Senate measure would exempt DB plans from minimum corporate tax

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Defined benefit (DB) pension plans and other post-retirement benefit plans would be exempt from Democrats' proposed minimum corporate tax, under draft legislation recently released by Senate Finance Committee Chairman Ron Wyden, D-OR. The carve-out responds to concerns raised by the American Benefits Council, Mercer and other stakeholders that the tax would give rise to a host of anomalies and counterproductive incentives harmful to the private pension system.

Proposed minimum tax. The House-passed Build Back Better Act (BBBA) (HR 5376) includes a controversial 15% minimum corporate income tax on entities with accounting income exceeding $1 billion, effective next year. Income reported on a company's financial statement or "book income," including gains and losses in DB plans, would determine whether the tax applies. This could subject affected DB plan sponsors to volatile tax liabilities due to fluctuations in the value of plan assets and interest rates. Moreover, by applying to accounting pension income, the tax would effectively eliminate deductions for plan contributions. Companies that have adopted "mark-to-market" accounting standards could be hit especially hard by these changes.

Senate would keep plans under current tax rules. The new Senate proposal would adjust financial statement income to effectively apply current income tax rules to DB and other post-retirement plans. The Finance Committee measure is not Senate Democrats' final draft; lawmakers are still working through a number of contentious unrelated issues. However, the pension plan protections are not controversial and will likely remain in the bill.

House-approved revenue raisers retained. Like the House-passed bill, the Finance measure includes retirement-related revenue raisers to help offset the cost of the bill. Those provisions include a ban on Roth conversions of after-tax contributions in employer retirement plans, a cap on aggregate defined contribution (DC) plan and individual retirement account (IRA) balances for high earners, and new restrictions on conversions and rollovers to Roth DC plan accounts and Roth IRAs. Earlier House proposals to substantially expand the saver's credit and require employers without retirement plans to offer automatic-enrollment DC plans or IRAs were dropped due to cost concerns. Neither of those proposals is expected to make a comeback in this Congress, despite pleas from supporters.

Christmas deadline in question. Democratic leaders and President Biden hope the Senate can pass its version of the BBBA before Christmas, though that appears to be an increasingly uphill battle. A key concern is whether Sen. Joe Manchin, D-WV, and other lawmakers will support the measure. Democrats need unanimous support to move the package out of the Senate under the budget reconciliation process. The House would then need to approve whatever the Senate passes before sending the bill to the president.

That process might well extend into next year, which could push out some effective dates, including the proposed 2022 start for prohibiting Roth conversions of after-tax contributions in qualified plans and IRAs. Plan sponsor groups are urging lawmakers to delay the provision's effective date and apply the ban only to high-income individuals, but the outlook is uncertain. In any event, any final legislation will likely include some form of restrictions on Roth conversions and limits on account balances.

Related resources

Non-Mercer resource

- Legislative text of draft portion of the BBBA (Senate Finance Committee, Dec. 11, 2021)

Mercer Law & Policy resource

- House OKs Roth conversion ban, tax hit for some DB plan sponsors (Nov. 19, 2021)

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