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Written Comments Submitted to the Senate Committee on Commerce State of Connecticut

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Hearing on SB 652: An Act Concerning Small Business Retirement Plans

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Mr. Chairman and members of the Committee, thank you for this opportunity to testify on SB 652. I am Michael Callahan, an Enrolled Actuary, and founder of Pentec, Inc., a full-service pension consulting and administration firm located in Southington, CT. Pentec administers nearly 500 retirement plans, most of which are sponsored by small businesses here in Connecticut.

I am speaking on behalf of three different organizations: the American Society of Pension Professionals and Actuaries (ASPPA), which is a national organization of more than 6,500 retirement plan professionals who provide consulting and administrative services for qualified retirement plans covering millions of American workers, particularly those maintained by small businesses; the Council of Independent 401(k) Recordkeepers (CIKR), which represents firms providing recordkeeping services for 401(k) plans with assets in excess of $120 billion; and the Small Business Council of America (SBCA), a national organization whose purpose is to represent the interests of private and family owned businesses in federal income and estate tax, health care, pension and other benefit concerns. All of these organizations focus on issues affecting small businesses and are well-qualified to comment on small employer retirement plan legislation such as SB 652.

All three organizations have consistently and actively supported other proposals to expand small business retirement plan coverage. This has included a federal tax credit enacted in 2001, which provides small businesses with up to a $500 annual tax credit for the start-up costs of a new small business retirement plan. However, we all oppose SB

652, because the bill is not likely to expand coverage, and may in fact do more harm than good.

SB 652 is based on two assumptions: first, small employers do not set up retirement plans because there are no low-cost options available in the marketplace, and second, a state-sponsored 401(k) plan would reduce fees – supposedly by as much as half. Neither is true.

Low-cost retirement plans for small employers exist in the market place right now. For example, Congress created SIMPLE IRA plans with no significant administrative costs specifically for small employers that do not want the cost or responsibility of a full blown 401(k) plan. In Connecticut both the Connecticut Business and Industry Association and the Connecticut Chamber have already developed "pooled" retirement plans with lower fees for small businesses in the state.

In preparation for this testimony, we checked on fees available in Connecticut for SIMPLE IRA plans. We found a small employer can pay $10 per employee to set up a SIMPLE plan and $10 per person per year for administration – hardly burdensome out-of-pocket costs for the employer. Congress also wanted to help employers set up more flexible plans, like 401(k) plans. If an employer has not sponsored a plan for the past three years, the federal government will actually pay part of the first three years of administrative costs through a tax credit of up to $500 per year.

If an employer doesn't want to set up a retirement plan, it is generally either because the employer is not educated about available options, or the employer does not want to commit to making contributions for employees each year. SB 652 doesn't address either problem.

There would be little, if any, cost savings under a state-sponsored 401(k) plan. A state-sponsored 401(k) plan for small business would be much more expensive to administer than the state's 403(b) or 457 plans. There are practical reasons any business person should understand – like the additional cost of collecting payroll information and contributions from hundreds of small employers instead of from established governmental payroll systems. But more importantly, 401(k) plans are subject to different, far more detailed, federal rules than 403(b) or 457 plans for state employees.

ERISA, the labor law that protects employees' rights to benefits, does not apply to plans for state and local government employees – but it does apply to small employer and private not for profit retirement plans. The ERISA rules, and Internal Revenue Code non-discrimination requirements, are designed to protect rank and file workers. These rules are important -- they are also complicated and time consuming.

It is critical to understand that each and every private business is required to adopt a plan, and perform required testing, as a single employer. This requirement creates a long list of responsibilities for the service provider for each plan. One of the first steps can be among the most complicated – determining if the employer is a stand-alone business, or part of a controlled group or affiliated service group. This means the state would have to request ownership information from the employer-- not just ownership in the small business, but what other businesses the owners own in case the small business needs to be

combined with other businesses for testing under controlled group or affiliated service rules. Once the administrator has determined what constitutes the employer for purposes or retirement plan coverage and discrimination testing purposes, the administrative tasks can begin. These tasks include (1) gathering payroll data from multiple sources; (2) determining if the data is complete, and if the right elements of pay have been included or excluded; (3) reviewing reported hours worked for reasonableness, and use the information to adjust vesting and determine which employees must be included in testing and contribution allocations; (4) determining key employees and HCE's; (5) completing discrimination and top heavy testing and retesting; (6) determining and processing refunds to correct any failed testing; (7) allocating employer contributions according to the plan's formula and (8) completing required federal filings and notices. Other services that must be provided on an ongoing basis include administering loans and defaults on loans; distribution processing; document processing and amendments; and compliance with federally mandated ERISA requirements such as providing communication, website, and educational materials necessary to fulfill its fiduciary duty to small business and the workers.

There is no easy way around the rules and there should not be – the rules are designed to protect rank and file employees. There also is no magic that will allow the state of Connecticut to test hundreds of plans more efficiently than businesses that have been doing the work for years.

In the private pension system today, plan advisors – actuaries, administrators, accountants and attorneys -- help employers choose the plan that is best for that small business and its workers, and operate the plan in accordance with federal law and regulations. Is the state ready to bear this burden for each and every plan and worker? Who will represent the small business if the IRS or DOL audits their plan? And will the state recover these expenses from program assets, *i.e.* workers, as well? These are just a few real downsides faced by private service providers every day – and the state would bear the same burden. The state will not be able to eliminate its responsibility for the risk of non-compliance by contracting with a third party.

Connecticut should not compete with its own small, private businesses unless there is a market failure. State governments should only step in private markets if there is an inherent unfairness which disadvantages its citizens. In Connecticut, the marketplace for 401(k) plans and other pension vehicles is robust and highly competitive. Connecticut's private service providers compete in this market and create jobs and pay taxes. SB 652 would allow the state to compete directly with private service providers even though small businesses already have many options to provide pension plans, along with multiple opportunities to avoid or limit costs.

SB 652 is a well-intentioned, but very bad idea. The state's creation of a 401(k) plan for small businesses and tax exempt entities will only cause harm to they very system it would be trying to help. The effort would be better spent on educating employers about existing options, or giving employers a tax credit to help make the contributions that are the real roadblock to establishing a plan.

The Committee should oppose SB 652.