

**Comments of**  
**The National Association of Manufacturers**  
**Submitted to the House Ways and Means Committee**  
**Pensions/Retirement Tax Reform Working Group**

**April 2013**

**Overview**

The National Association of Manufacturers (NAM)—the largest manufacturing association in the United States representing manufacturers in every industrial sector and in all 50 states—has long held that our current tax system is antiquated, fundamentally flawed and discourages economic growth and U.S. competitiveness. NAM members strongly support efforts to make the tax code more pro-growth, pro-competitive, fairer, simpler and predictable. We very much appreciate the current focus in the White House and on Capitol Hill on improving our nation's tax system.

Because of manufacturing's critical importance to our nation's economy, any effort to rewrite the federal tax code should result in a balanced, fiscally responsible plan that allows manufacturers in the United States to prosper, grow and create jobs and also enhances their global competitiveness.

To achieve these goals, manufacturers have long held the belief that certain elements must be included in a comprehensive tax reform plan: a corporate tax rate of 25 percent or lower; permanent lower taxes for small businesses; a strengthened, permanent research & development (R&D) incentive; a territorial tax system; and a robust capital cost-recovery system. The NAM discusses many of these goals in greater detail in its submissions to other working groups.

Manufacturers have long provided generous benefits to their employees, reflecting their commitment to their workforce—an essential factor in the success of manufacturing in the United States. To that end, it is important to manufacturers that an improved, pro-job, pro-growth, pro-competitive tax code maintains some key priorities specifically regarding the tax treatment of employee benefits.

In particular, NAM members believe that a tax reform plan should continue to recognize that private-sector employee benefit plans efficiently offer medical, health and retirement benefits to workers. The tax treatment of employee medical, health and retirement benefit plans should permit employers to exercise reasonable discretion in determining the types, coverage, conditions of eligibility, contributions and investments necessary to attract and retain qualified workers in a globally competitive market.

In addition, tax policy should encourage, rather than impede, the adequate funding of private, voluntary retirement plans. Accordingly, income and gains of the assets of such plans should be permitted to accumulate free of all taxes. The federal government can best help individuals attain economic security by fostering economic conditions and incentives that encourage individuals to seek retirement security through personal savings and investment.

A strong Social Security system is also critical to workers' long-term retirement security. Consequently, manufacturers believe that the Social Security system should be adequately funded to preserve the current safety net for American workers. However, the NAM believes that the system's projected shortfalls should not be paid for by increased employer costs. During the current debate, we appreciate the bipartisan support for reforming Social Security by using a more realistic basis for calculating cost-of-living increases. Absent Social Security reform, beneficiaries could face as much as a 25 percent cut to their benefits beginning in 2033. We strongly support Congressional efforts to reach a bipartisan solution to ensure the long-term solvency of this program.

Since this working group aims to better understand and become experts on pension and retirement policy, we want to take this opportunity to more fully detail the manufacturing perspective.

### **Traditional Pension Plans**

Many manufacturers—particularly long-established businesses—offer or have offered their employees “traditional pension” or defined benefit plans (DB plans). For a variety of reasons, including complex regulatory compliance requirements, legal liability, the advent of fierce global competition, longer life expectancies and changing career paths, companies have been exiting the DB plan system. Despite this trend, employers continue to fund these plans long after they are closed. In doing so, employers provide important benefits to long-serving employees who continue to work for the company or have deferred settlement with the plan until their retirement. As Congress works to reform our tax system, we urge you to address several issues that will help foster a better DB system and enable manufacturers to continue to provide these important benefits to employees.

The unpredictable and “pro-cyclical” nature of DB plan funding impedes employers' ability to continue these plans. NAM members strongly supported provisions on pension funding stabilization in Moving Ahead for Progress in the 21st Century (MAP-21), the highway transportation reauthorization enacted in 2012. Unfortunately, the benefits of that stabilization are limited mostly to 2012 and 2013. Beginning in 2014, funding volatility will resume, as a result of the Federal Reserve Board's stated intention to maintain historically low interest rates until at least 2015. As you know, funding burdens tend to become highest during economic downturns—when companies are least able to deal with the additional costs. To continue to maintain DB plans, companies must pursue long-term planning. Because of continued funding uncertainty, many plan sponsors have had to freeze, close or terminate DB plans. If Congress wants to continue to encourage the use of these traditional retirement benefit plans, it must enact long-term fixes that will provide certainty to employers and employees alike.

The growing cost of Pension Benefit Guaranty Corporation (PBGC) premiums imposes an additional financial burden on sponsors of DB plans. While the PBGC was established to serve as the backstop to DB plans, in reality the overwhelming majority of companies will pay out all the dollars they owe their participants without any help from PBGC. Nonetheless, some plan sponsors are forced to pay hundreds of dollars per participant, which can amount to hundreds of thousands—and in some cases millions—of dollars per year. In addition to stabilization provisions, MAP-21 also included a significant increase in employer-paid PBGC premiums. NAM members opposed this increase and believe that additional payments to PBGC only further divert needed resources away from their businesses and make it more difficult to provide benefits directly to their employees.

Manufacturers oppose any additional increase in PBGC premiums as part of tax reform or any other legislative vehicle. We also strongly oppose any effort—such as what we understand was suggested during the MAP-21 discussions—to grant the PBGC the authority to set its own premiums. We believe such an arrangement would result in premiums being set based on a much narrower set of priorities than under current practice and would give too much authority to the PBGC while simultaneously relinquishing Congress’s authority to set premiums.

Finally, the burden created by Section 4062(e) of the Employee Retirement Income Security Act (ERISA) causes continual concern for employers with DB plans. While designed to protect the retirement assets of workers when a company closes its doors, employers can incur huge liabilities to PBGC for simple and routine business reorganizations. Manufacturers believe this provision injects unnecessary uncertainty and possibly significant additional costs into legitimate business planning. We urge Congress to repeal this provision or, at a minimum, reform the statute to require additional transparency from the PBGC in determining whether a Section 4062(e) violation has occurred.

### **Nondiscrimination Rules for Qualified Plans**

Many manufacturers that sponsor DB plans would like to be able to transition from a DB plan to a defined contribution (DC) plan structure to reflect the changing nature of the workplace and employees’ needs. To allow companies to provide a meaningful transition period, the NAM supports a change to the nondiscrimination rules applicable to qualified retirement plans.

In particular, manufacturers support a provision that would allow companies to grandfather a nondiscriminatory group of employees so they may continue to accrue benefits after a plan is frozen and be treated as a nondiscriminatory group on a permanent basis, unless plan amendments modify the group or the benefit formula applicable to the group. The proposal would prevent these frozen plans from violating the rules prohibiting discrimination in favor of highly compensated employees. The current nondiscrimination rules effectively do not allow for any meaningful grandfathering period. This transition concept likely was not considered when the rules were first promulgated.

Without this change, the discrimination tests could potentially have an adverse effect on many manufacturers’ older employees who have many years of dedicated service. For example, the simplest and surest way to currently comply with the nondiscrimination rules is to completely freeze the plan (i.e., close the grandfather period). Another method to comply with the nondiscrimination rules is to remove the highly compensated employees from the plans, starting with those who barely clear the highly compensated employee threshold. Neither of these solutions, however, improves retirement income for employees in the long run.

Many manufacturers have designed their transition from a DB structure to a DC structure in a way that allows their older, long-service employees who are close to retirement to maintain their then-current DB plan. To pass the tests, some companies may now be forced to change the retirement benefit structure (i.e., from DB to DC) of employees who are closest to retirement and have the least amount of time to make up the difference—the very outcome employers sought to avoid by implementing the transition period in the first place.

In sum, the NAM supports changes to the nondiscrimination rules, providing that if the nondiscrimination tests are satisfied as of the date of the plan freeze, then they are deemed satisfied thereafter unless the employer amends the plan to make a material change to the grandfathered group or to the benefit formula.

## Phased Retirement

Employers of all sizes are facing the issue of how to retain their critical talent as large numbers of employees near retirement age. According to the Pew Research Center, approximately 10,000 Americans will turn 65 every day for the next 19 years. This fact is causing many manufacturers to lose the services of these highly skilled, experienced workers because the benefits laws create limited options: continue to work or retire. In already challenging times, companies face a significant loss in institutional knowledge, leadership and talent due to retirements. They do not have the ability to gradually phase these skilled workers into retirement, which would enable the transfer of valuable knowledge to the next generation of workers. This loss will continue unless the law is changed to allow employers to offer an alternative to employees: voluntary phased retirement.

Phased retirement allows an employee who is approaching retirement age to work a reduced schedule and/or different responsibilities for a set period, eventually transitioning from working to retiring. Phased retirement may include a pre-retirement, gradual reduction of work and/or post-retirement, part-time work for pensioners who wish to remain employed.

The benefits of encouraging phased retirement could be significant. Employers would not experience major workforce disruptions or the loss of critical talent and institutional knowledge. Employees who want the additional financial security of employment can continue to work and earn wages and benefits while transitioning gradually into retirement. Although financial resources influence retirement decisions, employees who have a high level of job satisfaction and feel valued by their employers do not necessarily want to retire at the required age. Importantly, allowing employers the flexibility to design bona fide phased retirement programs can help not only address the issue of retaining critical, highly skilled talent, it can also broaden the tax base and reduce the pressure on federal retirement programs such as Social Security and Medicare.

Unfortunately, employers face several barriers to implementing a phased retirement program. Both the tax code and ERISA impose requirements that limit flexibility in retirement plans sponsored by private employers. For example, current law prohibits private sponsors of DB plans from making in-service distributions for employees who have not yet reached normal retirement age<sup>1</sup> or age 62. This age restriction limits the employers' ability to offer phased retirement to workers eligible for early retirement under their pension plans. Importantly, employers will not offer these programs if they are considered a "protected benefit" subject to the tax code's anti-cutback rules. Also, current regulations would make it difficult to pass nondiscrimination testing based on the inclusion of beneficiaries who participate in a phased retirement program.

Of note, last summer, the President signed into law a phased retirement option for eligible Federal employees. The rationale is to encourage the most experienced Federal employees to extend their contributions to the nation and help agencies improve continuity of operations by bolstering mentoring and knowledge-retention programs. The same rationale applies to private employers, who also need the flexibility to offer voluntary phased retirement programs to their critical employees in a nondiscriminatory manner based on workforce needs. By making small changes to the law, phased retirement programs can offer employers the

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<sup>1</sup> It is unclear whether in-service distributions from a DB plan are permitted on the attainment of the plan's early retirement age.

flexibility to design a retirement strategy that makes sense and employees the ability to change what it means to retire.

## **Conclusion**

Manufacturers have a long history of providing generous benefits to their workforce, and the NAM wants to ensure that this tradition, which serves employers and employees alike, continues. To that end, it is important to manufacturers that an improved, pro-job, pro-growth, pro-competitive tax code maintains the key priorities outlined above regarding the treatment of employee benefits.

While the NAM strongly advocates for comprehensive reform of our current tax code, we also believe that it is important to keep our current tax system in place until policymakers agree on a final reform plan. Piecemeal changes or repeal of longstanding rules will inject more uncertainty into business planning, making U.S. companies even less competitive, and threaten economic growth and U.S. jobs.

As outlined in the NAM's [\*A Growth Agenda: Four Goals for a Manufacturing Resurgence in America\*](#), a key objective for the association is to create a national tax climate that enhances the global competitiveness of manufacturers in the United States and avoids policy changes that would increase the tax burden on the manufacturing sector. Manufacturers very much appreciate the efforts of Chairman Camp and the members of the House Ways and Means Committee for their diligent work to reform the U.S. tax system. Manufacturers thank you for the opportunity to share our thoughts and concerns with you, and we look forward to further discussing these issues and working with the Pensions/Retirement Tax Reform Working Group and the rest of the Committee to achieve a pro-growth, pro-competitiveness and pro-manufacturing tax system.