# DESCRIPTION OF SUBTITLE B — RETIREMENT OF BUDGET RECONCILIATION LEGISLATIVE RECOMMENDATIONS

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# INTRODUCTION

The House Committee on Ways and Means has scheduled a committee markup of Subtitle B — Retirement of Budget Reconciliation Legislative Recommendations. This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of the bill.

[1] This document may be cited as follows: Joint Committee on Taxation, *Description of Subtitle B — Retirement of Budget Reconciliation Legislative Recommendations* (JCX-35-21), September 7, 2021. This document can also be found on the Joint Committee on Taxation website at www.jct.gov. All section references herein are to the Internal Revenue Code of 1986, as amended (herein "Code"), unless otherwise stated.

## SUBTITLE B — RETIREMENT

## A. Automatic Contribution Plans and Arrangements

### 1. Tax imposed on employers failing to maintain automatic contribution plan or arrangement

#### Present Law

Whether to offer a retirement plan is a choice by an employer. The Code provides for multiple types of tax-favored employer-sponsored retirement plans, including qualified retirement plans and annuities,[2] tax-deferred annuities,[3] governmental eligible deferred compensation plans,[4] savings incentive match plans for employees ("SIMPLE") individual retirement arrangements ("IRAs"),[5] and simplified employee pensions ("SEPs").[6] Each of these are subject to varying requirements under the Code and, in some cases, under the Employee Retirement Income Security Act of 1974 ("ERISA"). Another retirement vehicle available to individuals is an IRA.[7] There are two basic types of IRAs, traditional IRAs and Roth IRAs, as further described below.

**Qualified retirement plans**

Qualified retirement plans are of two general types: defined benefit plans, under which benefits are determined under a plan formula and paid from general plan assets, rather than individual accounts; and defined contribution plans, under which benefits are based on a separate account for each participant, to which are allocated contributions, earnings, and losses. Some qualified retirement plans are referred to as hybrid plans because they have features of both a defined benefit plan and a defined contribution plan; for example, cash balance plans are defined benefit plans, but plan benefits are defined by reference to a hypothetical account balance. Qualified annuity plans are similar to qualified retirement plans in treatment, but plan assets are invested in annuity contracts rather than held in a trust or custodial account.

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[2] Secs. 401(a) and 403(a).

[3] Sec. 403(b).

[4] Sec. 457(b).

[5] Sec. 408(p).

[6] Sec. 408(k).

[7] The term "IRA" includes both individual retirement accounts, under section 408(a), and individual retirement annuities, under section 408(b).

Defined contribution plans

In general

Defined contribution plans may provide for nonelective contributions and matching contributions by employers and pre-tax (that is, contributions are either excluded from income or deductible) or after-tax contributions by employees. Total contributions made to an employee's account for a year cannot exceed the lesser of $58,000 (for 2021)[8] or the employee's compensation. The deduction for employer contributions to a defined contribution plan for a year is generally limited to 25 percent of the participant's compensation. A participant must at all times be fully vested in his or her own contributions to a defined contribution plan and must vest in employer contributions under three-year cliff vesting or two-to-six-year graduated vesting.

Defined contribution plans often provide for loans to participants and generally provide for distributions on severance from employment and, depending on the type of plan, may provide for in-service distributions.[9] Defined contribution plans may provide for distributions to be made in a lump sum or installments; defined contribution plans may offer annuity distributions, but most are not required to offer annuities.

General types of defined contribution plans

Defined contribution plans may themselves be of different types, specifically, profit-sharing plans, stock bonus plans, or money purchase pension plans, and may include special features, such as a qualified cash or deferred arrangement (section 401(k)) or an employee stock ownership plan ("ESOP"). Rules requiring annuity benefits for surviving spouses and spousal consent to certain distributions apply to money purchase pension plans and, in some cases, other defined contribution plans offering annuities. However, most defined contribution plans are exempt from these requirements as long as they provide that a participant's account balance will be paid to the participant's surviving spouse (unless the spouse consents to a different beneficiary).

Section 401(k) plans

Under a section 401(k) plan, an employee may elect to have contributions (elective deferrals) made to the plan, rather than receive the same amount in cash. For 2021, elective deferrals of up to $19,500 may be made, plus, for employees aged 50 or older, up to $6,500 in catch-up contributions. Elective deferrals generally cannot be distributed from the plan before the employee's severance from employment, death, disability, or attainment of age 59½, or in the case of hardship or plan termination.

[8] Plans may permit employees aged 50 or older to make catch-up contributions; in that case the limit (including catch-up contributions) is $64,500 for 2021.

[9] For example, because money purchase pension plans are pension plans, they generally cannot allow for distributions except for at retirement or termination of employment.

Elective deferrals are generally made on a pre-tax basis. However, a section 401(k) plan may include a qualified Roth contribution program under which elective deferrals are made on an after-tax basis (designated Roth contributions), and certain distributions ("qualified distributions") are excluded from income. Many section 401(k) plans provide for matching contributions and may also provide for employer nonelective contributions and after-tax employee contributions.

Section 401(k) plans may be designed so that elective deferrals are made only if the employee affirmatively elects them. However, a section 401(k) plan may provide for "automatic enrollment," under which elective deferrals are made at a specified rate unless the employee affirmatively elects not to make contributions or to make contributions at a different rate. Various rules have been developed to provide favorable treatment for plans that provide for automatic enrollment, subject to certain notice requirements.

Elective deferrals under a section 401(k) plan are subject to a special nondiscrimination test, called the actual deferral percentage test or "ADP" test, which compares the average deferral rates for highly compensated employees and non-highly compensated employees. A similar test, the actual contribution percentage test or "ACP" test, applies to employer matching contributions and after-tax employee contributions. Design-based safe harbors are also available for satisfying the special nondiscrimination requirements.

ESOPs

An ESOP is a stock bonus plan that is designated as an ESOP and is designed to invest primarily in employer stock. An ESOP can be a standalone plan or it can be a portion of another type of defined contribution plan.

ESOPs are subject to additional requirements that do not apply to other plans that hold employer stock, including a requirement that certain participants must be permitted to diversify a portion of their accounts. However, certain benefits are available to ESOPs that are not available to other types of qualified retirement plans, including an exception to the prohibited transaction rules for certain loans and, in the case of a C corporation, higher deduction limits. ESOPs maintained by S corporations are subject to special rules, including restrictions on the provision of employer stock and stock options (or other "synthetic equity") to certain "disqualified persons."

**Section 403(b) plans**

Tax-deferred annuity plans (referred to as section 403(b) plans) are generally similar to qualified defined contribution plans but may be maintained only by (1) tax-exempt charitable organizations,[10] and (2) educational institutions of State or local governments (that is, public schools, including colleges and universities).[11] Section 403(b) plans may provide for employees

[10] These are organizations exempt from tax under section 501(c)(3). Section 403(b) plans of private, tax-exempt employers may be subject to ERISA as well as the requirements of section 403(b).

[11] Sec. 403(b).

to make elective deferrals (in pre-tax or designated Roth form), including catch-up contributions, or other after-tax employee contributions, and employers may make nonelective or matching contributions on behalf of employees. Contributions to a section 403(b) plan are generally subject to the same contribution limits applicable to qualified defined contribution plans, including the limits on elective deferrals.

**Governmental section 457(b) plans**

Special rules apply with respect to deferred compensation arrangements of State and local government and tax-exempt employers.[12] Amounts deferred under an eligible deferred compensation plan, *i.e.*, a section 457(b) plan, are not currently included in income. In the case of a State or local government employer, a section 457(b) plan is generally limited to elective deferrals and provides tax benefits similar to a section 401(k) or section 403(b) plan in that deferrals are contributed to a trust or custodial account for the exclusive benefit of participants, but are not included in income until distributed (and may be rolled over to another tax-favored plan).[13] Generally, the same contribution limits apply that apply to section 401(k) and section 403(b) plans.[14]

**SIMPLE IRA plan**

A small employer that employs no more than 100 employees who earned $5,000 or more during the prior calendar year can establish a simplified tax-favored retirement plan, which is called the SIMPLE retirement plan. A SIMPLE IRA plan is generally a plan under which contributions are made to an IRA for each employee (a "SIMPLE IRA").[15] A SIMPLE IRA plan allows employees to make elective deferrals to a SIMPLE IRA, subject to a limit of $13,500 (for 2021). An individual who has attained age 50 before the end of the taxable year may also make catch-up contributions under a SIMPLE IRA plan up to a limit of $3,000 (for 2021).

**Simplified employee pensions**

A SEP is an IRA to which the employer may make contributions for an employee up to the lesser of 25 percent of the employee's compensation or the dollar limit applicable to

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[12] Sec. 457.

[13] In the case of a tax-exempt employer, sections 457(b) and 457(f) limit the amount of unfunded nonqualified deferred compensation that can be provided on a tax-deferred basis.

[14] However, the section 457(b) plan limits apply separately from the combined limit applicable to section 401(k) and section 403(b) plan contributions, so that an employee covered by a governmental section 457(b) plan and a section 401(k) or section 403(b) plan can contribute the full amount to each plan. In addition, under a special catch-up rule, for one or more of the participant's last three years before normal retirement age, the otherwise applicable limit is increased to the lesser of (1) two times the normal annual limit ($39,000 for 2021) or (2) the sum of the otherwise applicable limit for the year plus the amount by which the limit applicable in preceding years of participation exceeded the deferrals for that year.

[15] Sec. 408(p).

contributions to a qualified defined contribution plan ($58,000 for 2021).[16] All contributions must be fully vested. Any employee must be eligible to participate in the SEP if the employee has (1) attained age 21, (2) performed services for the employer during at least three of the immediately preceding five years, and (3) received at least $650 (for 2021) in compensation from the employer for the year. Contributions to a SEP generally must bear a uniform relationship to compensation. Effective for taxable years beginning before January 1, 1997, certain employers with no more than 25 employees could maintain a salary reduction SEP ("SARSEP") under which employees could make elective deferrals.

**Individual retirement arrangements**

There are two basic types of IRAs: traditional IRAs,[17] to which both deductible and nondeductible contributions may be made,[18] and Roth IRAs, to which only nondeductible contributions may be made.[19] The principal difference between these two types of IRAs is the timing of income tax inclusion. For a traditional IRA, an eligible contributor may deduct the contributions made for the year, but distributions are includible in gross income to the extent attributable to earnings on the account and the deductible contributions. For a Roth IRA, all contributions are after-tax (that is, no deduction is allowed) and, if certain requirements are satisfied, distributions are not includible in gross income.

Annual contribution limit

An annual limit applies to contributions to IRAs. The contribution limit is coordinated so that the aggregate maximum amount that can be contributed to all of an individual's IRAs (both traditional and Roth) for a taxable year is generally the lesser of a certain dollar amount ($6,000 for 2021) or the individual's compensation.[20] In the case of a married couple, contributions can be made up to the dollar limit for each spouse if the combined compensation of the spouses is at least equal to the contributed amount.

An individual who has attained age 50 before the end of the taxable year may also make catch-up contributions to an IRA. For this purpose, the aggregate dollar limit is increased by $1,000. Thus, for example, if an individual over age 50 contributes $7,000 to a Roth IRA for 2021 ($6,000 plus $1,000 catch-up), the individual will not be permitted to make any contributions to a traditional IRA for that year. In addition, deductible contributions to

[16] Sec. 408(k).

[17] Sec. 408.

[18] Sec. 219.

[19] Sec. 408A.

[20] Under a special rule, the contribution limit for nondeductible contributions to an IRA may be increased in certain circumstances by the amount of qualified foster payments that are difficulty of care payments that an individual excludes from gross income. Sec. 408(o)(5). Thus, for example, an individual who receives such difficulty of care payments but has no compensation for a taxable year may nevertheless be permitted to contribute to an IRA.

traditional IRAs and after-tax contributions to Roth IRAs generally are subject to adjusted gross income ("AGI") limits. IRA contributions generally must be made in cash.

Traditional IRAs

An individual may make deductible contributions to a traditional IRA up to the IRA contribution limit if neither the individual nor the individual's spouse is an active participant in an employer-sponsored retirement plan. If an individual (or the individual's spouse) is an active participant in an employer-sponsored retirement plan, the deduction is phased out for taxpayers with AGI for the taxable year over certain indexed levels. In the case of an individual who is an active participant in an employer-sponsored plan, the AGI phase-out ranges for 2021 are: (1) for single taxpayers, $66,000 to $76,000; (2) for married taxpayers filing joint returns, $105,000 to $125,000; and (3) for married taxpayers filing separate returns, $0 to $10,000. If an individual is not an active participant in an employer-sponsored retirement plan, but the individual's spouse is, the deduction is phased out for taxpayers with AGI for 2021 between $198,000 and $208,000.

To the extent an individual cannot or does not make deductible contributions to a traditional IRA or contributions to a Roth IRA for the taxable year, the individual may make nondeductible contributions to a traditional IRA (that is, no AGI limits apply), subject to the same contribution limits as the limits on deductible contributions, including catch-up contributions.

Roth IRAs

Individuals with AGI below certain levels may make nondeductible contributions to a Roth IRA. The maximum annual contribution that can be made to a Roth IRA is phased out for taxpayers with AGI for the taxable year over certain indexed levels. The AGI phase-out ranges for 2021 are: (1) for single taxpayers, $125,000 to $140,000; (2) for married taxpayers filing joint returns, $198,000 to $208,000; and (3) for married taxpayers filing separate returns, $0 to $10,000.

**Automatic enrollment**

Employer-sponsored retirement plans that include salary reduction arrangements are generally designed so that an employee will receive cash compensation unless the employee affirmatively elects to make elective deferrals to the plan. Alternatively, such plans may provide that elective deferrals are made at a specified rate (when the employee becomes eligible to participate) unless the employee elects otherwise (*i.e.*, affirmatively elects not to make contributions or to make contributions at a different rate). This alternative plan design is referred to as automatic enrollment.

Nondiscrimination test and automatic enrollment safe harbor

An annual nondiscrimination test, the ADP test, applies to elective deferrals under a section 401(k) plan.[21] The ADP test generally compares the average rate of deferral for highly

[21] Sec. 401(k)(3).

compensated employees to the average rate of deferral for non-highly compensated employees and requires that the average deferral rate for highly compensated employees not exceed the average rate for non-highly compensated employees by more than certain specified amounts. If a plan fails to satisfy the ADP test for a plan year based on the deferral elections of highly compensated employees, the plan is permitted to distribute deferrals to highly compensated employees ("excess deferrals") in a sufficient amount to correct the failure. The distribution of the excess deferrals must be made by the close of the following plan year.[22]

The ADP test is deemed to be satisfied under two section 401(k) plan designs ("section 401(k) safe harbor plans"), which include requirements relating to certain minimum matching or nonelective contributions, a notice requirement, and certain other required rights and features.[23] One type of section 401(k) safe harbor plan includes automatic enrollment ("automatic enrollment section 401(k) safe harbor plan").

An automatic enrollment section 401(k) safe harbor plan must provide that, unless an employee elects otherwise, the employee is treated as electing to make elective deferrals at a default rate equal to a percentage of compensation as stated in the plan that is at least (1) three percent of compensation through the end of the first plan year that begins after the first deemed election applies to the participant, (2) four percent during the second plan year, (3) five percent during the third plan year, and (4) six percent during the fourth plan year and thereafter. An automatic enrollment section 401(k) safe harbor plan generally may provide for default rates higher than these minimum rates, but the default rate cannot exceed 15 percent for any year (10 percent during the first year). The plan also must satisfy either a matching contribution ("matching contribution automatic enrollment section 401(k) safe harbor plan") or nonelective contribution requirement.[24]

A matching contribution automatic enrollment section 401(k) safe harbor plan must also meet a notice requirement. The plan must provide each employee eligible to participate, within a reasonable period before each plan year, with a written notice that describes the employee's rights and obligations under the arrangement. Such notice must be sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and must be written in a manner calculated to be understood by the average employee to whom the arrangement applies. In addition, the notice must (1) explain the employee's right under the arrangement to elect not to have elective contributions made on the employee's behalf (or to elect to have such contributions made at a different percentage), and (2) in the case of an arrangement under which the employee may elect among two or more investment options, explain how contributions made under the arrangement will be invested in the absence of any investment election by the

[22] Sec. 401(k)(8).

[23] Sec. 401(k)(12) and (13). If certain additional requirements are met, matching contributions under a section 401(k) safe harbor plan may also satisfy a nondiscrimination test applicable under section 401(m).

[24] The matching contribution requirement is 100 percent of elective contributions of the employee for contributions not in excess of one percent of compensation, and 50 percent of elective contributions for contributions that exceed one percent of compensation but do not exceed six percent, for a total matching contribution of up to 3.5 percent of compensation. Alternatively, the plan can provide that the employer will make a nonelective contribution of three percent. Section 401(k)(13)(D).

employee. The employee also must have a reasonable period of time after receipt of the notice and before the first elective contribution is made to make either such election.

## Description of Proposal

The proposal generally imposes an excise tax on an employer that does not maintain or facilitate an automatic contribution plan or arrangement. There are four general categories of automatic contribution plans and arrangements under the proposal:

1. a defined contribution plan that (a) is a qualified retirement plan, qualified annuity plan, or section 403(b) plan,[25] (b) includes a qualified cash or deferred arrangement or a salary reduction arrangement, and (c) meets the requirements under the proposal relating to notices, eligibility, contribution, investment, fees, and lifetime income (as described below);

2. an automatic IRA arrangement, which in addition to meeting certain requirements applicable to automatic IRA arrangements described below, must meet the requirements relating to eligibility, contribution, investment, and fees;

3. a SIMPLE IRA that meets the requirements relating to notices, contribution, investment, and fees; and

4. a grandfathered plan.

A grandfathered plan is a plan or arrangement that is established and maintained by an employer as of the date of enactment of the proposal, and must be a qualified retirement plan, qualified annuity plan, section 403(b) plan, a SEP, or a SIMPLE IRA.[26] In addition, section 403(b) plans that are not subject to title I of ERISA[27] and that offer annuity contracts or custodial accounts as of the date of enactment are also grandfathered. Grandfathered plans are not subject to the notice, eligibility, contribution, investment, fee, or lifetime income requirements described below.

### Notice requirement

For automatic contribution plans and arrangements subject to the notice requirement (generally all except for automatic IRA arrangements, which have a separate notice requirement), a plan or arrangement meets the notice requirement with respect to an employee if it meets the notice requirements applicable to a matching contribution automatic enrollment section 401(k) safe harbor plan (or similar requirements), excluding any notice requirement that is not applicable or relevant to the particular plan or arrangement.

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[25] Plans described in section 219(g)(5)(A)(i), (ii), and (iv).

[26] Plans or arrangements described in section 219(g)(5)(A)(i), (ii), (iv), (v), or (vi).

[27] 29 C.F.R. sec. 2510.3-2(f).

**Eligibility requirement**

For automatic contribution plans and arrangements subject to the eligibility requirement (generally all plans and arrangements other than SIMPLE IRAs), the general rule is that all employees of an employer must be eligible to participate in an automatic contribution plan or arrangement maintained or facilitated by the employer.[28] However, certain exclusions apply. The plan or arrangement is not required to extend eligibility for participation to (1) an employee who has not attained age 21, (2) certain categories of employees who can be excluded from minimum coverage testing for qualified plans,[29] and (3) employees who have not met the service requirement. An employee has not met the service requirement if the employee has not completed at least one of the following periods: (1) the period of service applicable to the minimum age and service conditions for qualified plans (generally, the period of service ending with the later of the date the employee attains age 21 or the date the employee completes one year of service),[30] or (2) a period of two consecutive 12-month periods during each of which the employee has at least 500 hours of service.

For purposes of these rules, employers within a controlled group are treated as a single employer, and eligible employees within an employer need not be eligible to participate in the same automatic contribution plan or arrangement. With respect to entry dates, rules similar to the rules applicable to qualified plans apply to employees who have satisfied the applicable age and service requirements and are otherwise entitled to participate in a plan or arrangement.[31]

**Contribution requirements**

Under the automatic contribution plan or arrangement, each employee who is eligible to participate must be treated, unless the employee elects otherwise, as having elected to have the employer make elective contributions (payroll deduction contributions in the case of an automatic IRA arrangement) in an amount equal to the applicable qualified percentage of compensation. Such percentage is determined under the terms of the plan or arrangement, subject to certain rules. The qualified percentage must be applied uniformly and must be at least (1) six percent during the period ending on the last day of the first plan year that begins after the date on which the first elective contribution is made with respect to an employee, (2) seven percent during the second plan year, (3) eight percent during the third plan year, (4) nine percent during the fourth plan year, and (5) 10 percent during the fifth plan year and thereafter. The plan or arrangement may generally provide for a qualified percentage higher than these minimum

[28] Automatic contribution plans and arrangements, depending on the type of plan, may also be subject to requirements relating to eligibility under the Code, such as under section 410.

[29] Sec. 410(b)(3).

[30] Sec. 410(a)(1), determined without regard to subparagraph (B)(i) thereof.

[31] Sec. 410(a)(4). Thus, an employee who has attained age 21 and has completed one of the required periods of service applicable to automatic contribution plans and arrangements and who is otherwise entitled to participate must generally be able to commence participation no later than the earlier of (1) the first day of the first plan year beginning after the date on which the employee satisfies the eligibility requirements, or (2) the date six months after the date on which the employee satisfies such requirements.

rates, but the qualified percentage cannot exceed 15 percent for any plan year (10 percent during the first plan year). In the case of an automatic IRA arrangement, however, the qualified percentage must equal the minimum percentage applicable to a particular plan year. Thus, for example, an employee's qualified percentage during the second plan year must be seven percent.

The election to make elective contributions at the qualified percentage ceases to apply to an employee if the employee makes an affirmative election not to contribute or to contribute at a different level.

**Investment requirements**

Under the proposal, the automatic contribution plan or arrangement must provide that, absent an investment election by the participant or beneficiary, amounts are invested only in the specific class of assets or funds described under Department of Labor regulations that is generally referred to as life-cycle and target date funds.[32]

In the case of an automatic IRA arrangement, with respect to any IRA of a trustee or issuer designated by the employer,[33] the IRA must offer the participant the following investment options as alternatives to the default option (and may not offer any other investment options): (1) a class of assets or funds that is designed to protect the principal of the individual on an ongoing basis, (2) the class of assets or funds described under Department of Labor regulations that is generally described as a balanced fund,[34] and (3) any other class of assets or funds determined by the Secretary of Treasury ("Secretary") to be a qualified investment for this purpose.

**Fee requirement**

In the case of an automatic contribution plan or arrangement that is not otherwise subject to title I of ERISA, no participant may be charged unreasonable fees or expenses. This rule applies to an automatic IRA arrangement only in the case of an IRA of a trustee or issuer designated by the employer.

**Lifetime income requirement**

For automatic contribution plans subject to the lifetime income requirement (generally all plans other than SIMPLE IRAs and automatic IRA arrangements), the plan must permit participants to elect to receive at least 50 percent of their vested account balance in the form of a lifetime income feature. A lifetime income feature means either (1) a feature that guarantees a minimum level of income annually (or more frequently) for at least the remainder of the life of the employee or the joint lives of the employee and the employee's designated beneficiary, or (2)

[32] The class of assets or funds must constitute a qualified default investment alternative under Department of Labor regulation section 2550.404c-5(e)(4)(i).

[33] Similarly, the default option of a life-cycle or target date fund is required only under an IRA of a trustee or issuer designated by the employer. The automatic IRA arrangement may alternatively permit employees to make payroll deduction contributions to any IRA specified by the employee.

[34] 29 CFR 2550.404c-5(e)(4)(ii).

an annuity payable on behalf of the employee under which payments are made in substantially equal periodic payments (not less frequently than annually) over the life of the employee or the joint lives of the employee and the employee's designated beneficiary.[35] An exception from this rule applies to a participant whose vested account balance is $200,000 or less at the time of distribution. A plan that applies this rule is not treated as discriminating in favor of highly compensated employees[36] solely by reason of applying such rule.

**Automatic IRA arrangements**

Under the proposal, an automatic IRA arrangement generally means, with respect to an employer (and trustee or issuer designated by the employer), an arrangement under which an employee may elect to have the employer make deposits on behalf of the individual as payroll deduction contributions to an IRA or to have such payments made directly in cash. The employee must be treated under the arrangement as having made an election to make payroll deduction contributions until the employee makes an affirmative election not to have such contributions made or to make the contributions at a different level, and must be permitted to elect to modify the manner in which such amounts are invested. Such contributions must meet the general requirements applicable to contributions to an automatic contribution plan described above. Automatic IRA arrangements must also meet the requirements relating to eligibility, investment, and fees, as described above.

Contributions and employee notices

The proposal also subjects automatic IRA arrangements to certain administrative requirements. With respect to payments under the arrangement, the employer must make payments elected or treated as elected by the employee on or before the last day of the month following the month in which the compensation otherwise would have been payable to the employee in cash. The employer also must notify each employee eligible to participate, within a reasonable period of time before the beginning of the year (and, for the first year the employee is eligible, a reasonable period before the first day of eligibility), of (1) the opportunity to elect to have contributions made (or to be so treated), (2) the opportunity to elect not to have payroll deduction contributions made or to have such contributions made at a different percentage or in a different amount, and (3) the opportunity to modify the manner in which such amounts are invested for such year. The notice must be provided in paper form or, if the employee so elects, in electronic form.

Under the proposal, an employer is not treated as failing to satisfy any requirements under the Code merely because an individual's aggregate contributions to IRAs exceed the limit on deductible IRA contributions,[37] or merely because the employer chooses to limit contributions under the plan on behalf of an employee for a calendar year in a manner designed

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[35] Sec. 401(a)(38)(B)(iii).

[36] Under section 401(a)(4).

[37] The deductible amount in effect under section 219(b)(5) (determined without regard to subparagraph (B) thereof).

to avoid exceeding such limit. In addition, the employer is not treated as failing to satisfy any requirements under the Code merely because the employer makes all payroll deduction contributions on behalf of all employees to an IRA of a trustee or issuer that has been designated by the employer, but only if the provider of such accounts, and the investments therein, are identified on the website established by the Secretary to provide information on automatic IRA arrangements (as described below). However, for such rule to apply, each participant must be notified in writing that the participant's balance may be transferred without cost or penalty to another IRA established by or on behalf of the participant.[38] The employer is permitted, but not required, to provide for an employee election to have payroll deduction contributions made to an IRA specified by the employee. The IRA to which payroll deduction contributions are made on behalf of an employee must be a Roth IRA unless the participant elects otherwise.

Model notice and other directives to the Secretary

The proposal directs the Secretary to issue regulations as necessary to carry out the purpose of the rules relating to automatic IRA arrangements, including establishing procedures to assist employers in connecting with certified and available providers of IRAs and to communicate to individuals the importance of investment diversification.

In addition, the proposal directs the Secretary to issue a model notice, written in a manner calculated to be understandable to the average worker, that is simple for employers to use, to notify employees of the requirement for the employer to provide certain employees with the opportunity to participate in an automatic IRA arrangement, and to satisfy the notice requirements applicable to automatic IRA arrangements as described above. The Secretary must also provide model forms for enrollment, including automatic enrollment, in an automatic IRA arrangement, and establish a website or other electronic means that small employers and individuals can access and use to obtain information on automatic IRA arrangements (including clear, standardized, easy-to-compare information on fees and expenses and investment returns in a format prescribed by the Secretary) and to obtain notices and forms. The information on such website must be provided in a manner designed to assist employers and providers by facilitating the identification by employers of private-sector providers of IRAs, including the provider's investment options, that are appropriate for use in automatic IRA arrangements.

Under the proposal, the Secretary also must establish a process (1) for the provider of an automatic IRA arrangement to demonstrate to the Secretary that the arrangement meets the applicable requirements, and (2) to certify any arrangement that the Secretary determines so demonstrates, to regularly monitor compliance and update such determinations and certifications, and to list all arrangements so certified on the website described above as appropriate for use by employers and participants.

Finally, the proposal requires the Secretary, not later than 90 days after the date of the enactment of this proposal, to establish an Automatic IRA Advisory Group ("Advisory Group"). The purpose of the Advisory Group is to make recommendations, advise, and assist in the Secretary's implementation and administration of the requirements related to automatic IRA

[38] The notice must be provided in paper form or, if the employee so elects, in electronic form.

arrangements, including the investment and fee requirements. Such implementation and administration includes:

- the procedures and criteria for the periodic certification, website listing, and monitoring of investment options that meet the requirements of those paragraphs,
- user-friendly disclosure regarding investment returns, terms, fees, and expenses to facilitate comparison,
- the use of low-cost investment options,
- the appropriate use of electronic and paper methods to provide notice and disclosure,
- any possible learnings or efficiencies based on the Secretary's procedures and experience in approving nonbank IRA trustees, and
- such other related matters as may be determined by the Secretary.

The Advisory Group must consist of not more than 15 members and be composed of such individuals as the Secretary may consider appropriate to provide expertise regarding the financial needs and challenges of lower- and middle-income households. At least one member must be an expert in retirement-related consumer protections or must represent the general public, and at least one member must be a representative of the Department of the Treasury. The members of the Advisory Group serve without compensation. The Department of the Treasury must provide appropriate administrative support to the Advisory Group, including technical assistance, and the Advisory Group may use the services and facilities of the Department, with or without reimbursement, as determined by the Department. Not later than one year after the date of the enactment of this proposal, the Advisory Group must submit to the Secretary a report containing its recommendations. The Secretary may request that the Advisory Group submit subsequent reports.

Safe harbor for certain State-provided programs

Under the proposal, an arrangement facilitated by an employer does not fail to be treated as an automatic IRA arrangement merely because it is provided or otherwise offered, in whole or in part, by a State. This permits a State that currently has an automatic IRA enrollment program for employees working in the State to offer participation in the program to employees of employers who wish to facilitate an automatic IRA arrangement but whose employees work partially or wholly in other States.

Other rules applicable to automatic IRA arrangements

For purposes of the rules applicable to prohibited transactions,[39] if an employer is required under an automatic IRA arrangement to deposit amounts withheld from an employee's compensation into an IRA but fails to timely do so, such amounts are treated as assets of the IRA.

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[39] Sec. 4975(c).

For purposes of the 10-percent additional tax that applies to early distributions from an IRA,[40] such tax does not apply to a distribution to an individual from an IRA that is part of an automatic IRA arrangement if such distribution is made not later than 90 days after the individual is first deemed to have made an election to contribute to the IRA.

**Excise tax**

The proposal imposes an excise tax on an employer[41] for failing to maintain or facilitate an automatic contribution plan or arrangement. The tax is $10 (adjusted for inflation) on any failure with respect to an employee for each day in the noncompliance period. The noncompliance period is the period beginning on the date the failure occurs, and ending on the earlier of (1) the date such failure is corrected, or (2) the date that is three months after the last date on which the employee is required to be eligible to participate in an automatic contribution plan or arrangement maintained or facilitated by the employer.

Exceptions apply to the imposition of the excise tax. The tax is not imposed on an employer with respect to any employee who is eligible to participate in a different automatic contribution plan or arrangement than one or more other employees of the employer.[42] No tax is imposed on any failure during any period for which it is established to the satisfaction of the Secretary that the employer[43] did not know, nor exercising reasonable diligence would have known, that the failure existed. In addition, no tax is imposed on any failure if (1) such failure was due to reasonable cause and not willful neglect, and (2) the failure is corrected during the nine-and-a-half-month period beginning on the first date the employer knew that such failure existed, or would have known exercising reasonable diligence. In the case of taxes imposed on a failure that is due to reasonable cause and not willful neglect, such tax may not exceed $500,000.[44] The Secretary also may waive part or all of such taxes to the extent that the payment of the tax would be excessive relative to the failure involved.

The proposal also exempts certain categories of employers from the excise tax. The tax does not apply to an employer to the extent such employer participates in an arrangement under a qualified State law. A qualified State law is a State law that (1) was enacted before the date of enactment of the proposal, and (2) either requires certain employers to facilitate an automatic IRA arrangement pursuant to a payroll deduction savings program of the State, or allows certain

[40] Sec. 72(t).

[41] The term employer under the proposal includes all employers treated as a single employer under secs. 414(b), (c), (m), or (o). However, all employers, determined without regard to that rule, are jointly and severally liable for liability of any other employer with which they are aggregated for the excise tax under the proposal.

[42] For this purpose, "employer" means any employers treated as a single employer under sections 414(b), (c), (m), or (o).

[43] For this purpose, "employer" includes any employer required to be aggregated under sections 414(b), (c), (m), or (o).

[44] If not all persons who are treated as a single employer have the same taxable year, the taxable years taken into account for this purpose are determined under principles similar to the principles of section 1561.

employers to contribute to, or participate in, a multiple employer plan[45] established and maintained by the State. A qualified State law continues to be treated as such even if it is amended after the date of enactment of the proposal.

The tax also does not apply to any employer with respect to a plan or arrangement that, during the prior calendar year, was maintained or facilitated only by (or included the participation only of) employers each of which had no more than five employees receiving at least $5,000 of compensation from the employer for that year. The tax does not apply to a governmental plan[46] or church plan.[47] It also does not apply to any employer that has been in existence for fewer than two years, taking into account all predecessor employers.

### Effective Date

The proposal is effective for plan years beginning after December 31, 2022.

## 2. Deferral-only arrangements

### Present Law

#### Section 401(k) plans

A section 401(k) plan is a type of profit-sharing or stock bonus plan that contains a qualified cash or deferred arrangement. Such arrangements are subject to the rules generally applicable to qualified defined contribution plans. In addition, special rules apply to such arrangements. Employees who participate in a section 401(k) plan may elect to have contributions made to the plan (referred to as "elective deferrals") rather than receive the same amount as current compensation.[48] The maximum annual amount of elective deferrals that can be made by an employee for a year is $19,500 (for 2021) or, if less, the employee's compensation.[49] For an employee who attains age 50 by the end of the year, the dollar limit on elective deferrals is increased by $6,500 (for 2021) (called "catch-up contributions").[50] An employee's elective deferrals must be fully vested. A section 401(k) plan may also provide for employer matching and nonelective contributions.

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[45] A plan described in section 413(c).

[46] Sec. 414(d).

[47] Sec. 414(e).

[48] Elective deferrals generally are made on a pre-tax basis and distributions attributable to elective deferrals are includible in income. However, a section 401(k) plan is permitted to include a "qualified Roth contribution program" that permits a participant to elect to have all or a portion of the participant's elective deferrals under the plan treated as after-tax Roth contributions. Certain distributions from a designated Roth account are excluded from income, even though they include earnings not previously taxed.

[49] Sec. 402(g).

[50] Sec. 414(v).

In order to constitute a qualified cash or deferred arrangement, no benefit under the arrangement may be conditioned, directly or indirectly, on the employee electing to have the employer make or not make contributions under the arrangement in lieu of receiving cash.[51] However, matching contributions are exempt from this rule.

**Nondiscrimination test**

Actual deferral percentage test

An annual nondiscrimination test, called the actual deferral percentage test (the "ADP" test) applies to elective deferrals under a section 401(k) plan.[52] The ADP test generally compares the average rate of deferral for highly compensated employees to the average rate of deferral for non-highly compensated employees and requires that the average deferral rate for highly compensated employees not exceed the average rate for non-highly compensated employees by more than specified amounts. If a plan fails to satisfy the ADP test for a plan year based on the deferral elections of highly compensated employees, the plan is permitted to distribute deferrals to highly compensated employees ("excess deferrals") in a sufficient amount to correct the failure. The distribution of the excess deferrals must be made by the close of the following plan year.[53]

The ADP test is deemed to be satisfied if a section 401(k) plan includes certain minimum matching or nonelective contributions under either of two plan designs ("401(k) safe harbor plan"), described below, as well as certain required rights and features and the plan satisfies a notice requirement.[54]

Section 401(k) safe harbor contributions

Under one type of section 401(k) safe harbor plan ("basic section 401(k) safe harbor plan"), the plan either (1) satisfies a matching contribution requirement ("matching contribution basic section 401(k) safe harbor plan") or (2) provides for the employer to make a nonelective contribution to a defined contribution plan of at least three percent of an employee's compensation on behalf of each non-highly compensated employee who is eligible to participate in the plan. The matching contribution requirement under the matching contribution basic section 401(k) safe harbor plan requires a matching contribution equal to at least 100 percent of elective contributions of the employee for contributions not in excess of three percent of compensation, and 50 percent of elective contributions for contributions that exceed three percent of compensation but do not exceed five percent, for a total matching contribution of up to four percent of compensation. The required matching contributions and the three percent nonelective

[51] Sec. 401(k)(4)(A).

[52] Sec. 401(k)(3). Long-term part-time workers may be excluded from this and other nondiscrimination tests. Sec. 401(k)(2)(D).

[53] Sec. 401(k)(8).

[54] Sec. 401(k)(12) and (13). If certain additional requirements are met, matching contributions under 401(k) safe harbor plan may also satisfy a nondiscrimination test applicable under section 401(m).

contribution under the basic section 401(k) safe harbor plans must be immediately nonforfeitable (that is, 100 percent vested) when made.

Another safe harbor applies for a section 401(k) plan that includes automatic enrollment ("automatic enrollment section 401(k) safe harbor plan"). Under an automatic enrollment section 401(k) safe harbor plan, unless an employee elects otherwise, the employee is treated as electing to make elective deferrals at a default rate equal to a percentage of compensation as stated in the plan and at least (1) three percent of compensation through the end of the first plan year that begins after the first deemed election applies to the participant, (2) four percent during the second plan year, (3) five percent during the third plan year, and (4) six percent during the fourth plan year and thereafter. An automatic enrollment section 401(k) safe harbor plan generally may provide for default rates higher than these minimum rates, but the default rate cannot exceed 15 percent for any year (10-percent during the first year).[55] The matching contribution requirement under this safe harbor is 100 percent of elective contributions of the employee for contributions not in excess of one percent of compensation, and 50 percent of elective contributions for contributions that exceed one percent of compensation but do not exceed six percent, for a total matching contribution of up to 3.5 percent of compensation ("matching contribution automatic enrollment section 401(k) safe harbor plan"). Alternatively, the plan can provide that the employer will make a nonelective contribution of three percent, as under the basic section 401(k) safe harbor plan. However, under the automatic enrollment section 401(k) safe harbor plans, the matching and nonelective contributions are allowed to become 100 percent vested after two years of service (rather than being required to be immediately vested when made).

Section 401(k) safe harbor notice requirements

Both the matching contribution basic section 401(k) safe harbor plans and the matching contribution automatic enrollment section 401(k) safe harbor plans are subject to an employee notice requirement.[56] Under the requirement, the plan must provide each employee eligible to participate, within a reasonable period before each plan year, with a written notice that describes the employee's rights and obligations under the arrangement. Such notice must be (1) sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and (2) written in a manner calculated to be understood by the average employee to whom the arrangement applies.

Additional notice requirements apply in the case of a matching contribution automatic enrollment section 401(k) safe harbor plan. The notice must (1) explain the employee's right under the arrangement to elect not to have elective contributions made on the employee's behalf (or to elect to have such contributions made at a different percentage), and (2) in the case of an arrangement under which the employee may elect among 2 or more investment options, explain how contributions made under the arrangement will be invested in the absence of any investment

[55] These automatic increases in default contribution rates are required for plans using the safe harbor. Rev. Rul. 2009–30, 2009-39 I.R.B. 391, provides guidance for including automatic increases in other plans using automatic enrollment, including under a plan that includes an eligible automatic contribution arrangement.

[56] Secs. 401(k)(12)(A); 401(k)(13)(B).

election by the employee. The employee also must have a reasonable period of time after receipt of the notice and before the first elective contribution is made to make either such election.

**Description of Proposal**

The proposal establishes a new type of section 401(k) plan, a "deferral-only arrangement," that is treated as satisfying the ADP test.[57] A deferral-only arrangement is a cash or deferred arrangement that meets certain requirements relating to (1) automatic enrollment, (2) elective contributions, and (3) employee notices.

Under the deferral-only arrangement, each employee who is eligible to participate must be treated (unless the employee elects otherwise) as having elected to have the employer make elective contributions in an amount equal to the applicable qualified percentage of compensation. Such percentage is determined under the terms of the arrangement, subject to certain rules. The qualified percentage must be applied uniformly, and must be at least (1) six percent during the period ending on the last day of the first plan year that begins after the date on which the first elective contribution is made with respect to an employee, (2) seven percent during the second plan year, (3) eight percent during the third plan year, (4) nine percent during the fourth plan year, and (5) 10 percent during the fifth plan year and thereafter. The arrangement may generally provide for a qualified percentage higher than these minimum rates, but the qualified percentage cannot exceed 15 percent for any plan year (10 percent during the first plan year). The election to make elective deferrals at the qualified percentage ceases to apply to an employee if the employee makes an affirmative election not to contribute or to contribute at a different level.

In addition, under the arrangement, the only contributions that may be permitted are elective contributions of employees eligible to participate. Thus, the employer may not make matching or nonelective contributions to the plan. In addition, the aggregate amount of any employee's elective contributions for a calendar year may not exceed the contribution limit that is generally applicable to individual retirement arrangements ($6,000 for 2021).[58] Catch-up contributions are permitted (for an employee who attains age 50 by the end of the year) up to $1,000, indexed for inflation.

The arrangement also must satisfy the notice requirement applicable to a matching contribution automatic enrollment section 401(k) safe harbor plan. Similar to section 401(k) safe harbor plans, deferral-only arrangements are not treated as top-heavy plans.[59]

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[57] Sec. 401(k)(3)(A)(ii).

[58] The amount of an employee's elective contributions under the deferral-only arrangement may not exceed the deductible amount in effect for the taxable year under section 219(b)(5), determined without regard to the amount of catch-up contributions described in subparagraph (B) thereof.

[59] Top-heavy requirements apply under the Code to limit the extent to which accumulated benefits or account balances under a qualified retirement plan can be concentrated with key employees. Sec. 416.

## Effective Date

The proposal is effective for plan years beginning after December 31, 2022.

**3. Increase in credit limitation for small employer pension plan startup costs including for automatic contribution plan or arrangement**

## Present Law

### Small employer startup credit

A nonrefundable income tax credit is available for qualified startup costs of an eligible small employer that adopts a new qualified retirement plan, SIMPLE IRA plan or SEP (referred to as an eligible employer plan), provided that the plan covers at least one nonhighly compensated employee.[60] Qualified startup costs are expenses connected with the establishment or administration of the plan or retirement-related education for employees with respect to the plan. The amount of the credit is equal to 50 percent of the qualified startup costs paid or incurred by the employer during the taxable year and is limited to the greater of (1) a flat dollar amount of $500 per year or (2) the lesser of $250 for each nonhighly compensated employee or a flat dollar amount of $5,000. The credit applies for up to three years beginning with the year the plan is first effective, or, at the election of the employer, with the year preceding the first plan year.

An eligible employer is an employer that, for the preceding year, had no more than 100 employees with compensation of $5,000 or more. In addition, the employer must not have had a plan covering substantially the same employees as the new plan during the three years preceding the first year for which the credit would apply. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[61] All eligible employer plans of an employer are treated as a single plan.

No deduction is allowed for the portion of qualified startup costs paid or incurred for the taxable year equal to the amount of the credit.

## Description of Proposal

The proposal modifies the nonrefundable income tax credit for qualified startup costs of an eligible small employer that adopts an eligible employer plan (i.e, a qualified retirement plan, SIMPLE IRA plan, or SEP), other than a deferral-only arrangement as described in section 131102 of the bill. The credit is not available for the startup costs with respect to deferral-only arrangements as described in section 131102 of the bill. Because an automatic IRA arrangement,

[60] Sec. 45E. A nonhighly compensated employee is an employee who is not a highly compensated employee as defined under section 414(q). A qualified retirement plan is a qualified plan under section 401(a) or a qualified annuity plan under section 403(a).

[61] Secs. 52(a) or (b) and 414(m) or (o).

as described in section 131101 of the bill, is not an eligible employer plan, the credit is also not available for these arrangements.

The nonrefundable income tax credit is available for qualified startup costs of an eligible small employer for up to five years beginning with the year the plan is first effective, or, at the election of the employer, with the year preceding the first plan year. For an eligible employer with 25 or fewer employees with compensation of $5,000 or more, the credit is available for 100 percent of qualified startup costs.

For taxable years beginning after December 31, 2022, no credit is allowed for amounts paid or incurred with respect to an eligible employer plan that is not an automatic contribution plan as defined in section 131101 of the bill.

**Effective Date**

The proposal is effective for taxable years beginning after December 31, 2021.

### 4. Credit for certain small employer automatic retirement arrangements

**Present Law**

**Small employer startup credit**

A nonrefundable income tax credit is available for qualified startup costs of an eligible small employer that adopts a new qualified retirement plan, SIMPLE IRA plan or SEP (referred to as an eligible employer plan), provided that the plan covers at least one nonhighly compensated employee.[62] Qualified startup costs are expenses connected with the establishment or administration of the plan or retirement-related education for employees with respect to the plan. The amount of the credit is equal to 50 percent of the qualified startup costs paid or incurred by the employer during the taxable year and is limited to the greater of (1) a flat dollar amount of $500 per year or (2) the lesser of $250 for each nonhighly compensated employee or a flat dollar amount of $5,000. The credit applies for up to three years beginning with the year the plan is first effective, or, at the election of the employer, with the year preceding the first plan year.

An eligible employer is an employer that, for the preceding year, had no more than 100 employees with compensation of $5,000 or more. In addition, the employer must not have had a plan covering substantially the same employees as the new plan during the three years preceding the first year for which the credit would apply. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[63] All eligible employer plans of an employer are treated as a single plan.

[62] Sec. 45E. A nonhighly compensated employee is an employee who is not a highly compensated employee as defined under section 414(q).

[63] Secs. 52 (a) or (b) and 414(m) or (o).

No deduction is allowed for the portion of qualified startup costs paid or incurred for the taxable year equal to the amount of the credit.

**Automatic enrollment**

A qualified defined contribution plan may include a qualified cash or deferred arrangement under which employees may elect to have plan contributions ("elective deferrals") made rather than receive cash compensation (commonly called a "section 401(k) plan"). A SIMPLE IRA plan is an employer-sponsored retirement plan funded with individual retirement arrangements ("IRAs") that also allows employees to make elective deferrals.[64] Section 401(k) plans and SIMPLE IRA plans may be designed so that the employee will receive cash compensation unless the employee affirmatively elects to make elective deferrals to the plan. Alternatively, a plan may provide that elective deferrals are made at a specified rate (when the employee becomes eligible to participate) unless the employee elects otherwise (*i.e.*, affirmatively elects not to make contributions or to make contributions at a different rate). This alternative plan design is referred to as automatic enrollment.

Small employer credit

A nonrefundable income tax credit is available for an eligible employer that establishes an eligible automatic contribution arrangement under a qualified employer plan, requiring the plan to include a cash or deferred arrangement under which participants are treated as having made an election to make elective contributions at a uniform percentage of compensation.[65] Qualified employer plans include 401(a) plans, 403(a) plans, SIMPLE IRA plans and SEPs but exclude governmental plans and plans maintained by tax-exempt employers.

The credit is equal to $500 for any taxable year of an eligible employer that occurs during the period of three taxable years beginning with the first taxable year for which an eligible employer includes an eligible automatic contribution arrangement in a qualified employer plan that it sponsors. No taxable year is treated as occurring within the credit period unless the eligible automatic contribution arrangement is included in the plan for the year.

An eligible employer is an employer that, for the preceding year, had no more than 100 employees with compensation of $5,000 or more. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[66] All eligible employer plans of an employer are treated as a single plan.

**Description of Proposal**

Under the proposal, a nonrefundable income tax credit equal to a flat dollar amount of $500 is available to eligible employers who (1) participate in an automatic IRA arrangement, as

[64] Sec. 408(p).

[65] Sec. 45T.

[66] Secs. 52(a) or (b) and 414(m) or (o).

described in section 131101 of the proposal, including an arrangement pursuant to a qualified State law;[67] or (2) maintain a deferral-only arrangement as described in section 131102 of the proposal. The credit is available during the first four years in which the eligible employer participates in an automatic IRA arrangement or maintains a deferral-only arrangement.

An eligible employer is an employer that, on each day of the preceding year, had no more than 100 employees with compensation of $5,000 or more and did not maintain a qualified employer plan[68] during the portion of the calendar year preceding the adoption of the automatic IRA arrangement or deferral-only arrangement and the two preceding calendar years. Members of controlled groups and affiliated service groups are treated as a single employer for purposes of these requirements.[69] All eligible employer plans of an employer are treated as a single plan. No deduction is allowed for expenses incurred in connection with establishing, maintaining, or facilitating such plan or arrangement, or for expenses incurred in connection with the retirement-related education of employees, equal to the amount of the credit.

**Effective Date**

The proposal is effective for taxable years beginning after December 31, 2021.

[67] Described in section 4980J(a)(2)(A), as added by section 131101 of the proposal.

[68] Sec. 4972(d).

[69] Secs. 52(a) or (b) and 414(m) or (o).

## B. Saver's Match

### 1. Matching payments for elective deferral and IRA contributions by certain individuals

#### Present Law

Eligible taxpayers may claim a nonrefundable income tax credit for qualified retirement savings contributions to certain retirement accounts.[70] Subject to adjusted gross income ("AGI") limits, the credit is available to individuals who are age 18 or older, other than individuals who are full-time students or claimed as a dependent on another taxpayer's return. The maximum amount of the contribution that may be taken into account is $2,000 with a maximum credit of $1,000 per eligible individual.[71]

The amount of the credit is based on the taxpayer's AGI and filing status. The credit is a percentage of the taxpayer's qualified retirement savings contributions with a percentage of 10 percent, 20 percent, or 50 percent, as shown in the table below. The credit is in addition to any deduction or exclusion that would otherwise apply with respect to the contribution. The credit offsets minimum tax liability as well as regular tax liability.

**Table 1.–Credit Rates for Saver's Credit (for 2021)**

| Joint Filers | Heads of Households | All Other Filers | Credit Rate |
|---|---|---|---|
| $0 – $39,500 | $0 – $29,625 | $0 – $19,750 | 50 percent |
| $39,501 – $43,000 | $29,626 – $32,250 | $19,751 – $21,500 | 20 percent |
| $43,001 – $66,000 | $32,251 – $49,500 | $21,501 – $33,000 | 10 percent |

Eligible contributions for purposes of the credit include (1) contributions to traditional and Roth IRAs; (2) elective deferrals to a section 401(k) plan, a section 403(b) plan, a governmental section 457(b) plan, a SIMPLE IRA, or a SEP; (3) voluntary after-tax employee contributions to a qualified retirement plan or annuity or a section 403(b) plan; and (4) contributions to a section 501(c)(18)(D) plan. Public Law 115-97 also added a fifth type of eligible contribution for contributions to Achieving a Better Life Experience ("ABLE") accounts for which the taxpayer is a designated beneficiary. ABLE accounts are savings accounts utilized by individuals with disabilities. A credit for such contributions is available from calendar years 2018 through 2025.

The amount of any contribution eligible for the credit is reduced by distributions received by the taxpayer (or by the taxpayer's spouse if the taxpayer files a joint return with the spouse) from any plan or IRA to which eligible contributions can be made during the taxable year for which the credit is claimed, the two taxable years prior to the year the credit is claimed, and during the period after the end of the taxable year for which the credit is claimed and prior to the

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[70] Sec. 25B; Pub. L. No. 109-290.

[71] See IRS Form 8880, *Credit for Qualified Retirement Savings Contributions*.

due date for filing the taxpayer's return for the year. Distributions that are rolled over to another retirement plan do not affect the credit.

## Description of Proposal

An eligible individual will be allowed a refundable income tax credit, up to $500 (adjusted for inflation), equal to a percentage of qualified retirement savings contributions made by the individual to his or her retirement account.[72] The credit will be paid by the Secretary as a contribution to the eligible individual's applicable retirement savings vehicle. The contribution will be made as soon as practicable after the eligible individual files a tax return making a claim for the credit.

### Qualified retirement savings contributions

The maximum percentage of qualified retirement savings contributions eligible for the credit remains 50 percent, but the maximum amount of qualified retirement savings contributions that may be taken into account is $1,000 (reduced from $2,000 under present law). The percentage is reduced by the number of percentage points which bears the same ratio to 50 percentage points as the excess of the taxpayer's modified AGI for the taxable year, over the applicable dollar amount, bears to the phaseout range.[73] For eligible married individuals who file a joint tax return, the applicable dollar amount is $50,000, and the phaseout range is $20,000. For eligible individuals who file as head of household, the applicable dollar threshold and phaseout range are 75 percent of that in effect for joint return filers. For all other taxpayers, the applicable dollar amount and phaseout range is 50 percent of the amounts in effect for joint return filers. Taxpayers who are eligible for a credit less than $100 but more than $0 will be allowed a credit of $100 under this proposal.

The proposal retains the criteria that individuals who have attained age 18 as of the close of the taxable year are eligible for the credit. An eligible individual does not include any individual who would be claimed as a dependent on another individual's return,[74] or any individual who is a student.[75]

The qualified retirement savings contribution is the sum of the amounts of: (1) the qualified retirement contributions made by the eligible individual,[76] (2) any elective deferrals plus elective deferral of compensation by such individuals under a governmental section 457(b)

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[72] Sec. 6433.

[73] Modified AGI is determined as AGI without regard to sections 911, 931, and 933, and without regard to any exclusion or deduction allowed for any qualified retirement savings contribution made during the taxable year.

[74] Sec. 151.

[75] Sec. 152(f)(2).

[76] Sec. 219(e).

plan,[77] (3) voluntary employee contributions by such individual to a qualified retirement plan,[78] and (4) contributions made by such individuals to an ABLE account of which such individual is the designated beneficiary.[79]

The amount of qualified retirement savings contributions is reduced (but not below zero) by the aggregate distributions received by the individual during the testing period from any entity of a type to which the foregoing contributions may be made. For purposes of determining distributions received by an individual, any distribution received by a spouse of such individual shall be treated as received by such individual if they file a joint return for such taxable year and for the taxable year during which the spouse receives the distribution. An excepted distribution is qualified disability expenses.[80]

The testing period is the period that includes the taxable year plus the two preceding taxable years and the period after such taxable year and before the due date (including extensions) for filing the tax return for such taxable year. Certain distributions made during the testing period are not taken into account for purposes of the reduction.[81] Finally, any portion of a distribution transferred or paid in a rollover contribution[82] to an account or plan to which qualified retirement contributions can be made will not be applied to any reduction in qualified retirement savings contributions for purposes of this proposal.

**Payment of credits**

As previously noted, the credit will be paid in the form of a contribution to the individual's applicable retirement savings vehicle that is an account or plan elected by the individual. An eligible individual must elect to have the contribution made to an account or plan which (1) is a Roth IRA or designated Roth account (within the meaning of section 402A) of an applicable retirement plan;[83] (2) is for the benefit of the eligible individual; (3) accepts contributions made under this proposal, and (4) is designated by such individual, in such form and manner as the Secretary may provide, on the tax return for the taxable year.[84]

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[77] Secs. 402(g)(3), 457(b), 457(e)(1)(A).

[78] Sec. 4974(c).

[79] Sec. 529A.

[80] Sec. 529A(e)(5).

[81] Distributions made during the testing period are not taken into account for purposes of the reduction if made under sections 72(p), 401(k)(8), 401(m)(6), 402(g)(2), 404(k), or 408(d)(4). In addition, distributions to which sections 408(d)(3) or 408A(d)(3) applies are not taken into account for purposes of the reduction.

[82] As defined in sections 402(c), 403(a)(4), 403(b)(8), 408A(e), or 457(e)(16).

[83] Applicable retirement plan is defined in section 402A(e)(1).

[84] A plan or arrangement will not violate any requirement of Code sections 401, 403, 408A, or 457 solely because it accepted such contributions.

A payment of a credit that is a contribution shall be treated as an elective deferral made by the individual which is a designated Roth contribution, if contributed to an applicable retirement plan, or as a Roth IRA contribution made by such individual, if contributed to a Roth IRA, except as provided by the Secretary under regulations. The contribution is not taken into account with respect to any qualified plan limitations.[85]

Any contribution that was erroneously paid, including a payment that is not made to an applicable retirement saving vehicle will be treated as an underpayment of tax[86] for the taxable year in which the Secretary determines that the payment was erroneous. In the case of an erroneous credit, section 72 will not apply to the distribution of such contribution (and any income attributable thereto) if the distribution is received no later than the due date (including extensions) for filing the individuals tax return. Any plan or arrangement to which a contribution is made under this proposal, or from which a distribution is made, is not be treated as violating the requirements applicable to such plan solely by reason of such contribution or distribution.[87]

**Information related to payment of credits**

If an eligible individual elects to have the credit contributed to an account or plan, the Secretary shall guidance to the custodian of the account or the plan sponsor, as the case may be, detailing the treatment of such contribution and reporting requirements with respect to such contribution.

The Secretary is required to: (1) amend IRS Form 5500 to require separate reporting of the aggregate amount of contributions received by the plan during the year; and (2) amend IRS Form 5498 to require similar reporting with respect to individual retirement plans.[88]

**Treatment of the U.S. territories**

The Secretary shall pay to each territory of the United States that has a mirror Code tax system—the U.S. Virgin Islands, Commonwealth of the Northern Mariana Islands, and Guam—amounts equal to the loss (if any) to that territory by reason of amendments made by this proposal. Such amounts will be determined by the Secretary based on information provided by the government of the territory. With respect to any United States territory, a mirror Code tax system means the income tax system of such territory if the income tax liability of the residents of such territory is determined by referenced to the income tax laws of the United States as if that territory were the United States.

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[85] As imposed by sections 402(g)(1), 403(b), 408(a)(1), 408(b)(2)(B), 408A(c)(2), 414(v)(2), 415(c), or 457(b)(2). Also, such contributions are disregarded for purposes of sections 401(a)(4), 401(k)(3), 401(k)(11)(B)(i), and 416.

[86] Such a payment shall not be treated as an underpayment of tax for purposes of Part II of subchapter A of Chapter 68.

[87] The plan is not treated as violating secs. 401, 403, 408A, 457.

[88] Sec. 7701(a)(37) (defining individual retirement plans).

For territories that do not have a mirror Code—Puerto Rico and American Samoa--the Secretary will pay amounts estimated by the Secretary as being equal to the aggregate benefits (if any) that would have been provided to residents of that territory by reason of the amendments made by this proposal if the territory had a mirror Code. The respective territory must have a plan, which has been approved by the Secretary, under which such territory will promptly distribute such payments to its residents in order for the territory to receive amounts estimated to equal aggregate benefits.

A credit under the proposal will not be allowed against income taxes to any person to whom a credit is allowed against taxes imposed by the territory due to this proposal, or who is eligible for a payment resulting from a determination of aggregate benefits in a non-mirror Code territory.

### Effective Date

The amendments made by this proposal shall apply to taxable years beginning after December 31, 2024.

## 2. Deadline to fund IRA with tax refund

### Present Law

There are two general types of individual retirement arrangements ("IRAs"): traditional IRAs and Roth IRAs.[89] The total amount that an individual may contribute to one or more IRAs for a year is generally limited to the lesser of: (1) a dollar amount ($6,000 for 2021); and (2) the amount of the individual's compensation that is includible in gross income for the year.[90] In the case of an individual who has attained age 50 by the end of the year, the dollar amount is increased by $1,000. In the case of a married couple, contributions can be made up to the dollar limit for each spouse if the combined compensation of the spouses that is includible in gross income is at least equal to the contributed amount.

An individual may make contributions to a traditional IRA (up to the contribution limit) without regard to his or her adjusted gross income. An individual may deduct his or her contributions to a traditional IRA if neither the individual nor the individual's spouse is an active participant in an employer-sponsored retirement plan. If an individual or the individual's spouse is an active participant in an employer-sponsored retirement plan, the deduction is phased out for taxpayers with adjusted gross income over certain levels.[91]

[89] Secs. 408 and 408A.

[90] Sec. 219(b)(2) and (5), as referenced in secs. 408(a)(1) and (b)(2)(B) and 408A(c)(2). Under section 4973, IRA contributions in excess of the applicable limit are generally subject to an excise tax of six percent per year until withdrawn.

[91] Sec. 219(g).

A taxpayer is deemed to have made a contribution to an IRA on the last day of the preceding taxable year if the contribution is made on account of such taxable year and is not made later than the due date for the filing of the return (not including extensions).[92]

## Description of Proposal

The proposal provides that a taxpayer may elect on a tax return to have the Secretary contribute all or a portion of any amount owed to the taxpayer to an IRA of the taxpayer to the extent the return is not filed later than the time for filing the return (not including extensions). Such a contribution will be treated as a contribution for the taxable year of the return, regardless of when the refund that funds the contribution is actually paid.

## Effective Date

The amendments made by this proposal shall apply to taxable years beginning after December 31, 2022.

[92] Sec. 219(f)(3).

## C. Estimated Revenue Effect of the Proposal

The following table presents the estimated Federal fiscal year budget receipts of the proposal:

**ESTIMATED REVENUE EFFECTS OF VARIOUS PENSION PROVISIONS**

**Fiscal Years 2022 - 2031**

*[Millions of Dollars]*

| Provision | Effective | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2022-26 | 2022-31 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **SUBTITLE B - RETIREMENT** | | | | | | | | | | | | | |
| A. Automatic Contribution Plans and Arrangements | | | | | | | | | | | | | |
| 1. Tax imposed on employers failing to maintain automatic contribution plan or arrangement [1]................................... | pyba 12/31/22 | --- | -874 | -1,615 | -2,096 | -2,768 | -3,099 | -3,269 | -3,248 | -3,061 | -2,717 | -7,353 | -22,747 |
| 2. Deferral-only arrangements................................................ | pyba 12/31/22 | - - - - - - - - - - - - - - - - - - - - - - - - - - - - - *Estimate Included in Item A,1. Above* - - - - - - - - - - - - - - - - - - - - - - - - - - - - - | | | | | | | | | | | |
| 3. Increase in credit limitation for small employer pension plan startup costs including for automatic contribution plan or arrangement [1]................................... | tyba 12/31/21 | --- | -1 | -3 | -12 | -28 | -62 | -118 | -192 | -280 | -379 | -44 | -1,075 |
| 4. Credit for certain small employers automatic retirement arrangements..................................................... | tyba 12/31/21 | - - - - - - - - - - - - - - - - - - - - - - - - - - - - - *Estimate Included in Item A.3. Above* - - - - - - - - - - - - - - - - - - - - - - - - - - - - - | | | | | | | | | | | |
| B. Saver's Match | | | | | | | | | | | | | |
| 1. Matching payments for elective deferral and IRA contributions by certain individuals..................................... | tyba 12/31/24 | --- | --- | --- | --- | -3,755 | -3,727 | -3,753 | -3,827 | -3,902 | -3,966 | -3,755 | -22,929 |
| 2. Deadline to fund IRA with tax refund................................ | tyba 12/31/22 | --- | --- | [2] | [2] | [2] | [2] | [2] | [2] | [2] | [2] | [2] | [2] |
| **NET TOTAL** ........................................................................................ | | **---** | **-875** | **-1,618** | **-2,108** | **-6,551** | **-6,888** | **-7,140** | **-7,267** | **-7,243** | **-7,062** | **-11,152** | **-46,751** |

Joint Committee on Taxation
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NOTE: Details may not add to totals due to rounding. The date of enactment is assumed to be October 1, 2021.

Legend for "Effective" column:
tyba = taxable years beginning after
pyba = plan years beginning after

| [1] Estimate contains the following budget effects: | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2022-26 | 2022-31 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Total Revenue Effect.................................................................................................. | --- | -874 | -1,615 | -2,096 | -2,768 | -3,099 | -3,269 | -3,248 | -3,061 | -2,717 | -7,353 | -22,747 |
| On-budget effects...................................................................................................... | --- | -881 | -1,647 | -2,163 | -2,884 | -3,263 | -3,478 | -3,497 | -3,343 | -3,001 | -7,575 | -24,157 |
| Off-budget effects...................................................................................................... | --- | 7 | 32 | 67 | 116 | 164 | 209 | 249 | 282 | 284 | 222 | 1,410 |

[2] Negligible Revenue Effect.