Retirement and Tax Reform

THE ISSUE: With 10,000 people reaching retirement age every day for the next 16 years, it is important that public policy incentivizes and encourages families to save and plan for retirement. Some in Washington believe the current tax code is complex, outdated, and in need of reform. Whether Congress considers a comprehensive approach or something more concise, it will be important for policy makers to ensure that families and workers can continue to protect against the risks of dying too soon or outliving their savings. Life insurance and annuity products can help minimize these risks and are often necessary to obtaining financial and retirement security.

BACKGROUND: Insurance products and employer-provided benefits help Americans provide financial protection and security for themselves and their loved ones. Whether it is the economic loss from dying prematurely, becoming ill or disabled, or outliving savings in retirement, most families do not have the resources to manage these risks on their own.

Life insurance products are unique in their ability to successfully and affordably transfer risk from the individual to a larger pool of savers or insureds. Policy benefits paid at the death of a breadwinner help families avoid the hardship of lost income. Sometimes life insurance can be a back-up savings source to be used in emergencies. Annuities pay a guaranteed stream of income, protecting individuals from outliving their assets and can be purchased both in a qualified retirement plan or held personally. Disability income insurance protects workers' income by replacing a portion of their earnings if they cannot work due to accident or illness. Whether people seek protection and security products on their own or as part of a group with the assistance of their employer, our nation's tax system should not discourage these actions.

Nearly 90 million Americans rely on a private sector plan such as a 401(k) defined contribution or defined benefit plan to save for retirement[1] and 42.5 million households own IRAs.[2] Seventy-five million American families rely on annuities or other life insurance products for long term financial security.[3] Unfortunately, Baby Boomers and GenXers are projected to have a retirement income deficit of $4.3 trillion and roughly 44% will lack adequate retirement income for basic expenses.[4]

Current tax rules do not tax earnings on life insurance policy values unless there is an actual distribution. This tax treatment is consistent with general tax principles and is a necessary component of the affordable pricing structure of life insurance products. Policy premiums are paid with after-tax dollars, and if taken, distributions are taxed at ordinary income tax rates. Any changes to how products and product providers are taxed would have a negative effect on families and workers, making it more difficult and more expensive to properly manage risks or adequately plan for retirement.

The current tax treatment of insurance, contributions to retirement savings, and employer-provided benefits encourage people to prepare and plan for the future and thus relieves pressure on already strained government programs. Recent tax reform proposals included provisions that would make it more costly to offer products, resulting in millions of American families being uninsured or under-insured. Other proposals have included provisions that reduce or limit retirement plan contributions. Lawmakers contemplating tax reform should diligently protect the fair and necessary treatment of insurance products that over 75 million families rely upon to assure their financial security.

NAIFA POSITION: Americans need public policy that continues to encourage them to plan ahead, protect their families' financial security and adequately save for retirement. Well prepared families will have adequate retirement savings accounts, life insurance, medical insurance, and guaranteed income annuities to supplement social security benefits. With the strain on federal entitlement programs as well as on state and local programs, now is not the time to make it more difficult or more expensive for families to plan for their long-term financial needs.

NAIFA believes that tax reform should preserve the tax treatment of retirement savings options under current law. In particular, NAIFA believes that Congress should not eliminate or limit the current ability to contribute tax-deferred amounts

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[1] U.S. Department of Labor Employee Benefits Security Administration, *Private Pension Plan Bulletin, Abstract of 2014 Form 5500 Annual Report* (September 2016).
[2] "ICI Research Perspective," *Investment Company Institute (ICI),* 2017, available at https://www.ici.org/pdf/per23-01.pdf
[3] American Council of Life Insurers, 2016 Life Insurer's Fact Book
[4] Employee Benefit Research Institute, *EBRI Notes: Retirement Income Adequacy for Boomers and Gen-Xers: Evidence from the 2012 EBRI Retirement Security Projection Model.*

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to 401(k), IRA, and other retirement plans. While these pre-tax retirement plan contributions do not give rise to immediate tax, they are fully taxed (along with any growth) when an individual draws them down in retirement.

NAIFA is concerned that proposals, such as those included in former Chairman Dave Camp's 2014 tax reform plan, to limit tax-deferred contributions and, instead direct taxpayers to Roth-type accounts, would create a disincentive to saving for retirement. Current tax-deferred retirement options give taxpayers a current tax saving from making a retirement plan contribution. Roth accounts, by contrast, provide no immediate tax incentive to prioritize long-term retirement savings over consumption. For many taxpayers with competing priorities, such as purchasing a home or saving for college for their children, the Roth option would not provide sufficient incentive to save for retirement.

Limiting retirement savings options to Roth-type accounts would also have significant adverse effects on employer-sponsored retirement plans. As you are aware, Roth accounts (including in 401(k) plans) do not permit employer-matching contributions, and it is unclear how such contributions could be integrated into a Roth-focused retirement system. Without tax-deferred employer matching contributions to retirement plans, employees would have significantly less incentive to make their own contributions. Moreover, without the ability to make pre-tax retirement plan matching contributions, many closely-held business owners may decide that it is easier to not offer a retirement plan at all. The behavioral response of employers and workers to limiting retirement savings to Roth-type options will lead to significantly less retirement readiness on the part of Americans.

ABOUT NAIFA: Founded in 1890 as The National Association of Life Underwriters, NAIFA is the nation's oldest and largest association representing the interests of insurance professionals from every Congressional district in the United States. NAIFA members assist consumers by focusing their practices on one or more of the following: life insurance and annuities, health insurance and employee benefits, multiline, and financial advising and investments. NAIFA's mission is to advocate for a positive legislative and regulatory environment, enhance business and professional skills, and promote the ethical conduct of its members.

For More Information Please Contact:

Diane Boyle
Sr. Vice President
(703) 770-8252
dboyle@naifa.org

Judi Carsrud
Director
(703) 770-8155
jcarsrud@naifa.org