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Comments to The President's Advisory Panel on Federal Tax Reform

Filed on behalf of American Council of Life Insurers

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The President's Advisory Panel on Federal Tax Reform
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Members of the Panel:

The American Council of Life Insurers (ACLI) is pleased to respond to the second request for public comment issued by the President's Advisory Panel on Federal Tax Reform.[1] Our previously filed response to your first request for comments highlighted the general need for this Panel to include in its report the continuation and expansion of initiatives that encourage individuals to take personal responsibility for retirement planning and promote long-term retirement savings. We believe that any reform proposal should include provisions that encourage retirement savings and investment through the retention and expansion of the current system's tax incentives.

The second request for comments solicits specific proposals to reform the tax code and invites either proposals for comprehensive reform or proposals to reform particular aspects or elements of the current code. While we believe that the current code does a good job of encouraging long-term retirement savings, we have identified a number of areas where change would strengthen existing provisions.

[1] ACLI represents 354 life insurance companies operating in the United States. These 354 member companies account for 74 percent of the industry's total assets, 69 percent of the life insurance premiums, 79 percent of annuity considerations, 51 percent of disability income insurance premiums, and 81 percent of long-term care insurance premiums in the United States.

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Qualified Plan Retirement Proposals

Our member companies believe that the code should strongly encourage employers to offer lifetime annuities to participants in all types of qualified plans – defined benefit (DB) as well as defined contribution (DC) plans. While DB plans generally offer lifetime annuities, the number of individuals covered by these plans continues to decrease. The latest available data indicate that there are 22 million active participants in DB plans. In contrast, there are more than 50 million active DC plan participants.[2] While some DC plan participants also will receive benefits from DB plans, the trend is clear – the growth in employment-based retirement plans is in DC plans. In the past quarter century there has been a precipitous decline in the number of DB plans sponsored by private sector employers, from 148,096 in 1980 to 49,895 in 1999. [3] Most DC plans do not offer the lifetime annuity distribution option to employees. When employees retire or otherwise terminate employment, they are generally offered the option of receiving the DC balance in a lump sum, or transferring it to an individual retirement account or another qualified plan. Many employers may recognize the benefits to employees of a lifetime annuity option, but decline to make the annuity available due to administrative and statutory hurdles they encounter in offering an annuity. These hurdles include Department of Labor rules relating to the "safest available annuity"[4], as well as the potential applicability of the complicated "qualified joint and survivor annuity rules[5]" for DC annuities. Removing these hurdles should not have any negative affect on federal revenues and would encourage more employers to offer an annuity option. This would benefit employees by helping ensure retirement income lasts

[2] Private Pension Plan Bulletin, Abstract of 1999 Form 5500 Annual Reports, U.S. Department of Labor, Number 12, Summer 2004, Table A1.
[3] Id. at Table E1.
[4] DOL Interpretative Bulletin 95-1, 29 C.F.R. § 2509.95-1. *See also*, DOL Advisory Opinion 2002-14A.
[5] Internal Revenue Code section 417, 26 U.S.C. 417

throughout retirement, rather than "run-out" should the retirement last longer than expected or planned.

Employees, in turn, do not demand an annuity option. They may believe they can manage assets themselves either through transfer of DC assets to an IRA or receipt of DC proceeds in a lump sum. Unfortunately, managing assets in retirement is a difficult challenge and there is genuine concern that the next generation of retirees who are "doing it alone" with a lump sum of money may struggle with this task. Encouraging these retirees to turn a portion of their retirement monies into a lifetime annuity will help them with this management. A number of legislative proposals introduced in the last Congress would provide a modest tax incentive to retirees selecting a lifetime income annuity.[6] In brief, under these proposals, a portion of the otherwise taxable retirement income would be received without tax if the income were from a lifetime annuity. These modest proposals may be the incentive that some retirees need to help them consider the benefits of a lifetime annuity and select this option. With a lifetime annuity, and only with a lifetime annuity, will a retiree be guaranteed to receive a steady amount for life (and for the life of his or her surviving spouse if this payment option is selected).

In addition to facilitating and encouraging annuities in DB plans, our members also join with others involved in retirement security issues to support legislation that (a) facilitates automatic enrollment of new employees in qualified plans, (b) permits investment advice to employees, and (c) makes permanent the 2001 changes to the retirement plan investment limits in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA).

[6] Pension Preservation and Savings Expansion Act of 2003 (H.R.1776, sec. 109); Secure Annuity Income for Life Act of 2003 (H.R.2458)

Individual Plan Retirement Proposals

Approximately 51 percent of full- and part-time workers – nearly 53 million people – do not have access to employer-provided retirement plans of any kind. These individuals have the hardest retirement saving task of all – they need the discipline to save, access to information about how to save, and assistance in managing their savings in retirement. In addition, the amount set aside for retirement in individual savings, outside of a qualified plan, does not receive the same advantageous tax treatment as an amount saved in a qualified plan.

In order to help individual savers to manage their savings throughout retirement, we support a tax incentive for those who receive a portion of their retirement savings through a lifetime annuity, similar to the incentive for qualified plan annuitization described above. However, the tax incentives for lifetime payouts in this context should be more substantial. Since individual retirement planning is more challenging, the tax incentive needs to be meaningful enough to change the economics of the decision-making process. Legislation providing this tax incentive was introduced in this Congress as well as in the 108th. [7]

Corporate Proposals

In order to better assist Americans in providing for their retirement security, life insurers also are interested in reducing the complexity of the corporate income tax as it pertains to our industry. Certain complicated tax provisions – relating to the filing of consolidated returns and applying only to life insurance companies – unduly burden the affected life insurers, unnecessarily increase the cost of products to consumers, and create marketplace inefficiencies. Legislation has been proposed that would remove these outdated and complex restrictions and limitations.[8] This would provide fundamental fairness for life insurers and enable the affected life insurers to

[7] Retirement Security for Life Act of 2005, 109th Cong., 1st Sess. S. 381 and H.R. 819
[8] 108th Cong, 1st Sess, H.R. 2228 and S. 1495

better compete with other financial institutions. To the best of our knowledge, there has not been any substantive opposition to the removal of these consolidated return rules. Those who have examined the issue closely, including more than 50 percent of the House Ways & Means Committee for the last Congress, agree that change is needed.

* * *

In conclusion, barriers to retirement savings and investment must continue to be lowered. Therefore, we request that this Panel include in its report to the President recommendations for (1) continuation of the existing tax incentives to encourage Americans to save for retirement, (2) new incentives related to lifetime annuity payments to assist retirees in managing their retirement assets, and (3) the elimination of life insurance company consolidated return restrictions and limitations.

On behalf of our member companies, ACLI looks forward to working with the Panel regarding the issues raised in this letter. Any questions or comments on these issues are welcome.

Sincerely yours,

Frank

Frank Keating