
'Rothification is a Stupid Idea'

By Kerry Pechter Thu, Sep 28, 2017

During a panel discussion at the IRI conference, former Treasury official Seth Harris, Voya's Sean Cassidy and former Oklahoma congressman J.C. Watts shared strong opinions about tax reform, the DOL fiduciary rule and Donald Trump.



Donald Trump's tax cut plan, or rather a sketch for a draft of one, became public yesterday. It included a brief reassurance that tax incentives for retirement savings would not be sacrificed to pay for the cuts, but didn't contain specifics on that topic.

Two days earlier, at the Insured Retirement Institute conference in Palm Beach on Monday, a panel of Washington veterans discussed the issues that preoccupy the thoughts of many of the annuity manufacturers and distributors who attended the meeting.

They worry that the administration might try to pay for tax relief for corporations and wealthy individuals by making the tax treatment of contributions to (and growth in) retirement plan accounts more like the treatment of Roth accounts. Income tax on contributions to traditional retirement accounts can be deferred until age 70½. Contributions to Roth accounts are taxable but withdrawals are generally not taxed.

The retirement industry opposes that shift, as did members of the panel at the IRI conference.

"Rothification is a stupid idea that will not die," said Seth Harris, an ex-deputy Secretary of Labor in the Obama administration. "It's bad policy that's there just to fund a corporate tax cut. The tax cut will have to be paid for, and the other pay-fors are just as ugly. But the Roth 401(k) is a horrible idea."

Another panelist, Sean Cassidy, vice president of federal government affairs for Voya Financial, described one possible scenario.

"We're looking at the potential impact of Rothification. The Camp draft proposal (written by former House Ways and Means chairman Dave Camp, R-MI) of 2014 proposed a 50/50 model where the first \$9,000 in contributions is tax-deferred and the next \$9,000 is on a Roth basis. That idea is currently in play, but now they're asking, 'How low can we draw the tax-deferred line? At \$3,500? \$2,500?'"

The retirement industry, which relies on tax deferral to incentivize plan participants to save, believes that a weakened form of tax deferral would hurt the industry and hurt retirees.

"My company is concerned about the behavioral response. Will people stop saving at the tax-deferred limit?" Cassidy said, noting that the retirees don't necessarily feel commonality with the industry. "Politically, it's sensitive. The voting public is shedding no tears for the life or annuity industry," he added.

A highly technical but important problem, Cassidy explained, is that tax deferral for retirement savings appears on the annual federal budget as a conspicuous twelve-figure expense, with no precise accounting for the income taxes that retirees will eventually pay when they withdraw the savings.

"Congress looks at tax deferral as an expenditure," he said. "They put it on the same list as true deductions like the mortgage interest deduction. We're saying, bring the money [the future income tax paid on withdrawals from 401(k)s and IRAs] into the 10-year budget window [where it would be netted against current expenditures]."

The panelist, moderated by TV journalist Candy Crowley, also commented on the Obama Department of Labor's fiduciary rule, with its requirement that advisors act in their clients' best interests when handling retirement savings. It's expected that the Trump administration will delay action on the rule until July 2019.

The annuity industry, assuming Hillary Clinton would be president and continue Obama retirement policies, has already done much to adapt to those policies, even as it continues to oppose them. It has spent tens of millions on new products, training, technology and compliance procedures—which may never be rolled back, regardless of what the Trump administration does.

"The battle over the best interest exemption is over," Harris said. "The new battle will be over who is in charge. If Labor strikes down the DOL rule, then the SEC and the National Association of Insurance Commissioners will become important. Then the debate will be, 'What is the enforcement policy?'"

"But if you're all breathing a sigh of relief over the 18-month delay, that would be a mistake," he added. "It's just breathing room. The SEC hasn't produced a rule in seven years; it's not going to produce one in 18 months. It will be up to the industry to push the SEC and DOL and NAIC into a room and give them clear guidance about what you want. But I think you'll get a regime that's more acceptable to industry than what we have now."

But with so much uncertainty in the Labor department, where budgets are reportedly being slashed and no deputy Labor secretary for employee benefits has even been nominated, progress might be difficult. "There's DOL fatigue on Capital Hill," Cassidy said. "The legislative staff turns over and then the next wave needs to be educated about the issues. It's like pushing string."

All three panelists—former Oklahoma Republican congressman J.C. Watts was the third—agreed that confusion reigns in official Washington today, and that the main source of dysfunction is President Trump himself. "There's no plan, no strategy. He just acquiesces to things and then backs away and gets outraged if he loses," said Cassidy.

Watts agreed. "I don't think there's a strategy [behind what Trump does]," he said. "To him, people are just actors on a stage and he has to control the script. He will always position himself to lead the parade if he wins and blame somebody if he loses."

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