The Savings Coalition of America

Submission to the President's Advisory Panel on Federal Tax Reform

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Organizations and Associations

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Executive Summary

The Savings Coalition of America urges the President's Advisory Panel on Tax Reform to include the Bush Administration's savings proposals in its recommendations for tax reform. These proposals, the Lifetime Savings Accounts (LSA), Retirement Savings Accounts (RSA) and the Employer Retirement Savings Accounts (ERSA), simplify the current tax code and provide incentives for Americans to save. These proposals, as included in the Treasury Blue Book raise revenue over a 10 year time frame.

The RSA proposal would consolidate the three types of current IRAs into a single account that could only be used for retirement savings; other withdrawals would be subject to tax and penalty. Instead of a list of exceptions for penalty-free early withdrawals, a new account, a LSA would be created that could be used to save for any purpose, including retirement savings, health care, emergencies, and education.

Individuals could contribute up to $5,000 per year to their RSA and $5,000 to their LSA. No income limits would apply to LSA or RSA contributions. Contributions would be nondeductible, but earnings would accumulate tax-free, and qualified distributions would be excluded from gross income. The RSA and LSA contribution limit would be indexed for inflation.

The ERSA would consolidate the variety of 401(k)-type retirement plans into a single plan that exist today thereby making them easier to administer. The proposal simplifies some of the needlessly complex pension coverage and non-discrimination testing rules for employer-sponsored retirement plans. The proposal also eliminates programs that are no longer necessary with the continued move to 401(k) plans.

April 29, 2005

The Honorable Connie Mack
Chairman
The President's Advisory Panel on Federal Tax Reform
1440 New York Avenue NW
Suite 2100
Washington, DC 20220

Dear Chairman Mack:

On behalf of its 75 member organizations, the Savings Coalition of America ("Coalition") is pleased to submit the following recommendations in response to the April 5 invitation for proposals by the President's Advisory Panel on Federal Tax Reform ("Panel"). The Coalition urges the Panel to reform the current aspects of the income tax code pertaining to savings incentives. In particular, the Coalition urges the Panel to consider the savings incentives included in the President's Budget Request over the past three years; the Lifetime Savings Accounts (LSAs), Retirement Savings Accounts (RSAs) and Employer Retirement Savings Accounts (ERSAs). According to the General Explanations of the Administration's Fiscal Year 2006 Revenue Proposals, also known as the Treasury Blue Book, these proposals which simplify savings for all Americans raise revenue over ten years.

Administration's LSA, RSAs, ERSAs Proposal

In 2003 and subsequent years, the White House and the Department of the Treasury recommended proposals to create new simple and expanded savings vehicles, which will significantly increase opportunities for Americans to save for the future through new and less complicated venues. The accounts proposed by the President will provide Americans with a variety of savings vehicles that will meet their needs throughout their lives. The Coalition feels that the administration recognized the importance of simplicity for savings in these proposals. Coalition members know from experience that fewer rules and restrictions often result in higher participation rates across all socio-economic levels.

The Lifetime Savings Accounts (LSAs), Retirement Savings Accounts (RSAs), and the Employer Retirement Savings Accounts (ERSAs) will encourage Americans to save for all of life's major occurrences. The LSAs will promote the concept of savings to Americans at all ages.

The RSAs address a key component of retirement; personal savings. Personal savings is the third leg of the retirement stool in addition to employer-provided plans and Social Security. By eliminating income restrictions, the RSA will be a great tool for Americans to save for their retirements, especially baby boomers who are within a decade of beginning to retire. The ERSA is a simplified version of the 401(k) which may encourage more plan sponsorship. In addition, the proposal eliminates redundancy and duplicative incentives in the tax code. Both retirement account proposals will greatly assist Americans to be financially prepared for retirement.

The tax base for the proposals for improved, universally available savings incentives is based on the current income tax system. For the LSAs and RSAs, there will be no deductions for contributions. However, the contribution and earnings are free of tax upon withdrawal. The ERSA will have many features of current salary deferral arrangements which are tax-deductible. The ERSA simplifies the various types of retirement plans thereby making employer retirement savings simpler and more easily transferable. This is especially important when realizing that, on average, Americans in today's workforce are expected to make nine job/career changes in their lifetimes. Since these proposals are universally available, they would apply to Americans in all tax brackets.

As stated in the Coalition's earlier comments on tax reform to the Panel, we feel that savings incentives should apply to all Americans regardless of income level. Our tax system does not treat savings favorably. More savings is better encouraged through a universal approach and should not be subject to income restraints. The tax code should not be used to discriminate between successful Americans who need to save as much as those who are striving to get ahead.

Impact of Proposal Relative to Current System

The current income tax system has a number of retirement and education savings vehicles – both for individual savings as well as saving through an employer plan. The RSA and ERSA simplify the accounts thereby making them easier to understand and use. By eliminating the income limits on contributions to RSAs, all Americans are eligible to participate in savings for their retirements. The complexity of different income limits and types of Individual Retirement Accounts (IRAs) that exist today's will be eliminated which will result in these important savings vehicles being much easier to understand. These accounts will then be marketed by financial services firms, much like in the early 1980s when IRAs were available to all Americans. It is important to note that this marketing served as an education about these accounts and as a result we saw the average income of Americans contributing to IRAs was lower each year as more Americans became aware of the product and wanted to save. The elimination of income limits creates a sense of fairness across all socio-economic classes. Savings is a behavior we want to encourage and it should not be discouraged based on income and levels of success that any American may achieve.

Since the RSA would no longer have penalty-free withdrawal features, the LSA would provide Americans an opportunity to save for those important lifetime occurrences. The federal government acknowledged the need to have withdrawals for those events such as the first-time purchase of a home by allowing penalty-free withdrawals from IRAs. While ensuring that the RSA is used strictly for retirement, the LSA would encourage Americans to save for those other purposes.

The ERSA will consolidate the myriad of employer-sponsored defined contribution plans that exist today. Americans, on average, change jobs at least nine times in their working years. The ERSA would make it much easier of Americans to move their retirement accounts to a new employer. This would alleviate keeping track of a variety of different accounts and rules surrounding them. Again, our public policy should be one that encourages Americans to save and be prepared for retirement. The simplification of going to an ERSA would make it that much easier for our workers to participate. With this simplification in place, it is felt that more Americans will participate in their employer plans. In addition, the attractiveness of one type of employer-based retirement savings vehicle should encourage more employers to establish retirement plans for their workers.

Transition, Tradeoffs and Special Issues

The transition from the savings incentives under the current income tax system to the ones described in this paper would be fairly easy. The transition from many different types of IRAs with many levels of eligibility should be straightforward and fairly easy to implement. Since the RSA will be like the Roth IRA without withdrawal features or income limits, this should have a smooth transition. Since all of the industries in the financial services arena currently sell IRAs, there should not be any unfavorable treatment of any of them.

The transition from the current employer-sponsored plan system will be more complicated. There are some industries within the financial services sector that currently are the only ones eligible to provide certain products which make the current system inherently unfair. In addition, there are certain careers that have more favorable treatment with regard to how much they can save for retirement through their current plan. Again, this is unfair to those who are not in those careers. The ERSA would simplify the employer-sponsored plan system while equalizing savings opportunities across different sectors of employment.

Some financial services firms have expressed concern about the establishment of the LSA. They are concerned that the LSA will discourage employers from sponsoring retirement plans. It is felt that these savings vehicles in conjunction with RSAs would allow employers to put away funds for their retirements without having to sponsor a plan for their employees. However, with the modified contribution limits and other restrictions place on the LSA, the Savings Coalition believes that those concerns have been adequately addressed. In addition, the LSA is likely to encourage new savers who are not covered by an employer-sponsored retirement plan. The number of workers not covered has not decreased significantly despite a number of attempts to expand plan sponsorship. Therefore, it is important to consider initiatives that will encourage workers to start saving on their own.

The Savings Coalition urges the President's Advisory Panel on Federal Tax Reform to include the establishment of simplified savings vehicles such as those proposed by the Bush Administration in its recommendations for tax reform. We look forward to working with you on this important initiative.

Sincerely,

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