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July 25, 2008

Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D.C. 20044

Re: Automatic Contribution Arrangements; REG-133300-07; 72 Federal Register 63144; November 8, 2007

To Whom It May Concern:

The American Bankers Association (ABA)[1] appreciates this opportunity to provide comments to the Internal Revenue Service (IRS) regarding its Proposed Regulations on automatic contribution arrangements. This letter serves as a follow-up to our testimony at the May 19, 2008, hearing.

Many of our member institutions provide trust or custody services for institutional clients, including employee benefit plans, as well as services to individuals holding retirement assets in individual retirement accounts. As of 2007 more than 1,800 banks and savings associations held in excess of $21 trillion in fiduciary assets for both personal and institutional customers in approximately 20 million accounts.[2] As a result, the IRS' proposed regulation on automatic contribution arrangements is of great importance to the banking industry.

The Pension Protection Act of 2006 (PPA), Public Law 109-208, included provisions designed to encourage the use of automatic enrollment programs by making these programs easier for employers and their service providers to implement. We strongly support the IRS's efforts to implement the PPA's provisions and encourage more employers to adopt automatic enrollment programs. While much of the regulatory work achieved to date by the IRS will greatly assist in these efforts, we believe there are a few areas that would benefit from further revision and clarification.

SUMMARY RECOMMENDATIONS

Our key recommendations are that:

1. Employers should be permitted reasonable flexibility to design their eligible automatic contribution arrangements (EACAs) to apply to some but not all eligible employees.

[1] ABA brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $13.3 trillion in assets and employ more than two million men and women.

[2] FDIC Call Report Data, December 2007

2. Employers should be permitted to implement EACAs during the plan year.

3. More restrictive provisions for permissible withdrawals should be acceptable.

4. Employers should be permitted to treat rehired employees as new employees for EACA and QACA purposes.

BACKGROUND

The Pension Protection Act included provisions to facilitate automatic contribution arrangements. An automatic contribution arrangement is a cash or deferred arrangement that provides that, in the absence of an affirmative election by an eligible employee, the employee will be treated as having made an election to have a specified contribution made on his or her behalf under the plan (a "default election"). The more common term for this arrangement is automatic enrollment.

The new regulations reference two types of automatic contribution arrangements: eligible automatic contribution arrangements (EACAs) and qualified automatic contribution arrangements (QACAs). A QACA, created by the new section 401(k)(13) of the Internal Revenue Code, is a new design-based safe harbor created by the PPA, which will be deemed to have satisfied the Internal Revenue Code's nondiscrimination tests relating to employee elective deferrals and employer matching contributions. An EACA, created by the new Code Section 414(w), is a means to allow for the adoption of a permissible withdrawal provision to return, under certain circumstances, default elective deferrals to participants without either violating Code Section 401(k)(2)(B) or the distributions being subject to the 10% early withdrawal tax of Code Section 72(t).

These regulations were published in November 2007 and were proposed to be effective for plan years beginning on or after January 1, 2008. In the interim, they may be relied upon pending the issuance of final rules. If the final rules are more restrictive than those in the proposed rules, then the IRS has stated that they will be applied prospectively only.

DISCUSSION OF ISSUES

1. Employers should be permitted to design EACAs to apply to fewer than all eligible employees.

We understand that the IRS is interpreting the Proposed Regulations to require automatic enrollment to apply to all "eligible employees" covered by a plan, unless they affirmatively elect otherwise. This interpretation is neither required by the statute nor consistent with the policy behind the implementation of this provision of the PPA. Further, it is unduly burdensome to those employers who were preparing to add EACAs to their 401(k) plans effective in 2008.

Unlike Section 401(k)(13), which indicates that all current employees must participate in a QACA, there is no comparable provision in Code Section 414(w)(3), authorizing EACAs. Section 401(k)(13) generally refers to eligible employees as all current employees. On the other hand, Code Section 414(w) not only does not reference all current employees, but also states that notice must be provided to only certain employees. Specifically the statute only requires notice to be provided to participants covered by certain situations. Clearly, this indicates that Congress, in enacting the PPA, intended certain provisions to apply to all employees and other provisions to apply only to a certain impacted group of individuals.

In addition, nothing in Section 414(w) would lead an employer to believe that the IRS' prior position that automatic enrollment programs need not include all eligible employees had been repudiated by the legislation. In Revenue Ruling 98-30, in which contributions under an automatic enrollment feature were first formally recognized by the Service as elective contributions, the only employees permitted to make contributions under the automatic enrollment arrangement were newly hired employees.

Given the historical development of automatic enrollment, it was reasonable for employers and the practitioners and providers who assist them not to have anticipated that this limitation would be placed on EACAs. Since passage of the PPA in the summer of 2006 but before the IRS issued the proposed rules in November 2007, many employers took the steps needed to implement these arrangements, including design decisions involving what employees would be covered and whether an automatic increase feature would be included, as well as cost analyses. In addition, recordkeeping systems were developed to apply the EACA to fewer than all eligible employees.

The final regulations should continue to offer employers wide latitude and flexibility in structuring their automatic enrollment arrangements--EACAs, in particular. The clear policy of the PPA was to lift barriers that discouraged employers from implementing automatic enrollment. The Proposed Regulations add new barriers to EACAs that heretofore had never been required and we would submit are clearly not required by the PPA. If retained in the final regulations, these restrictions will continue to limit the adoption of these arrangements by imposing new burdens on implementing automatic contribution arrangements for certain employees.

2. Employers should be permitted to implement EACAs during the plan year, rather than at the beginning of the plan year.

The Proposed Regulations appear to require an EACA to be implemented at the beginning of the plan year. The final regulations should be clarified to indicate that implementation during the year is permissible as there is no full-year requirement required under the PPA.

Language in the PPA which provides that QACA notice must be given before each plan year does not support a requirement that EACAs are to be implemented at the beginning of the plan year. Rather, this provision, when read in conjunction with the more specific timing provision of 414(w)(4)(B), requires that the employee have a reasonable period of time to react after the notice and before the first elective contribution. In the absence of a separate, clear, full-year implementation requirement in the statute, it is reasonable to read those two notice timing provisions as simply requiring adequate notice before the arrangement applies to a participant and annually thereafter.

3. Employers should be permitted to design their EACA permissible withdrawals with more restrictive provisions than those specifically set forth in the Proposed Regulations.

The Proposed Regulations are clear that an employer who chooses to offer permissible withdrawals is not required to make the option available to all employees eligible under the EACA. We request that the final regulations provide further clarification of this point.

Specifically, we request that employers be allowed to restrict permissible withdrawals to a select group of employees, provided the group is nondiscriminatory. For example, employers may wish to restrict the withdrawals to employees who have not participated previously in the plan and who have no current deferral election in place (other than the default election) at the time the withdrawal request is made.

4. Employees should be permitted to treat rehired employees as new employees for EACA and QACA purposes.

Finally, the ABA requests guidance on the proper treatment of rehired employees under EACAs and QACAs, particularly where the arrangement includes annual automatic increases in elective contribution percentages. While recordkeeping systems retain certain information on participants for a period of time following cessation of employment, deferral percentages and in-service distribution information are not retained during that period. Therefore, it will be very difficult to modify current systems to ensure that rehired employees resume participation at the levels they were when employment at the firm ceased.

ABA recommends that the Final Regulations provide that rehired employees may be treated as new employees for purposes of both the deferral percentages and permissible withdrawal features.

CONCLUSION

The ABA appreciates the opportunity to have testified at the hearing on automatic contribution arrangements and to follow up with written commentary. We believe the automatic contribution rules will be an important step towards helping more employees save for retirement through automatic enrollment programs. We look forward to working with plan sponsors to put these programs in place. Thank you again for your time and consideration of our views. If you have any questions, please contact the undersigned at 202-663-5479.

Sincerely,

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