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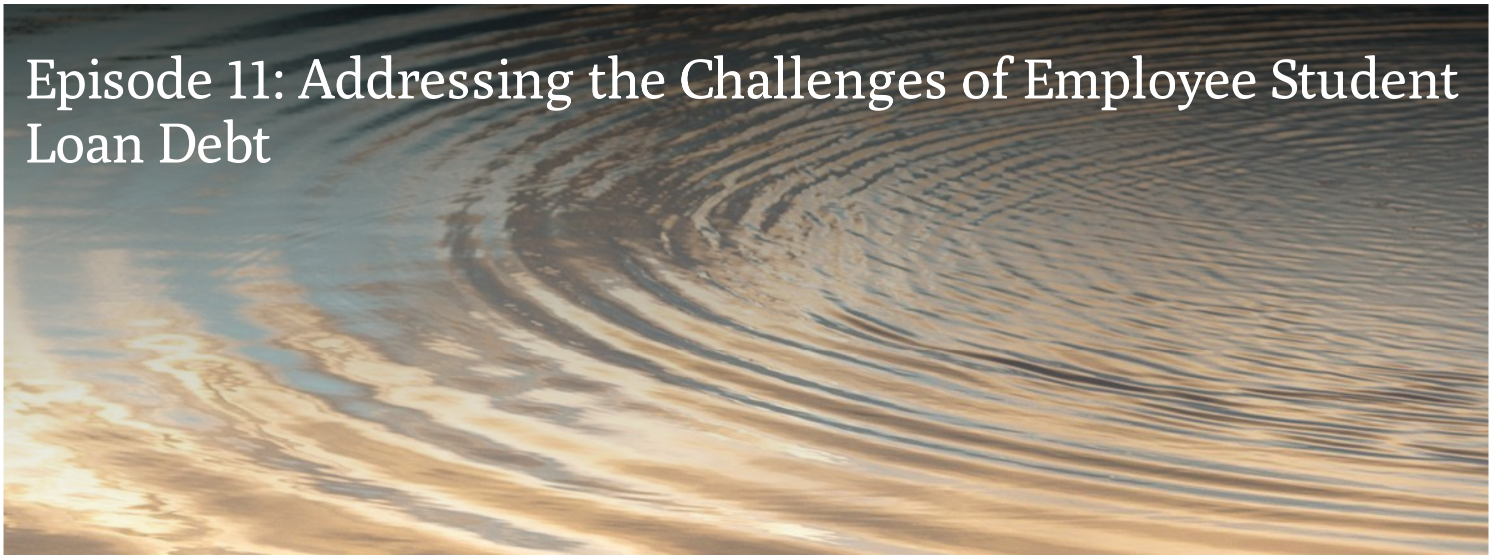
**PODCAST**

# Episode 11: Addressing the Challenges of Employee Student Loan Debt



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**Audio Transcript:**
**Joe Adams:** Welcome to Winston's Benefits Blast Podcast, where we explore innovative ideas and trends in employee benefits and executive compensation. I am Joe Adams, and I am joined today by my partner, Anne Becker. During this episode, we will be talking about how smart employers are helping their employees address the challenges of student loan debt. And, in this podcast, we're going to cover four topics:

- What is the scope of the problem?
- How common are employer programs at this point?
- What solutions have been tried so far (and we will walk through several different proposed solutions)? and
- What is next on the administrative and legislative front.

So, Anne, with that, can you give us a little background on the scope of the problem?

**Anne Becker:** Sure, Joe. Most listeners will be familiar to a certain extent with the scope of the student loan problem, because it is in the news quite a bit. But here are a few facts to set the stage:

- The balance on outstanding student loans reached 1.6 trillion dollars at the end of the first quarter, and more than a quarter of that is held by people younger than 30.
- The average person has a student loan balance of $33,332, according to the data from the American Institute of CPAs.
- And finally, a recent TIAA-MIT Agelab study finds that 73% of student loan borrowers delay maximizing retirement savings to pay off their debts.

And, as you know Joe, when employees don't make 401(k) contributions to their employer savings plans, often they also miss out on those employer-matching contributions.

So, how are employers reacting to this missed opportunity?

**Joe Adams:** That's a great question, Anne. We really want to hammer home that point, because I think we see that frequently with our employers, as many of our employers have switched away from defined benefit plans to 401(k) plans as their main retirement vehicle. When you have employees that are delaying making 401(k) contributions because of their student loan debt, it does delay the extent to which they are accumulating retirement assets and really delays the point which they can retire. So, a lot of smart employers worry about a retirement adequacy problem, specifically that their employees might not be able to *afford* to retire at some point.

We are seeing employers look at trying to solve this problem, and the programs are growing in popularity. One study from 2019 by the Society for Human Resources Management, SHRM says that 8% of employers were offering such programs in 2019. Although that might seem like a small percentage, that's double what the percentage was in 2015, so we definitely see a trend growing there. Then another firm, Willis Towers Watson, did a survey, and according to their data, they believe that 32% of firms will be offering *some* sort of benefit by 2021.

So, there is a need for active, smart employers to actively go about trying to solve this problem. And we think it's really driven by two things:

- One, there's competition for talent. So, if you have a young demographic in your workforce, this might be a great way you can differentiate yourself from other potential employers.
- And two, there is the significant debt burden that you talked about, Anne, that is also really driving the need for solutions.

So, I think this will segue into our four different approaches that have been tried before. The utilization of these employer programs has been somewhat low up until now because of the cost, frankly. I think a lot of employers don't have the extra funds. So, some of these solutions – I like to think of them as Versions 1.0, 2.0, et cetera – have a tangible cost where employers are actually spending hard dollars and it is difficult for some employers to come with those hard dollars. But why don't we jump into what would we describe as "Version 1.0" in terms of solutions that have been tried so far, Anne?

**Anne Becker:** Sure, Joe. I think Version 1.0 would be employers who are helping their employees get a better rate on those student loans. Many employers now partner with firms to offer employees an ability to refinance their student loans by consolidating payments, lowering interest rates, and similar features. Our law firm, Winston & Strawn, offers Common Bond. Other similar firms include SoFi, Tuition.io, Goodly, Gradifi. So, there are many firms that provide these consolidation opportunities for employers, and there are some obvious benefits to these programs. They don't cost a lot unless the employer wants to make a contribution to these refinancings, and they are relatively easy to implement. These other firms administer the programs on behalf of the employers.

If the employers want to contribute to help their employees with the payments, there are a couple of ways they can do that: They can subsidize the interest rate potentially, or they could reimburse employees a certain amount each month to cover a portion of their employees' student loan repayments. I guess theoretically, we've also tossed around the possibility that the employer could buy the debt. But I don't think we've ever seen that, right Joe?

**Joe Adams:** We have not. No. So I think yeah, this seems to be the most common, this Version 1.0. To just say, "*This is on our employee webpage, where we have discount programs for if you need to buy a new TV, or you want to refinance your mortgage. Well, now we have a way to refinance your student loans. . . .*"

It is an easy thing for an employer to roll out, and like you said, I think the most common add-ons to Version 1.0, which will lead us to Version 2.0, is can the employer help with the payments. So, we've helped you refinance it and maybe, as long as you work here, we will subsidize the interest rate. If you quit, then you lose the subsidy which can be sort of a retention device, meaning that if you quit, you don't get the subsidized interest rate anymore.

So that is a nice summary of Version 1.0 in terms of things employers are doing.

The next approach we see we'll call Version 2.0, where the employer would just provide some money to help. And there's lots of examples of this in terms of XYZ Big Brokerage Firm, or ABC Accounting Firm, or some large healthcare company providing their employees, new employees, with a benefit that seems to be on average of $2,000 a year, maybe up to a $10,000 cap, to pay for their student loans. In terms of the pros and cons of Version 2.0, one of the main benefit is somewhat like in Version 1.0: this type of program is relatively easy to implement. You need some documentation to do it, but a pretty straightforward implementation.

As I said at the outset, employer utilization of these programs is low, and that points to one of the drawbacks of Version 2.0 in that involves a hard cash cost. So, for many employers, there's a cash/expense issue; we have to make sure we have money to provide that additional benefit. At some level, it also may presents a fairness issue with which some folks in the HR community may struggle. Specifically, a concern that some employees will say, "*Well, my coworker gets $10,000 a year, but I don't have college debt because I went to a lesser school, I went on scholarship, I worked part time, etc*." So, you have that issue to think about. But I think, by and large, the leading issue with Version 2.0 is the expense issue: we just don't have room in the budget to provide an extra benefit like that.

So, that that leads us to what we call Version 3.0, where employers trying to figure out, is there a way we can repackage some of our *existing* spend to provide this employer benefit?

**Anne Becker:** Right. One idea to that point, Joe, is to allow employees to contribute their paid time off in one fashion or another.

Another idea, which has received a lot of attention lately, is a plan design under which employees can receive a matching contribution based on 401(k) contributions that they make to their employer savings plan, or a non-elective student loan contribution that the employer makes on their behalf to the plan. But they can't get both. So, the employees either get a matching contribution on their 401(k), or they get a separate stand-alone student loan contribution from the employer. This approach was recently approved by the IRS in a Private Letter Ruling, and this approach was carefully designed to satisfy a technical issue: the contingent benefit rule. That rule states that no other benefit may be conditioned, directly or indirectly, on an employee's decision to make or not to make 401(k) contributions to a plan. Matching contributions are exempt from this rule, but student loan contributions are not; they are subject to this technical contingent benefit rule.

So, in this Version 3.0, the ordering of any matching contribution and any student loan contribution becomes important. And, employers considering this approach should also analyze who will administer the program and who will track student loan payments for purposes of a non-elective student loan contribution to the 401(k) plan? In addition, employers should know that there are some non-discrimination testing issues that are attached. The plan would need to perform coverage and amounts testing for each element of each feature of the plan – the 401(k), the match, and the student loan contribution. Then, last but not least, this Version 3.0 may not be available or workable for Safe Harbor plans. Those are plans that provide a specific benefit to all employees in a plan in order to avoid nondiscrimination testing.

**Joe Adams:** That's right, Anne; well said. The two hang-ups, or at least two takeaways here from this Version 3.0, is that you need to understand exactly that this is frequently communicated to employees as a "matching contribution" but it's *not* technically a matching contribution; the student loan contribution is a profit-sharing contribution, and certain IRS testing consequences that flow from that. We can certainly address all of those, but it is just something you need to be aware of and make sure you're thinking about.

Then, as you mentioned, the limitation on Safe Harbor plans is a real problem. If you have a Safe Harbor plan design where people put in a 401(k) contribution, they have to get a match. Again, the design Anne described is really premised on an employer that can't afford to give *both* a match and a student loan contribution. But in a Safe Harbor plan, the participants would have to get both.

That leads us to what we might describe as Version 4.0 in terms of what's coming next, and in terms of where we might get relief both on the regulatory/administrative level from the IRS and on the legislative level from Congress.

We had a meeting with the IRS and Treasury a couple months back, and they have indicated a willingness to address this issue and provide guidance that *all* employers could rely on. The Private Letter Ruling only applies to the one taxpayer to whom it was issued, is the standard caveat on IRS Private Letter Rulings. The rulings are indicative of the IRS's thoughts on a particular issue, but it can only be relied on by that one particular taxpayer. So, the idea is the would issue a Revenue Ruling that is similar to the Private Letter Ruling, and other taxpayers could rely on it. I think Treasury and IRS have started the process of issuing the Revenue Ruling; they are very inclined to help. They were very responsive to everyone's concerns, and I think they're inclined to help as best they can within the confines of the statute, the tax code.

The thought is that any relief contained in a Revenue Ruling would probably be very similar to the Private Letter Ruling. It would cover a 401(k) plan with sort of a make-whole "matching" contribution based on student loan repayments. However, the proposed Revenue Ruling likely would not cover Safe Harbor plans. As we just discussed, lots of our clients have switched to Safe Harbor 401(k) plans where people are guaranteed to get a certain level of match, so that would be the gap in the Revenue Ruling.

So that brings us to the legislative relief. In that regard, there is a couple of proposals have been floating through Congress that would similarly kind of mimic the approach that the IRS took forth in the Private Letter Ruling. I think that's part of the magic here, is if we get a Revenue Ruling from the IRS that says, "*This works for a regular 401(k) plan but doesn't work for a Safe Harbor plan*," then there will be a need for Congress to act and say, "*Okay, now we need to enact guidance that covers Safe Harbor plans*." We'd have the same approach from the Private Letter Ruling, confirming that de facto "matching contributions" based on student loan repayments would work. And, actually, some of the proposals would simplify the discrimination testing concerns that Anne raised because the student loan contribution would essentially be *treated* as a matching contribution – even though it was a profit-sharing contribution, it would be tested as a matching contribution – which would simplify discrimination testing greatly. The legislation would also

- apply to Safe Harbor plans, and
- apply to 403(b) plans, which are similar 401(k) plans but for employers in the tax-exempt area. Obviously, since the Private Letter Ruling was issued by a for-profit entity, it only covers 401(k) plans.

So, the proposed legislation would also broaden that. Hopefully we'll get legislative relief. It had almost incredibly bipartisan support. A couple of versions of this were reported out. It's stalled a little bit due to some stuff in Congress right now, but hopefully this will get enacted.

Another thing that's been proposed is a bill called the Employer Participation in Repayment Act, which would sort of piggyback off an old tax code benefit Section 127 that allows employers to pay up to $5,250 on a tax- free basis for employees to attend school *currently*. The idea would be to sort of expand that *retroactively*, so it could cover student loan debt.

So, hopefully more good things to come on the administrative and legislative fronts. Anne, did I miss anything?

**Anne Becker:** No. You did great.

**Joe Adams:** Excellent. We would like to thank everyone for listening in to another edition of Winston's Benefit Blast Podcast. We would ask you to please make sure to stay tuned for future episodes, as we provide more insights on the latest legislative, regulatory, and practical developments regarding employee benefits and exec comp. We would also ask you to subscribe to our blog. You could do that by going on our website at winston.com, and there you can also find other updates on the latest legal developments in the employee benefits area.

Our thanks to everyone for your attention.

## Speakers

Joseph S. Adams

Anne Becker

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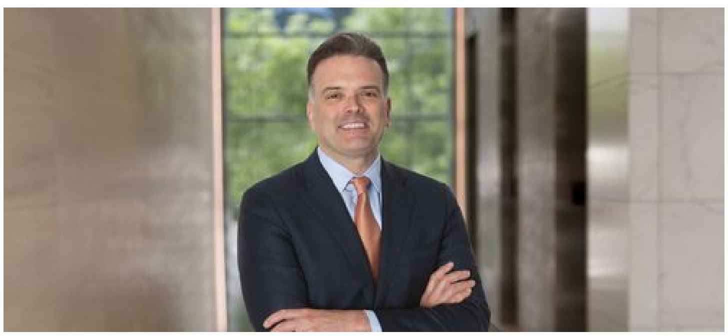

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