The SECURE Act Set To Pass (Finally)

By Kerry Pechter *Thu, Dec 19, 2019*

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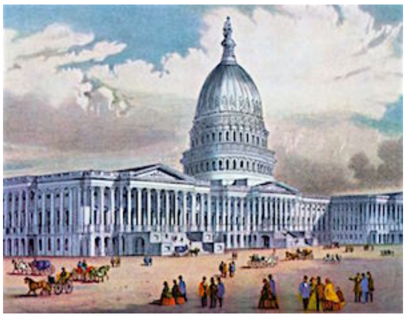

After years of lobbying by large firms in the retirement industry, the Setting Every American Community Up for Retirement Enhancement (SECURE) Act of 2019 appears headed for enactment as part of Congress' $1.4 trillion appropriations **bill**, whose passage averts an otherwise imminent government shutdown.

On Tuesday, the House of Representatives approved a government funding bill that contains the **SECURE Act** by a vote of 297 to 120, according to press bulletins. The Senate was expected to pass the bill and send it to the White House for President Trump's signature this week.

"Things look likely that SECURE will be in the year-end funding package that Congress must pass in order to keep the federal government running," said Brian Graff, CEO of the American Retirement Association, in a statement.

Melissa Kahn

Those who have worked towards this goal for several years are elated. "This is an early Christmas present," said Melissa Kahn, managing director of the Defined Contribution team at State Street Global Advisors (SSgA), in an interview yesterday.

Her firm, the world's third largest asset manager, distributes its target date funds (TDFs), exchange-traded funds and other investments through large retirement plans. The aggregation of dozens or hundreds of unrelated small firms into large open MEPs (multiple employer plans) could vastly expand the market for those products.

"We're fired up for what's ahead," said Troy Tisue, CEO of TAG Resources LLC in Knoxville, TN, whose firm began experimenting with and promoting the idea of open MEPs in 2004. "This is obviously a big deal for TAG as the open MEP is in our DNA. But the real winner here is the small business owner."

Policymakers are hoping that thousands of small employers—and the millions of low-income or minority workers they employ—will join such plans and that the nation's "coverage gap"—the fact that at any given time about half of American workers lack a tax-deferred savings plan at work—will shrink.

Elements of the Act

The SECURE Act is a retirement industry wish-list at least three years in the making. It will:

- Allow companies—regardless of industry—to join industry-sponsored multiple-employer 401(k) plans;
- Increase the auto-enrollment safe harbor cap on participant contributions to 15% from 10%;
- Simplify the non-elective contribution 401(k) safe harbor by providing notice and amendment flexibility;
- Treat certain taxable non-tuition fellowship and stipend payments as compensation for IRA purposes, thus making it easier for individuals receiving such payments to save through an IRA;
- Repeal the maximum age (now 70½) for making traditional IRA contributions;
- Increasing the age at which required minimum distributions (RMDs) must start from 70½ to 72;
- Expand the types of education costs that are coverable by 529 plans; and
- Increase the credit limit for small employer start-up costs and create a new auto-enrollment credit to defray associated start-up costs.

The significance of 'open MEPs'

For large full-service retirement plan providers like Empower, Fidelity, Lincoln Financial, MassMutual, Principal, and T. Rowe Price (some of whom also issue annuities), for asset managers like State Street Global Advisors and BlackRock, for large plan recordkeepers, for third-party administrators, for independent fiduciaries, and for financial advisers who act as brokers for 401(k) plans, the SECURE Act should, over time, create new business opportunities.

The Act could allow these companies, for the first time, to sponsor 401(k) plans—something that in the past only an employer could do. In the past, companies could join multiple employer plans only if they had something important in common—like the same industry, the same union, or the same profession.

These new multiple employer plans will be promoted to dozens or hundreds of small to mid-sized companies whose employers have been reluctant to start or are tired of running their own 401(k)s.

The potential for 'in-plan' annuities

The retirement industry also sees growth opportunities emerging from the SECURE Act's partial lifting of employers' liability when offering "in-plan" annuities. Today, plan sponsors (i.e., individual employers) are reluctant to include any type of annuity as an allocation option within their plan's investment lineups. They believe that, if they did so under current pension law, the bankruptcy—however unlikely—of an annuity provider (i.e., a life insurer) could expose them to steep legal and financial risks or complications.

The annuity option to be offered in retirement plans would most likely be lifetime income benefit riders attached to TDFs. These funds are the default investment option for millions of participants, and the rider could be set up as part of the default. These riders have cost about 50 basis points a year and could be added, automatically, to participants when they reach, for example, age 45 or 50. No one is mentioning the introduction of fixed multiple-premium income annuities in retirement plans, which would carry restrictions on liquidity.

Empower Retirement, Prudential Retirement and Lincoln Financial all have TDF-based 401(k) lifetime income-generating products that have been lying more or less dormant, awaiting the SECURE Act's passage to trigger a new round of marketing to large plan sponsors.

"We've had a product available," said Will Fuller, the president of Annuity Solutions at Lincoln Financial, in a recent interview. "We've given it a compelling guarantee. We made sure that it's portable. The take-up rate today is minuscule, but [the SECURE Act] would mean a completely new frontier for the annuity industry." The Lincoln product, **Secured Retirement Income**, is available as either as a standalone investment, or included in the glide path of a custom target-date portfolio.

The impetus for change

The retirement industry not only wanted the changes included in the SECURE Act; it *needed* them. The industry has been consolidating since the Great Financial Crisis, and only the largest asset managers, recordkeepers, and plan administrators with the biggest economies of scale are expected to survive over the long-term.

Indeed, an analyst at Cerulli Associates wrote this week that the retirement industry is moving toward "an oligarchy" of a few large providers. Today, just 10 plan recordkeepers handle an estimated 75% of 401(k) assets today, writes Cerulli's Anastasia Krymkowski.

But Cerulli doesn't expect the SECURE Act to have an instant effect on the retirement market or to disrupt the industry's current hierarchy. "This is not going to make or break the big guys," she told *RIJ*. "It will be interesting to see how this plays out over the next five years."

Size will matter for retirement services vendors that are trying to cope with a variety of headwinds. They include declining fees for investment products, rising costs of technology—ranging from artificially-intelligent chat bots to cyber-security measures—and potential competition from the state-sponsored, auto-enrolled, public-option Roth IRA savings programs for small companies that have sprung up in Oregon, California, and other states.

In addition, some observers fret that the hunger for fast growth might tempt large providers into a form of industry cannibalization, where firms try to entice existing 401(k) plans into open MEPs instead of pitching to employers with no current plan or pre-existing pool of manageable assets.

One item that the SECURE Act withholds from retirement plan providers is the ability to sponsor retirement plans and simultaneously sell its own products to the plan. The potential synergies of such an arrangement are obvious, but so are the potential conflicts of interest and opportunities for unethical self-dealing.

"Today, you can't be the sponsor of a multiple employer plan and provide the MEP with your own products. That would be a prohibited transaction" under ERISA (Employee Retirement Income Security Act of 1974), SSgA's Kahn told *RIJ* yesterday. "Even if the Department of Labor allows some exemptions to the prohibited transaction rule, there would still be a lot of restrictions on providers."

Ben Norquist

“That could be a dangerous opening for too much conflict of interest,” said Ben Norquist, CEO of Convergent Retirement Plan Solutions LLC in Brainard, MN., in an interview. His firm serves as an intermediary between the federal government and industry, helping firms digest new developments like the SECURE Act.

“We provide education, training and content that prepares plan advisers, sponsors and vendors for either ‘reactive compliance’ or growth opportunities. We’re doing a webcast about the SECURE Act on Wednesday,” he told *RIJ* yesterday.

Norquist expects to field a lot of nervous questions about the effective dates of certain provisions in the bill. For instance, the Act allows retirement account owners to delay required minimum distributions until age 72 and make IRA contributions until then, but the new rule applies only to those reaching age 70½ in 2020 or later. The elimination of the “stretch IRA” and the 10-year distribution requirement applies to deaths after December 31, 2019, but not for deaths before then.

The Act will create confusion at first, but Norquist welcomes a bit of regulatory confusion. “We’ve always told the financial services industry that, even when there are negative changes, confusion creates opportunity,” he said. “With all the money pouring into fintech (financial technology), and all the efforts to streamline plan services, the open MEP concept creates a lot of interesting possibilities.”