
Secure 2.0: A Booster Shot for Qualified Savings Industry

By Kerry Pechter Thu, May 6, 2021

The proposed bill would allow ETFs in variable annuities and remove the 25% limit on the share of IRA money that can be used to buy a Qualified Longevity Annuity Contract. But it would keep the QLAC dollar cap at \$135k. (Photo: Ways & Means Committee chair Richard Neal (D-MA), left, with ranking member Kevin Brady (R-TX)).



The House Ways & Means Committee voted yesterday to approve “Secure 2.0,” otherwise known as H.R. 2954 or “The Securing a Strong Retirement Act of 2020.” With a few last-minute tweaks, it now goes to House of Representatives for consideration.

With that bipartisan action—for which the committee members lavishly praised themselves during a Twitter webcast yesterday—the committee moved the 401(k) industry closer to receiving a second-round booster shot from Congress. The first shot was the SECURE Act of 2019, which introduced pooled 401(k) plans, an easier path to in-plan annuities, and other innovations.

The Insured Retirement Institute and the American Council of Life Insurers both welcomed the passage of Secure 2.0 in press releases this week, as well they should. Like the SECURE Act, Secure 2.0 accommodates many specific remedies sought by the 401(k) industry itself.

For instance, the bill expands auto-enrollment and auto-investment in qualified plans, lets non-profit 403(b) plans form multiple employer plans and use collective investment trusts, and increases credits to plan sponsors for the costs of starting or joining a qualified savings plan.

Regarding participants, high-earners with the greatest ability to save will get the most out of the bill’s higher catch-up provisions, the delay of required minimum distributions (RMDs) from qualified plans to age 75 by 2032, and the ability to apply more savings to Roth 401(k) accounts—which helps affluent retirees to pass their 401(k) accounts to heirs tax-free.

Victims of domestic abuse—once indelicately known as battered women—will be allowed to take emergency cash penalty-free from their qualified accounts. People paying down student debt will be eligible for employer matching contributions. Wealthy people will be able to

transfer more of their IRA savings to charity.

In the annuity sphere, the bill would allow variable annuities to include ETFs as investment options and would remove existing limits on the amount of tax-deferred savings that could be used to buy Qualified Longevity Annuity Contracts (QLACs), which are deferred income annuities whose start date doesn't occur until after the RMD age.

"For the most part, it contains a reasonable set of provisions," said the Urban Institute's Eugene Steuerle in an interview with *RIJ*, demurring that there's no attempt to align the Social Security start age and the RMD age to create synergy between the two.

"Many [of the provisions] simply accommodate the simple fact that we are living longer, or, with QLACs, that we often don't save enough for older old age. However, age provisions for private retirement assets are now further out of synch with Social Security's age thresholds," he said.

QLACs have not been a big seller, but Mark Iwry, the former Treasury official who shepherded the QLAC into existence during the Obama administration, and who was consulted on the writing of the QLAC provisions in Secure 2.0, continues to recommend them for the people—i.e., women—most at risk of living to 95 or 100.

"The combination of mortality pooling and predictable investment for 15 to 20 years produces a meaningful add-on to Social Security income starting at 80 or 85," Iwry told *RIJ* yesterday. "Never mind that Homer [Simpson] thinks all those beers and cheeseburgers mean he'll never live past 80. The QLAC is for Marge."

A summary of the bill's provision can be found [here](#). We dive into a deeper level of detail below:

Increase RMD age to 75 by 2032. Congress wants to raise the age for initial minimum distributions from retirement accounts—again. The SECURE Act generally increased the required minimum distribution age to 72. Secure 2.0 increases the RMD age to 73 starting on January 1, 2022, to 74 starting on January 1, 2029, and to 75 starting on January 1, 2032. The bill also lowers the penalty on those who don't take large enough taxable distributions.

All Roth matching contributions. Secure 2.0 would allow participants in 401(k), 403(b) and governmental 457 plans the option of receiving the plan sponsor's matching contributions on a Roth basis, if the participant wishes. That helps participants who'd rather get tax-free withdrawals from their plans in retirement instead of making tax-deductible

contributions today.

The same provision should be welcomed by those who contemplate passing their retirement plan wealth to their children tax-free, and by those who expect federal taxes to go up if the government feels compelled to offset the inflationary impact of big infrastructure spending with a deflationary tax hike.

Allow ETFs in variable annuities. Section 203 of Secure 2.0 would “facilitate the creation of a new type of ETF that is ‘insurance dedicated.’” These new ETFs would be eligible for inclusion in individual variable annuities. ETFs are already available in retirement plans and IRAs. The new law would simply update Treasury regulations that were written before ETFs were invented.

Remove limits on funding Qualified Longevity Annuity Contracts (QLACs) with tax-deferred savings. QLACs are deferred income annuities whose payouts begin after the owner reaches the age (currently 72) at which RMDs from tax-deferred accounts, like IRAs and 401(k)s, are required. They were created in 2014.

The original rules were conservative, as a way to conserve tax expenditures. Retirees could use no more than 25% (up to \$125,000, originally) of their retirement account values to buy QLACs. In addition, spouses couldn’t pool their tax-deferred savings to buy joint-and-survivor QLACs. Under Secure 2.0, retirees could apply all of their tax-deferred savings to QLACs, up to \$135,000, and could buy QLACs with “spousal survival rights.”

These relaxations could help promote the purchase of QLACs, whose sales have also been hurt by low interest rates and by life insurers’ price increases to offset adverse selection (the risk that only the healthiest people will buy QLACs). There have also been mixed messages from the government.

People can use QLACs to start paying out income at any time after the RMD start date. But QLACs have nevertheless been positioned in government press releases as a kind of ALDA (advanced life deferred annuity) that doesn’t start paying income until ages 80 to 85. To give retirees more flexibility in setting an income commencement date, the government has always allowed QLAC payouts to start at anytime after the RMD date.

Add life annuities with rising benefits in qualified plans and IRAs. In the past, the government’s RMD rules included an actuarial test that was intended to discourage the use of annuities with back-loaded income streams in retirement accounts. The test, however, has the effect of excluding “period-certain” annuities, annuities that include guaranteed

annual increases of only 1% or 2%, and “return-of-premium” death benefits. “Without these types of guarantees, many individuals are unwilling to elect a life annuity under a defined contribution plan or IRA,” the bill’s summary said.

‘Wacky process’

Steuerle noted that the bill includes only a bit of help for middle-income Americans. “Since most retirement assets are held by those with above average wealth, most of the additional deferrals provided in the bill do little for those with more modest income. With one exception: the provision for automatic deposits into 401(k) plans could be quite significant,” he told *RIJ*.

He believes the budget impact of that provision will be mild. “The Joint Committee on Taxation, however, estimates a cost [in lost tax revenue] of only about \$700 million annually for that provision, which implies new contributions of perhaps a modest \$3 billion a year or so in new contributions to regular (non-Roth) accounts,” he added.

Steuerle also questioned the wisdom of encouraging Roth conversions. “The wacky budget process continues to provide incentives to make our kids and grandkids pay for the costs in the out-years by converting more contributions to Roth accounts. Most taxpayers with average income, moreover, are better off not using Roth accounts, but the confusion will likely drag more of them into using Roths,” he said.

While removing some of the frictions in the defined contribution system, the Act does nothing to increase the *capacity* of low income workers to save more, to prevent them from raiding their retirement savings before retirement, or to help re-finance Social Security before it runs short of revenue in 2034 or so. The bill doesn’t stimulate the spread of state-sponsored Roth auto-IRA plans or increase the ability of America’s gig workers to save.

The bill also ignores differences in the *quality* of qualified plans. An observer from Mars would never guess from the language of this bill that not all 401(k) plans are equal. Larger plans, sponsored by large, profitable companies, are more likely to offer low fees and low-cost investments and generous matching contributions. These differences mean that the 401(k) system reflects and reinforces patterns of wealth inequality, even as it helps individuals overcome them.