beginning in the year following the year of death. Eligible beneficiaries includes any beneficiary who, as of the date of death, is the surviving spouse of the employee (or IRA owner),[223] is disabled, is a chronically ill individual, is an individual who is not more than 10 years younger than the employee (or IRA owner), or is a child of the employee (or IRA owner) who has not reached the age of majority. In the case of a child who has not reached the age of majority, calculation of the minimum required distribution under this exception is only allowed through the year that the child reaches the age of majority.

Further, under the provision, the five-year rule also applies after the death of an eligible beneficiary or after a child reaches the age of majority. Thus, for example, if a disabled child of an employee (or IRA owner) is an eligible beneficiary of a parent who dies when the child is age 20 and the child dies at age 30, even though 52.1 years remain in measurement period,[224] the disabled child's remaining beneficiary interest must be distributed by the end of the fifth year following the death of the disabled child. If a child is an eligible beneficiary based on having not reached the age of majority before the employee's (or IRA owner's) death, the five-year rule applies beginning with the earlier of the date of the child's death or the date that the child reaches the age of majority. The child's entire interest must be distributed by the end of the fifth year following that date.

As under present law, if the surviving spouse is the beneficiary, a special rule allows the commencement of distribution to be delayed until end of the year that the employee (or IRA owner) would

[223] As in the case of the present law special rule in section 401(a)(9)(B)(iv) for surviving spouses, spouse is not defined in the provision. Under Treas. Reg. sec. 1.401(a)(9)–8, A–5, a spouse is the employee's spouse under applicable State law. In the case of a special rule for a surviving spouse, that determination is generally made based on the employee's marital status on the date of death. An exception is provided in Treas. Reg. sec. 1.401(a)(9)–6, A–6, under which a former spouse to whom all or a portion of the employee's benefits is payable pursuant to a qualified domestics relations order as defined in section 414(p) is treated as the employee's spouse (including a surviving spouse). In the case of a qualified joint and survivor annuity under section 401(a)(11) and 417, the spouse is generally determined as of the annuity starting date.

[224] The measurement period is the life expectancy of the child calculated for the child's age in the year after the employee's (or IRA owner's) death (age 21 (20 plus 1)).

have attained age 70½. If the spouse dies before distributions were required to begin to the spouse, the surviving spouse is treated as the employee (or IRA owner) in determining the required distributions to beneficiaries of the surviving spouse.

Definitions of disabled and chronically ill individual

Under the provision, disabled means unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to end in death or to be for long-continued and indefinite duration.[225] Further, under the definition, an individual is not considered to be disabled unless proof of the disability is furnished in such form and manner as the Secretary may require. Substantial gainful activity for this purpose is the activity, or a comparable activity, in which the individual customarily engaged prior to the arising of the disability (or prior to retirement if the individual was retired at the time the disability arose).[226]

Under the provision, the definition of a chronically ill individual for purposes of qualified long-term care insurance[227] is incorporated by reference with a modification. Under this definition, a chronically ill individual is any individual who (1) is unable to perform (without substantial assistance from another individual) at least two activities of daily living for an indefinite period (expected to be lengthy in nature)[228] due to a loss of functional capacity, (2) has a level of disability similar (as determined under regulations prescribed by the Secretary in consultation with the Secretary of Health and Human Services) to the level of disability described above requiring assistance with daily living based on loss of functional capacity, or (3) requires substantial supervision to protect the individual from threats to health and safety due to severe cognitive impairment. The activities of daily living for which assistance is needed for purposes of determining loss of functional capacity are eating, toileting, transferring, bathing, dressing, and continence.

Annuity payments under commercial annuities

The provision applies to after-death required minimum distributions under defined contribution plans and IRAs, including annuity contracts purchased from insurance companies under defined contribution plans or IRAs.

EFFECTIVE DATE

General effective date

In determining required minimum distributions after the death of an employee (or IRA owner), the provision is generally effective for required minimum distributions with respect to employees (or IRA owners) with a date of death after December 31, 2016.

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[225] The definition of disabled in section 72(m)(7) is incorporated by reference.

[226] Treas. Reg. sec. 1.72–17(f). Under the regulations, in determining whether an individual is disabled, primary consideration is given to the nature and severity of the individual's impairment. However, consideration is also given to other factors such as the individual's education, training, and work experience. Whether an impairment in a particular case constitutes a disability is determined with reference to all the facts in the case.

[227] Sec. 7702B(c)(2).

[228] Section 7702B(c) only requires this period to be at least 90 days.

Delayed effective date for governmental and collectively bargained plans

In the case of a governmental plan (as defined in section 414(d)), in determining required minimum distributions after the death of an employee, the provision applies to distributions with respect to employees who die after December 31, 2018.

In the case of a collectively bargained plan,[229] in determining required minimum distributions after the death of an employee, the provision applies to distributions with respect to employees who die in calendar years beginning after the earlier of two dates. The first date is the later of (1) the date on which the last collective bargaining agreement ratified before date of enactment of the provision terminates,[230] or (2) December 31, 2016. The second date is December 31, 2018.

Five-year rule after the death of a beneficiary

In the case of an employee (or IRA owner) who dies before the effective date (as described below) for the plan (or IRA), if the designated beneficiary of the employee (or IRA owner) dies on or after the effective date, the provision applies to any beneficiary of the designated beneficiary as though the designated beneficiary were an eligible beneficiary. Thus, the entire interest must be distributed by the end of the fifth calendar year after the death of the designated beneficiary. For this purpose, the effective date is the date of death of the employee (or IRA owner) used to determine when the provision applies to the plan (or IRA), for example, before January 1, 2017, under the general effective date.

Certain annuities grandfathered

The modification to the after-death minimum distribution rules does not apply to a qualified annuity that is a binding annuity contract in effect on the date of enactment of the provision and at all times thereafter. A qualified annuity with respect to an individual is a commercial annuity,[231] under which the annuity payments are made over the lives of the individual and a designated beneficiary (or over a period not extending beyond the life expectancy of the individual or the life expectancy of the individual and a designated beneficiary) in accordance with the required minimum distribution regulations for annuity payments as in effect before enactment of this proposal. In addition to these requirements, annuity payments to the individual must begin before the date of enactment, and the individual must have made an irrevocable election before that date as to the method and amount of the annuity payments to the individual or any designated beneficiaries. Alternatively, if an annuity is not a qualified annuity solely based on annuity payments not having begun irrevocably before the date of enactment, an annuity can be a qualified annuity if the individual has made an irrevocable election before the date of enactment as to the method and

[229] A collectively bargained plan is a plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers.

[230] The date that the last agreement terminates is determined without regard to any extension thereof agreed to on or after the date of enactment of the provision. Further, any plan amendment made pursuant to a collective bargaining agreement relating to the plan that amends the plan solely to conform to any requirement added by the provision shall not be treated as a termination of the collective bargaining agreement.

[231] For this purpose, commercial annuity is defined in section 3405(e)(6).

amount of the annuity payments to the individual or any designated beneficiaries.

Plan amendments made pursuant to the provision

A plan amendment made pursuant to the provision (or regulations issued thereunder) may be retroactively effective and (except as provided by the Secretary) will not violate the anti-cut-back rule, if, in addition to meeting the other applicable requirements described below, the amendment is made on or before the last day of the first plan year beginning after December 31, 2018 (or in the case of a governmental or collectively bargained plan, December 31, 2020), or a later date prescribed by the Secretary. In addition, the plan will be treated as operated in accordance with plan terms during the period beginning with the date of the provision or regulations take effect (or the date specified by the plan if the amendment is not required by the provision or regulations) and ending on the last permissible date for the amendment (or, if earlier, the date the amendment is adopted).

A plan amendment will not be considered to be pursuant to the provision (or applicable regulations) if it has an effective date before the effective date of the provision under the provision (or regulations) to which it relates. Similarly, the provision does not provide relief from the anti-cut-back rule for periods prior to the effective date of the relevant portion of the provision (or regulations) or the plan amendment. In order for an amendment to be retroactively effective and not violate the anti-cut-back rule, the plan amendment must apply retroactively for the period described in the preceding paragraph, and the plan must be operated in accordance with the amendment during that period.

B. INCREASE IN PENALTY FOR FAILURE TO FILE (SEC. 502 OF THE BILL AND SEC. 6651(a) OF THE CODE)

PRESENT LAW

The Federal tax system is one of "self-assessment," *i.e.,* taxpayers are required to declare their income, expenses, and ultimate tax due, while the IRS has the ability to propose subsequent changes. This voluntary system requires that taxpayers comply with deadlines and adhere to the filing requirements. While taxpayers may obtain extensions of time in which to file their returns, the Federal tax system consists of specific due dates of returns. In order to foster compliance in meeting these deadlines, Congress has enacted a penalty for the failure to timely file tax returns.[232]

A taxpayer who fails to file a tax return on or before its due date is subject to a penalty equal to five percent of the net amount of tax due for each month that the return is not filed, up to a maximum of 25 percent of the net amount.[233] If the failure to file a return is fraudulent, the taxpayer is subject to a penalty equal to 15 percent of the net amount of tax due for each month the return is not filed, up to a maximum of 75 percent of the net amount.[234] The net amount of tax due is the amount of tax required to be shown on the return reduced by the amount of any part of the tax which

[232] See *United States v. Boyle,* 469 U.S. 241, 245 (1985).
[233] Sec. 6651(a)(1).
[234] Sec. 6651(f).

is paid on or before the date prescribed for payment of the tax and by the amount of any credits against tax which may be claimed on the return.[235] The penalty will not apply if it is shown that the failure to file was due to reasonable cause and not willful neglect.[236]

If a return is filed more than 60 days after its due date, and unless it is shown that such failure is due to reasonable cause, then the failure to file penalty may not be less than the lesser of $205 or 100 percent of the amount required to be shown as tax on the return. If a penalty for failure to file and a penalty for failure to pay tax shown on a return both apply for the same month, the amount of the penalty for failure to file for such month is reduced by the amount of the penalty for failure to pay tax shown on a return.[237] If a return is filed more than 60 days after its due date, then the penalty for failure to pay tax shown on a return may not reduce the penalty for failure to file below the lesser of $205 or 100 percent of the amount required to be shown on the return.[238]

The failure to file penalty applies to all returns required to be filed under subchapter A of Chapter 61 (relating to income tax returns of an individual, fiduciary of an estate or trust, or corporation; self-employment tax returns, and estate and gift tax returns), subchapter A of chapter 51 (relating to distilled spirits, wines, and beer), subchapter A of chapter 52 (relating to tobacco, cigars, cigarettes, and cigarette papers and tubes), and subchapter A of chapter 53 (relating to machine guns and certain other firearms).[239] The failure to file penalty is adjusted annually to account for inflation. The failure to file penalty does not apply to any failure to pay estimated tax required to be paid by sections 6654 or 6655.[240]

REASONS FOR CHANGE

The Committee believes the present law penalties are too low to discourage noncompliance. The Committee believes that increasing the penalties will encourage the filing of timely and accurate returns which, in turn, will improve overall tax administration.

EXPLANATION OF PROVISION

Under the provision, if a return is filed more than 60 days after its due date, then the failure to file penalty may not be less than the lesser of $400 or 100 percent of the amount required to be shown as tax on the return.

EFFECTIVE DATE

The provision applies to returns with filing due dates (including extensions) after December 31, 2016.

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[235] Sec. 6651(b)(1).
[236] Sec. 6651(a)(1).
[237] Sec. 6651(c)(1).
[238] *Ibid.*
[239] Sec. 6651(a)(1).
[240] Sec. 6651(e).

C. Increased Penalties for Failure To File Retirement Plan Returns (sec. 503 of the bill and sec. 6652(d), (e), and (h) of the Code)

PRESENT LAW

Form 5500

An employer that maintains a pension, annuity, stock bonus, profit-sharing or other funded deferred compensation plan (or the plan administrator of the plan) is required to file an annual return containing information required under regulations with respect to the qualification, financial condition, and operation of the plan.[241] The plan administrator of a defined benefit plan subject to the minimum funding requirements[242] is required to file an annual actuarial report.[243] These filing requirements are met by filing an Annual Return/Report of Employee Benefit Plan, Form 5500 series, and providing the information as required on the form and related instructions.[244] A failure to file Form 5500 generally results in a civil penalty of $25 for each day during which the failure continues, subject to a maximum penalty of $15,000.[245] This penalty may be waived if it is shown that the failure is due to reasonable cause.

Annual registration statement and notification of changes

In the case of a plan subject to the vesting requirements under the Employee Retirement Income Security Act of 1974 ("ERISA"), the plan administrator is required to file a registration statement with the IRS with respect to any plan participant who (1) separated from service during the year and (2) has a vested benefit under the plan, but who was not paid the benefit during the year (a "deferred vested" benefit).[246] The registration statement must include the name of the plan, the name and address of the plan administrator, the name and taxpayer identification number of the separated participant, and the nature, amount, and form of the participant's deferred vested benefit. A failure to file a registration statement as required generally results in a civil penalty of $1 for each participant with respect to whom the failure applies, multiplied by the number of days during which the failure continues, subject to a maximum penalty of $5,000 for a failure with respect to any plan year.[247] This penalty may be waived if it is shown that the failure is due to reasonable cause.

A plan administrator is also required to notify the IRS if certain information in a registration changes, specifically, any change in the name of the plan or in the name or address of the plan administrator, the termination of the plan, or the merger or consolidation of the plan with any other plan or its division into two or more plans. A failure to file a required notification of change generally

[241] Sec. 6058.
[242] Sec. 412. Most governmental plans (defined in section 414(d)) and church plans (defined in section 414(e)) are exempt from the minimum funding requirements.
[243] Sec. 6059.
[244] Treas. Reg. secs. 301.6058–1(a) and 301.6059–1.
[245] Sec. 6652(e). The failure to file penalties in section 6652 generally apply to certain information returns, including retirement plan returns. The failure to file penalties in section 6651(a)(1), discussed above in section 502 of the bill, generally apply to income, estate, gift, employment and self-employment, and certain excise tax returns.
[246] Code sec. 6057(a). Under Code section 6057(e) and ERISA section 105(c), similar information must be provided to the separated participant.
[247] Sec. 6652(d)(1).

results in a penalty of $1 for each day during which the failure continues, subject to a maximum penalty of $1,000 for any failure.[248] This penalty may be waived if it is shown that the failure is due to reasonable cause.

Withholding notices

Withholding requirements apply to distributions from tax-favored employer-sponsored retirement plans and IRAs, but, except in the case of certain distributions, payees may generally elect not to have withholding apply.[249] A plan administrator or IRA custodian is required to provide payees with notices of the right to elect no withholding. A failure to provide a required notice generally results in a civil penalty of $10 for each failure, subject to a maximum penalty of $5,000 for all failures during any calendar year.[250] This penalty may be waived if it is shown that the failure is due to reasonable cause and not to willful neglect.

REASONS FOR CHANGE

The Committee notes that the penalties for failing to file certain retirement plan returns and statements or provide certain notices have not been increased in many years. The Committee believes the present law penalties are too low to discourage noncompliance. The Committee believes that increasing these penalties will encourage the filing of timely and accurate information returns and statements and the provision of required notices, which, in turn, will improve overall tax administration.

EXPLANATION OF PROVISION

Form 5500

Under the provision, a failure to file Form 5500 generally results in a penalty of $100 for each day during which the failure continues, subject to a maximum but the total amount imposed under this subsection on any person for failure to file any return shall not exceed $50,000.

Annual registration statement and notification of changes

Under the provision, a failure to file a registration statement as required generally results in a penalty of $2 for each participant with respect to whom the failure applies, multiplied by the number of days during which the failure continues, subject to a maximum penalty of $10,000 for a failure with respect to any plan year. A failure to file a required notification of change generally results in a penalty of $2 for each day during which the failure continues, subject to a maximum penalty of $5,000 for any failure.

Withholding notices

Under the provision, a failure to provide a required withholding notice generally results in a penalty of $100 for each failure, subject to a maximum penalty of $50,000 for all failures during any calendar year.

[248] Sec. 6652(d)(2).
[249] Sec. 3405.
[250] Sec. 6652(h).

EFFECTIVE DATE

The provision is effective for returns, statements and notifications required to be filed, and withholding notices required to be provided, in calendar years beginning after December 31, 2016.

D. Modification of User Fee Requirements for Installment Agreements (sec. 504 of the bill and sec. 6159 of the Code)

PRESENT LAW

The Code authorizes the IRS to enter into written agreements with any taxpayer under which the taxpayer agrees to pay taxes owed, as well as interest and penalties, in installments over an agreed schedule, if the IRS determines that doing so will facilitate collection of the amounts owed.[251] This agreement provides for a period during which IRS enforcement actions are held in abeyance while payments are made.[252] An installment agreement generally does not reduce the amount of taxes, interest, or penalties owed. However, the IRS is authorized to enter into installment agreements with taxpayers which do not provide for full payment of the taxpayer's liability over the life of the agreement. The IRS is required to review such partial payment installment agreements at least every two years to determine whether the financial condition of the taxpayer has significantly changed so as to warrant an increase in the value of the payments being made.

Taxpayers can request an installment agreement by filing Form 9465, Installment Agreement Request.[253] If the request for an installment agreement is approved by the IRS, the IRS charges a user fee.[254] Under sections 300.1 and 300.2 of the Treasury Regulations, the IRS currently charges $120 for entering into an installment agreement.[255] If the application is for a direct debit installment agreement, whereby the taxpayer authorizes the IRS to request the monthly electronic transfer of funds from the taxpayer's bank account to the IRS, the fee is reduced to $52. In addition, regardless of the method of payment, the fee is $43 for low-income taxpayers. For this purpose, low-income is defined as a person who falls below 250 percent of the Federal poverty guidelines published annually. Finally, there is no user fee if the agreement is for a term of 120 days or less (i.e., a short-term agreement).

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[251] Sec. 6159.

[252] Sec. 6331(k).

[253] The IRS accepts applications for installment agreements online, from individuals and businesses, if the total tax, penalties and interest is below $50,000 for the former, and $25,000 for the latter.

[254] 31 U.S.C. sec. 9701; Treas. Reg. sec. 300.1. The Independent Offices Appropriations Act of 1952 (IOAA), 65 Stat. B70, (June 27, 1951). A discussion of the IRS practice regarding user fees and a list of actions for which fees are charged is included in the Internal Revenue Manual. See "User Fees," paragraph 1.32.19 IRM, available at *https://www.irs.gov/irm/part1/irm_*01-032-019.html.

[255] On August 22, 2016, Treasury issued proposed changes to the schedule of user fees for installment agreements, effective January 2017, based on a biennial review of the costs of administering the program. *https://www.irs.gov/uac/irs-proposes-revised-fees-for-installment-agreements.* If finalized, the revised schedule imposes user fees in the following amounts: $225 for a regular installment agreement; $107 for a regular direct debit installment agreement; $149 for online payment agreement; $31 for a direct debit online payment agreement; $89 for a restructured or reinstated agreement; and $43 for an agreement with a low-income taxpayer.

REASONS FOR CHANGE

The Committee believes user fees are a barrier to compliance in collection and discourage low-income taxpayers from voluntary tax compliance, as many of them do not have the means to pay the user fee, even at the reduced rate. Further, when negotiating installment agreements, many low-income taxpayers are charged the full user fee, despite qualifying for the reduced amount.[256]

EXPLANATION OF PROVISION

The provision generally prohibits increases in the amount of user fees charged by the IRS for installment agreements. For low-income taxpayers (those whose adjusted gross income, as determined for the most recent year for which such information is available, does not exceed 250 percent of the applicable poverty level as determined by the Secretary), it alleviates the user fee requirement in two ways. First, it waives the user fee if the low-income taxpayer enters into an installment agreement under which the taxpayer agrees to make automated installment payments through a debit account. Second, it provides that low-income taxpayers who are unable to make payments electronically remain subject to the required user fee, but the fee is reimbursed upon completion of the installment agreement.

EFFECTIVE DATE

The provision applies to agreements entered into on or after the date that is 60 days after the date of enactment.

E. INCREASE INFORMATION SHARING TO ADMINISTER EXCISE TAXES (SEC. 505 OF THE BILL AND SEC. 6103(o) OF THE CODE)

PRESENT LAW

Generally, tax returns and return information ("tax information") are confidential and may not be disclosed unless authorized in the Code.[257] Return information includes data received, collected or prepared by the Secretary with respect to the determination of the existence or possible existence of liability of any person under the Code for any tax, penalty, interest, fine, forfeiture, or other imposition or offense. Criminal penalties apply for the unauthorized inspection or disclosure of tax information. Willful unauthorized disclosure is a felony under section 7213 and the willful unauthorized inspection of tax information is a misdemeanor under section 7213A. Taxpayers may also pursue a civil cause of action for disclosures and inspections not authorized by section 6103.[258]

Section 6103 provides exceptions to the general rule of confidentiality, detailing permissible disclosures. Under section 6103(h)(1), tax information is open to inspection by or disclosure to Treasury officers and employees whose official duties require the inspection or disclosure for tax administration purposes.

[256] See American Bar Association letter to Mr. Daniel Werfel, Acting Commissioner, IRS, "Comments Concerning User Fees for Processing Installment Agreements and Offers in Compromise," October 1, 2013, page 2, available at *http://www.americanbar.org/content/dam/aba/administrative/taxation/policy/100113comments.authcheckdam.pdf.*

[257] Sec. 6103(a).

[258] Sec. 7431.

The heavy vehicle use tax, an annual highway use tax, is imposed on the use of any highway motor vehicle that has a gross weight of 55,000 pounds or more.[259] Proof of payment of the heavy vehicle use tax must be presented to customs officials upon entry into the United States of any highway motor vehicle subject to the tax and that has a base in a contiguous foreign country.[260] If the operator of the vehicle is unable to present proof of payment of the tax with respect to the vehicle, entry into the United States may be denied.[261]

Prior to 2003, customs officials who had responsibility for enforcing and/or collecting excise taxes were employees of the U.S. Department of the Treasury ("Treasury"). Thus, prior to 2003, section 6103(h)(1) allowed disclosure of tax information by the IRS to these customs officials in the performance of their duties. In 2003, U.S. Customs and Border Protection became an official agency of the U.S. Department of Homeland Security.[262] At that time, customs officials were transferred from Treasury to the Department of Homeland Security.

REASONS FOR CHANGE

Allowing limited disclosures of tax information will facilitate tax administration and improve compliance with the heavy vehicle use tax by allowing customs officials to confirm payment or nonpayment of the tax.

EXPLANATION OF PROVISION

The provision allows the IRS to share returns and return information with employees of U.S. Customs and Border Protection whose official duties require such inspection or disclosure for purposes of administering and collecting the heavy vehicle use tax.

EFFECTIVE DATE

The provision is effective for disclosures made on or after the date of enactment.

F. REPEAL OF PARTNERSHIP TECHNICAL TERMINATIONS (SEC. 506 OF THE BILL AND SEC. 708(b)(1)(B) OF THE CODE)

PRESENT LAW

Present law provides that a partnership is considered as terminated under specified circumstances.[263] Present law also provides rules for the merger, consolidation, or division of a partnership.[264]

A partnership is considered as terminated if no part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership.[265]

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[259] Sec. 4481(a).
[260] Treas. Reg. 41.6001–3(a).
[261] Treas. Reg. 41.6001–3(b).
[262] The Homeland Security Act of 2002, Pub. L. No. 107–296 ("Homeland Security Act"), enacted November 25, 2002 established the U.S. Department of Homeland Security. Several agencies were combined under this new department.
[263] Sec. 708(b)(1).
[264] Sec. 708(b)(2). Mergers, consolidations, and divisions of partnerships take either an assets-over form or an assets-up form pursuant to Treas. Reg. sec. 1.708–1(c).
[265] Sec. 708(b)(1)(A).

A partnership is also considered as terminated if within any 12-month period, there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits.[266] This is sometimes referred to as a technical termination. Under regulations, the technical termination gives rise to a deemed contribution of all the partnership's assets and liabilities to a new partnership in exchange for an interest in the new partnership, followed by a deemed distribution of interests in the new partnership to the purchasing partners and the other remaining partners.[267]

The effect of a technical termination is the termination of the old partnership and the formation of a new partnership. As a result of a technical termination, some of the tax attributes of the old partnership terminate. Upon a technical termination, the partnership's taxable year closes, potentially resulting in short taxable years.[268] Partnership-level elections generally cease to apply following a technical termination.[269] A technical termination generally results in the restart of partnership depreciation recovery periods.[270]

REASONS FOR CHANGE

The Committee is concerned that the present-law rule providing for technical terminations of partnerships has become both a trap for the unwary and a tool subject to manipulation for the well-advised. This is because its effects on partnership-level tax attributes such as elections, depreciation periods, and closing of the partnership taxable year can be either unanticipated by the unwary, or planned by the well-advised, in the event of a sale or exchange of partnership interests. Further, well-advised taxpayers may avoid the effects of a technical termination by structuring transactions as something other than a sale or exchange of the requisite percentage of partnership interests in profits and capital in a 12-month period. The Committee believes that tax policy or tax administrability purposes served by the partnership technical termination rule are outweighed by these disadvantages, and therefore, the bill repeals the technical termination rule.

EXPLANATION OF PROVISION

The provision repeals the section 708(b)(1)(B) rule providing for technical terminations of partnerships.

The provision does not change the present-law rule of section 708(b)(1)(A) that a partnership is considered as terminated if no part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership.

[266] Sec. 708(b)(1)(B).

[267] Treas. Reg. sec. 1.708–1(b)(4).

[268] Sec. 706(c)(1); Treas. Reg. sec. 1.708–1(b)(3).

[269] Partnership level elections include, for example, the section 754 election to adjust basis on a transfer or distribution, as well as other elections that determine the partnership's tax treatment of partnership items. A list of elections can be found at William S. McKee, William F. Nelson, and Robert L. Whitmire, Federal Taxation of Partnerships and Partners, 4th edition, para. 9.01[7], pp. 9–42—9–44.

[270] Although section 168(i)(7) provides that for purposes of computing the depreciation deduction, generally the transferee partnership is treated as the transferor when property is contributed in a tax-free transaction governed by section 721, it further provides that this rule does not apply in the case of a technical termination. Thus, the deemed contribution under Treas. Reg. sec. 1.708–1(b)(4) may have the result of restarting depreciation periods applying the current adjusted basis of the property deemed contributed.

EFFECTIVE DATE

The provision applies to periods beginning after December 31, 2016. A transition rule provides that in the case of a period beginning before January 1, 2017, the present-law partnership technical termination rule applies without regard to any sale or exchange after December 31, 2016.

G. PENSION PLAN ACCELERATION OF PBGC PREMIUM PAYMENT (SEC. 507 OF THE BILL AND SEC. 4007 OF ERISA)

PRESENT LAW

Private defined benefit plans are covered by the Pension Benefit Guaranty Corporation ("PBGC") insurance program, under which the PBGC guarantees the payment of certain plan benefits, and plans are required to pay annual premiums to the PBGC.[271] PBGC premiums consist of a per-participant premium (referred to as "flat-rate" premiums) and, in the case of single-employer and multiple-employer plans, additional premiums (referred to as "variable-rate" premiums) based on the amount by which the present value of vested benefits under the plan exceeds the value of plan assets.

PBGC premiums for a plan year are generally due by a date within that plan year (referred to as the "premium payment year"). In general, premiums are due by the fifteenth day of the tenth calendar month that begins on or after the first day of the premium payment year.[272]

REASONS FOR CHANGE

The Committee believes that accelerating the due date of certain variable-rate premiums will strengthen the financial status of the PBGC insurance program.

EXPLANATION OF PROVISION

Under the provision, variable-rate premiums for which the due date under present law occurs during the period October 1, 2026, through November 30, 2026, must be paid by September 30, 2026.

Effective Date The provision is effective on the date of enactment.

III. BUDGET EFFECTS OF THE BILL

A. COMMITTEE ESTIMATES

In compliance with paragraph 11(a) of rule XXVI of the Standing Rules of the Senate and section 308(a)(1) of the Congressional Budget and Impoundment Control Act of 1974, as amended (the "Budget Act"), the following statement is made concerning the estimated budget effects of the revenue provisions of the Retirement Enhancement and Savings Act of 2016, as reported.

The bill is estimated to have the following effects on Federal budget receipts for fiscal years 2017–2026:

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[271] Title IV of ERISA.

[272] 29 C.F.R. sec. 4007.11(a). Under section 502 of the Bipartisan Budget Act of 2015, Pub. L. No. 114–74, premiums for plan years beginning in 2025 (that is, plan years beginning after December 31, 2024, and before January 1, 2026) are due by the fifteenth day of the ninth calendar month that begins on or after the first day of the premium payment year.

ESTIMATED BUDGET EFFECTS OF
THE "RETIREMENT ENHANCEMENT AND SAVINGS ACT OF 2016,"
AS REPORTED BY THE COMMITTEE ON FINANCE

Fiscal Years 2017 - 2026

[Millions of Dollars]

Provision	Effective	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2017-21	2017-26
I. Expanding and Preserving Retirement Savings													
A. Multiple Employer Plans and Pooled Employer and Multiple-Employer Plan Reporting [1]	yba 12/31/19 & pyba 12/31/19	---	-9	-18	-71	-183	-298	-430	-574	-722	-874	-281	-3,179
B. Removal of 10-Percent Cap from Automatic Enrollment Safe Harbor After First Plan Year	pyba 12/31/16	*Negligible Revenue Effect*											
C. Rules Relating to Election of Safe Harbor 401(k) Status	pyba 12/31/16	*Negligible Revenue Effect*											
D. Increase in Credit Limitation for Small Employer Plan Start-Up Costs	tyba 12/31/16	-1	-2	-2	-2	-2	-3	-3	-3	-3	-3	-11	-24
E. Small Employer Automatic Enrollment Credit	tyba 12/31/16	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	-1
F. Certain Taxable Non-Tuition Fellowship and Stipend Payments Treated as Compensation for IRA Purposes	tyba 12/31/16	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	-2
G. Repeal Maximum Age for Traditional IRA Contributions	cmf tyba 12/31/16	-3	-4	-5	-5	-6	-6	-7	-7	-8	-8	-23	-58
H. Expansion of IRA Ownership of S Corporation Bank Stock	1/1/16	-10	-17	-18	-19	-20	-21	-22	-22	-24	-25	-85	-198
I. Extended Rollover Period for Plan Loan Offset Amounts	loi tyba 12/31/16	*Negligible Revenue Effect*											
J. Modification of Rules Relating to Hardship Withdrawals from Cash or Deferred Arrangements	pyba 12/31/16	77	148	174	164	139	105	61	6	-55	-113	702	706
K. Qualified Employer Plans Prohibited from Making Loans Through Credit Cards and Other Similar Arrangements	pyba 12/31/16	*Negligible Revenue Effect*											
L. Portability of Lifetime Income Options	pyba 12/31/16	*Negligible Revenue Effect*											
M. Treatment of Custodial Accounts on Termination of Section 403(b) Plans	ptoa 12/31/16	*Negligible Revenue Effect*											
N. Clarification of Retirement Income Account Rules Relating to Church-Controlled Organizations	ybbo/a DOE	*Negligible Revenue Effect*											
Total of Expanding and Preserving Retirement Savings		**63**	**116**	**131**	**67**	**-72**	**-223**	**-401**	**-600**	**-812**	**-1,023**	**302**	**-2,756**
II. Administrative Improvements													
A. Plan Adopted by Filing Due Date for Year May Be Treated as in Effect as of Close of Year	paf tyba 12/31/16	-10	-11	-12	-12	-13	-15	-16	-17	-18	-19	-58	-142
B. Combined Annual Report for Group of Plans	ararf pyba 12/31/19	*Negligible Revenue Effect*											
C. Disclosure Regarding Lifetime Income [3]	[4]	*No Budget Effect*											

Provision	Effective	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2017-21	2017-26
D. Fiduciary Safe Harbor for Selection of Lifetime Income Provider [3]	DOE	No Budget Effect											
E. Modification of Nondiscrimination Rules to Protect Older, Longer Service Participation	generally DOE	Negligible Revenue Effect											
F. Modification of PBGC Premiums for Cooperative and Small Employer Charity ("CSEC") Plans [3][5]	pyba 12/31/15	-92	-96	-101	-106	-108	-109	-107	-100	-94	-92	-502	-1,004
Total of Administrative Improvements		**-102**	**-107**	**-113**	**-118**	**-121**	**-124**	**-123**	**-117**	**-112**	**-111**	**-560**	**-1,146**
III. Benefits Relating to the United States Tax Court [6][7]	**generally DOE**	**-2**	**[2]**	**[2]**	**[2]**	**[2]**	**[2]**	**[2]**	**[2]**	**[2]**	**[2]**	**-2**	**-4**
IV. Other Benefits													
A. Benefits for Volunteer Firefighters and Emergency Medical Responders (sunset 12/31/17)	tyba 12/31/16	-82	-27	---	---	---	---	---	---	---	---	-109	-109
B. Treatment of Qualified Equity Grants	[8]	-114	-158	-164	-157	-129	-71	-48	-30	-13	-10	-723	-894
Total of Other Benefits		**-196**	**-185**	**-164**	**-157**	**-129**	**-71**	**-48**	**-30**	**-13**	**-10**	**-832**	**-1,003**
V. Revenue Provisions													
A. Modifications to Required Minimum Distribution Rules	[9]	[10]	20	76	149	254	463	544	578	559	538	499	3,182
B. Increase in Penalty for Failure to File	rwfddiea 12/31/16	5	23	23	24	25	25	26	27	28	29	100	235
C. Increased Penalties for Failure to File Retirement Plan Returns	[11]	[10]	6	12	13	13	13	14	14	14	14	44	113
D. Modification of User Fee Requirements for Installment Agreements	aeiooatdti 60da DOE	1	2	3	5	6	6	6	6	6	7	17	49
E. Increase Information Sharing to Administer Excise Taxes	dmo/a DOE	3	8	14	15	16	17	18	19	19	20	56	150
F. Repeal of Partnership Technical Terminations	pba 12/31/16	10	17	20	21	22	23	24	25	28	30	90	220
G. Acceleration of PBGC Premium Payment [3][12]	DOE	---	---	---	---	---	---	---	---	---	1,007	---	1,007
Total of Revenue Provisions		**19**	**76**	**148**	**227**	**336**	**547**	**632**	**669**	**654**	**1,645**	**806**	**4,956**
NET TOTAL		**-218**	**-100**	**2**	**19**	**14**	**129**	**60**	**-78**	**-283**	**501**	**-286**	**47**

Joint Committee on Taxation

NOTE: Details may not add to totals due to rounding.

Legend for "Effective" column:

aeiooatdti = agreements entered into on or after the date that is
ararf = annual returns and reports for
cmf = contributions made for
dmo/a = disclosures made on or after
DOE = date of enactment

loi = loans offset in
paf = plans adopted for
pba = periods beginning after
pyba = plan years beginning after
ptoa = plan terminations occurring after

rwfddiea = returns with filing due dates (including extensions) after
tyba = taxable years beginning after
yba = years beginning after
ybbo/a = years beginning before, on, or after
60da = 60 days after

[Footnotes for the Table appear on the following page]

Footnotes for the Table:

[1] Estimate includes the following budget effects:

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2017-21	2017-26
Total Revenue Effects	---	-9	-18	-71	-183	-298	-430	-574	-722	-874	-281	-3,179
On-budget effects	---	-8	-16	-66	-170	-277	-399	-533	-671	-813	-260	-2,953
Off-budget effects	---	-1	-1	-5	-13	-22	-31	-41	-51	-61	-21	-227

[2] Loss of less than $500,000.

[3] Estimate provided by the Congressional Budget Office.

[4] Effective with respect to benefit statements provided more than 12 months after the latest of the issuance by the Secretary of Labor (1) interim final rules, (2) the model disclosure, or (3) prescribed assumptions.

[5] Estimate includes the following outlay effects [3]:

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2017-21	2017-26
outlay effects [3]	92	96	101	106	108	109	107	100	94	92	502	1,004

[6] Estimate provided by the Joint Committee on Taxation and the Congressional Budget Office.

[7] Estimate includes the following outlay effects [3]:

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2017-21	2017-26
effects [3]	2	[10]	[10]	[10]	[10]	[10]	[10]	[10]	[10]	[10]	2	4

[8] Generally effective with respect to stock attributable to options exercised or RSUs settled after December 31, 2016. The penalty for a failure to provide the notice required under the proposal applies to failures after December 31, 2016.

[9] Generally effective for required minimum distributions with respect to employees (or IRA owners) with a date of death after December 31, 2016.

[10] Gain of less than $500,000.

[11] Effective for returns, statements and notifications required to be filed, and withholding notices required to be provided, in calendar years beginning after December 31, 2016.

[12] Estimate includes the following outlay effects [3]:

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2017-21	2017-26
outlay effects [3]	---	---	---	---	---	---	---	---	---	-1,007	---	-1,007

B. Budget Authority and Tax Expenditures

Budget authority

In compliance with section 308(a)(1) of the Budget Act, the Committee states that the provisions of the bill relating to the Tax Court and PBGC premiums for CSEC plans involve new or increased budget authority.

Tax expenditures

In compliance with section 308(a)(1) of the Budget Act, the Committee states that certain provisions affect the levels of tax expenditures, as shown in the revenue table in Part A.

C. Consultation With Congressional Budget Office

In accordance with section 403 of the Budget Act, the Committee advises that the Congressional Budget Office has not submitted a statement on the bill. The statement from the Congressional Budget Office will be provided separately.

IV. VOTES OF THE COMMITTEE

In compliance with paragraph 7(b) of rule XXVI of the Standing Rules of the Senate, the Committee states that, with a majority present, the Retirement Enhancement and Savings Act of 2016, was ordered favorably reported on September 21, 2016, by a roll call vote of 26 ayes and 0 nays. The vote was as follows:

Ayes: Hatch, Grassley, Crapo, Roberts, Enzi, Cornyn, Thune (proxy), Burr (proxy), Isakson, Portman, Toomey (proxy), Coats, Heller, Scott, Wyden, Schumer, Stabenow, Cantwell, Nelson, Menendez, Carper, Cardin, Brown, Bennet, Casey, Warner.

V. REGULATORY IMPACT AND OTHER MATTERS

A. Regulatory Impact

Pursuant to paragraph 11(b) of rule XXVI of the Standing Rules of the Senate, the Committee makes the following statement concerning the regulatory impact that might be incurred in carrying out the provisions of the bill.

Impact on individuals and businesses and personal privacy

The bill includes various provisions relating to tax-favored retirement savings, including provisions designed to expand access to employer-sponsored plans and IRAs, to encourage greater participation in tax-favored arrangement, to preserve funds held in tax-favored form, and to help ensure that savings are sufficient to last through retirement. The bill also contains provisions relating to the U.S. Tax Court, benefits provided to emergency services volunteers, stock-based compensation provided to employees of closely held businesses, and tax compliance. Some provisions may involve additional record-keeping or reporting by individuals or businesses wishing to avail themselves of favorable tax treatment. A number of the provisions in the bill are designed to reduce the administrative burdens associated with tax-favored savings and other employee benefits.

The provisions of the bill do not impact personal privacy.

B. Unfunded Mandates Statement

This information is provided in accordance with section 423 of the Unfunded Mandates Reform Act of 1995 (Pub. L. No. 104–4).

The Committee has determined that the revenue provisions of the bill do not impose any Federal private sector or intergovernmental mandates on State, local, or tribal governments within the meaning of the Unfunded Mandates Reform Act of 1995.

C. Tax Complexity Analysis

Section 4022(b) of the Internal Revenue Service Reform and Restructuring Act of 1998 ("IRS Reform Act") requires the staff of the Joint Committee on Taxation (in consultation with the Internal Revenue Service and the Treasury Department) to provide a tax complexity analysis. The complexity analysis is required for all legislation reported by the Senate Committee on Finance, the House Committee on Ways and Means, or any committee of conference if the legislation includes a provision that directly or indirectly amends the Internal Revenue Code and has widespread applicability to individuals or small businesses. The staff of the Joint Committee on Taxation has determined that there are no provisions that are of widespread applicability to individuals or small businesses.

VI. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In the opinion of the Committee, it is necessary in order to expedite the business of the Senate, to dispense with the requirements of paragraph 12 of Rule XXVI of the Standing Rules of the Senate (relating to the showing of changes in existing law made by the bill as reported by the Committee).