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April 16, 2012

The Honorable Kevin de León
California State Senate
State Capitol, Room 5108
Sacramento, CA 95814

RE: SB 1234, An Act relative to universal retirement accounts

Dear Senator De León:

The Financial Planning Association® (FPA®) shares your goal of helping more Californians prepare for their retirement. However, we wanted to share our concerns with Senate Bill 1234, which you introduced on February 23, 2012.

About FPA

FPA is the largest membership organization for personal financial planning experts in the U.S. and includes professionals from all backgrounds and business models. FPA members adhere to the highest standards of professional competence, ethical conduct and clear, complete disclosure to those they serve.

FPA has 13 state chapters in California with hundreds of members who participate in numerous community outreach efforts across the state. Through these pro bono and consumer initiatives, our members help enhance financial literacy and provide assistance to Californians in need. Throughout the past year, FPA's California chapters have served thousands of individuals who need financial planning counsel. Examples of outreach efforts include: pro bono financial planning one-on-one consultations to military personnel and families; Boy Scouts educational seminars; Financial Education in high schools and colleges; Red Cross Disaster Relief; Families Forward; Council on Aging in OC; Women's Shelter; Junior Achievement; Job Corps; and Earned Assets Resource Network. Last year, seven FPA Chapters hosted financial planning clinic events in California which provided one-on-one support and group presentations on topics including Employee Benefits Planning, General Financial Planning, Estate Planning, Income Tax Planning, Insurance Planning, Investment Planning and Retirement Planning.

A Savings Crisis

More than just failing to save for retirement, Californians are simply not saving enough at all. Too many Americans do not have an emergency account for unexpected events, nor have they saved for predictable near-term events, like education expenses for their children or maintenance for their car. Many are living just a few paychecks away from financial insolvency. A survey conducted by FPA and other groups found that one third of Americans would be unable to pay their rent or mortgage payment within one month of losing their job.

Senate Bill 1234

SB-1234 contemplates direct and active involvement by the state in the private retirement account market. However, there does not appear to be a failure by the market to provide savings opportunities as evidenced by the large number of readily-available, low-cost financial products and tax-deferred individual retirement accounts (IRAs). Nor does SB-1234 address the root cause of this savings deficit: a fundamental lack of financial literacy by most of the public.

The state government could better address this issue through educational efforts, such as creating a financial literacy graduation requirement for high school students and greater

outreach to adults. Currently, there are twenty-four states that have such a requirement¹. It could also provide state incentives to encourage the creation of employer-provided retirement plans or to reward savings similar to the federal Saver's Credit. FPA and other groups would gladly partner with the state to educate citizens about these opportunities.

Should the state decide to embark on providing a state-run retirement benefit, it may improve individual's long-term retirement preparedness at the expense of their short and mid-term financial needs. IRAs and defined contribution plans allow individuals to access their savings in the event of financial hardship. IRAs allow for withdrawals for the purchase of a first home and contributions to a Roth IRA may be withdrawn for any reason to the extent of basis. Many defined contribution plans allow participants to take loans from their accounts. While these features do create leakage of retirement savings to other uses, they provide a critical safety net for immediate financial troubles. In addition, the ability to access one's contributions can encourage greater savings simply because individuals know their money isn't locked out of reach until retirement.

Further, we strongly encourage you to carefully examine the interaction of this proposal with current federal tax laws and the Employee Retirement Income Security Act (ERISA). If the state-run retirement plan operates outside of these laws, many low-income participants might lose access to tax deductions, credits and protections provided by the federal government.

For instance, a key driver to participation in defined contribution plans is the employer match, and to a lesser extent the deductibility of the employee's contribution. If the state-run plan is not recognized as a qualified plan under the internal revenue code, contributions by the employer would be likely treated as additional compensation to the employee. This would result in workers owing more taxes but with no more cash to pay the bill, an unfortunate outcome that would discourage participation. Also, contributions to the state plan may not be eligible for the federal Saver's Credit (IRC section 25B). Low-income individuals would likely forfeit this federal benefit of up to \$1,000.

Finally, this bill would create a new liability for the taxpayers of California. The current pensions plans offered by the state and local governments are putting substantial strain on government budgets. There is ample evidence that the current method of accounting for future pension liabilities is overly optimistic and understates the level of underfunding. Creating a new pension program will only compound this problem.

Financial planners are keenly aware of the lack of saving by the public. The proposed legislation contemplates dramatic involvement by the state government in the private retirement market and there is significant legal uncertainty regarding the bill's interaction with existing federal laws. Coupled with the state's budget issues and overly-generous accounting for its current pensions, the issue warrants extreme caution before creating a new retirement system that is duplicative to what is already available in the private market.

We appreciate the opportunity to provide input on this legislation. If you have any questions, please contact Phillips Hinch at (202) 449-6340.

Sincerely,



Daniel Barry
Managing Director of Governmental Relations & Public Policy
Financial Planning Association

¹ <http://www.jumpstart.org/state-financial-education-requirements.html>