Plan Sponsor
OUTLOOK

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A RESOURCE ON CURRENT ISSUES FOR PLAN SPONSORS AND ADMINISTRATORS

On the Horizon in 2015: A Closer Look at DC Plan Investments

Today's 401(k) plans bear a resemblance to the ones introduced in the late '70s and early '80s. Employees still defer a portion of their pay. However, plan features have changed a lot as the industry has learned more about participant needs and behaviors.

One area of significant change is in how the plan's assets are invested. And, it appears that more changes are underway. A recent paper points out several areas in which the investment menus of defined contribution plans seem to be evolving. It may be worth considering your own investment menu as you read through these trends:

- **Menu Consolidation** – A decade or two ago, plan sponsors (and their participants) believed that more was better in investment options. Actual participant behavior has shown that to be untrue. A trend toward limiting the number of investment options began in the last few years and does not appear to be letting up. Narrowing the number of available choices down to just one, or possibly two, funds in each core asset class is becoming the norm as plan sponsors strive to improve participant outcomes. How do limited investment choices and improved outcomes correlate? Participants who are overwhelmed by the sheer number of choices often fail to decide how to invest, leaving their money to sit on the sidelines in cash or an equivalent (an acceptable default investment in the early days). Offering fewer options, as well as improved qualified default investment alternatives, can be helpful in encouraging participants to take action.
- **Alternative Investment Vehicles** – Plan sponsors continue to strive for fee reduction, in part because it is a fiduciary responsibility to get value for their fees. One result is many are taking another look at mutual funds, the traditional funding vehicle in 401(k) plans. Collective investment trusts, separate accounts and exchange-traded funds, all of which may carry lower expense ratios, have led some plan sponsors to use them instead. At the same time, plan sponsors seeking lower fees are also looking at more indexed options, which tend to have lower trading costs due to less trading activity.
- **Qualified Default Investment Alternatives** – Readers are likely aware of the trend toward using target date or lifecycle funds as the plan's QDIA. With plan participants frequently leaning toward a "do it for me" approach to investing their retirement assets, these funds have become increasingly popular in the last several years. Along with managed accounts, where participants pay a fee to have their account managed for them, target date funds and lifecycle funds may meet plan sponsors' and participants' goals during the accumulation phase. The term "target date" refers to the approximate date when investors in the fund plan to start taking money out. Please keep in mind that different investment managers use different investment strategies. Participants should review holdings as they approach the target date to make sure the investments remain consistent with their objectives. The principal value of a target date fund is not guaranteed at any time, including at the target date.

- **Guaranteed Income Options** – Although the accumulation phase may be addressed, the payout phase of retirement is less so. Many plan participants have expressed interest in a guaranteed stream of income that would last their lifetime. The challenge is for providers to develop products that can meet the demand.

The paper, by Cammack Retirement in its *Insights* column, contains more information and is available at http://tinyurl.com/CammackTrends.

Knowledge vs. Action: The Disconnect

Knowledge and action are not always aligned, and a new study demonstrates such a misalignment for retirement savers. According to the study, Americans are generally behind in terms of retirement readiness, particularly falling short in figuring out how to save.

The study divided retirement preparation into three categories: sufficient knowledge and awareness of how to prepare ("knowing"); accurate and comprehensive planning activity ("planning"); and adequate savings to generate sufficient income replacement ("having"). For two groups, employees and retirees, the study asked a series of questions designed to assess all three categories, then scored the answers from zero to 10.

The big picture:

Employees
Employees received an average score of 5.8 out of 10 for the first category, knowing how to save. For the planning category, their average score was 3.0, and 3.5 for having adequate savings. Their overall average was 4.1.

Retirees
Retirees scored better, with a score of 7.0 out of 10 for knowing how to save, 4.2 for planning, and 5.3 for having enough savings. On average, the overall score for retirees was 5.5.

Confidence and concerns:

Employees
The study found that 65% of employees report they are at least somewhat confident in their ability to live securely throughout their retirement. Yet 59% of them reported a high level of concern about outliving their retirement savings.

Retirees
Among retirees, 82% are at least somewhat confident in their ability to live securely throughout retirement. However, 65% said they expect to live more than 20 years in retirement, even while 40% don't believe their savings would last beyond 20 years.

What They Know

It appears from the study that increased emphasis on educating employees about financial activities that can lead to retirement security is working. When asked about the importance of a few of the following actions, significant numbers of employees reported they are extremely or very important:

- Start saving as soon as you possibly can – 92%
- Create a holistic financial plan – 87%
- Determine the amount of future monthly income your current savings would produce – 85%
- Take advantage of financial advice from your own financial professional – 69%
- Take advantage of financial advice at the workplace – 63%

What They Do

The disconnect between knowledge and action is apparent, though, when employees who participated in the study were asked whether or not they had actually taken these financial planning steps:

- 31% said they have a written budget
- 36% have used a Web-based retirement calculator
- 17% have a formal, written financial plan

Role Models Who Know and Do

The study identified a subset of employees and retirees who could be considered role models, because of their proactive status relative to retirement preparation. They scored highest on the study's index because of the following key findings, among others.

- Nearly two-thirds (65%) of the employees had a written budget, and almost half (45%) had a formal written financial plan
- More than two-thirds of the retirees (68%) had a financial plan and 81% had a relationship with a financial professional
- 82% of employees and 78% of retirees had a specific strategy for investing their assets
- An overwhelming majority—97%—of the retirees in this group reported they are happy with their financial security, and 81% said they retired because they wanted to
- Among employees in this role model category, 96% said they are somewhat or very confident in how well they are prepared for retirement

You can read more results from the survey, the Voya Retire Ready Index, at http://tinyurl.com/VoyaRetireReady.

Pension Plan Limitations for 2015

401(k) Maximum Elective Deferral (*$24,000 for those age 50 or older, if plan permits)	$18,000*
Defined Contribution Maximum Annual Addition	$53,000
Highly Compensated Employee Threshold	$120,000
Annual Compensation Limit	$265,000

Plan Sponsors Ask…

Q: An employee claims that someone who used to work in our HR department informally gave him incorrect information about his status in our retirement plan. He relied on it and turned down a job offer. Could we be in trouble?

A: In short, you might be. This is a situation where you should immediately get some advice from your ERISA counsel. Even though the conversation doesn't seem to have been documented in writing, there have been cases where verbal promises were considered in legal actions between a plan and a participant. One example is Lees v. Munich Reinsurance America Inc. et al. In that case, Richard Lees worked for American Re-Insurance Company, which was purchased by Munich Reinsurance America. For a period of about three years, Lees was paid by a third entity, although he worked for American. When American sought to have Lees' payroll transferred to their system, he agreed when he was told that his time at the third entity would be treated as time at American for purposes of his pension benefits. This message was apparently conveyed orally and not in writing.

The U.S/ District Court for the District of New Jersey did not find any precedent on which to base an exclusion of oral misrepresentations relative to a breach of ERISA fiduciary duty claim. In effect, the judge found sufficient facts to support allowing a claim to proceed. Read the decision for yourself at http://tinyurl.com/PSMunichVerbalDecision.

Q: Employees take a lot of loans from our plan, and we worry that their retirement prospects will be affected. Is there research to support (or refute) our concerns?

A: There has been a lot written about plan leakage, which is when invested assets leave 401(k) plans to go elsewhere, usually to fund consumption of some kind. Plan leakage usually refers to loans, withdrawals when people change jobs, hardship withdrawals, and the like. The concern with the removal of any money invested in a plan is the cumulative impact of the withdrawal due to compounding over time.

In a blog post for MarketWatch, well-known economist Alicia H. Munnell says that in order to accumulate enough money for retirement, employees need to not only save but also leave their savings invested for the long term.

Munnell writes that Vanguard's report "How America Saves" has quantified data about plan leakage, allowing researchers like her to understand how much money is withdrawn from 401(k) plans and where the money is going. The report found that the percentage of assets leaving 401(k) plans due to loans and other forms of leakage was 1.2%. Munnell says that although this appears to be a very small number, its impact can be substantial for individual participants. Balances at retirement, she says, are almost 20% smaller than they would have been in the absence of leakage, although loans seem to play a minor role.

Read more of Munnell's thoughts on plan leakage at http://tinyurl.com/MarketWatchPlanLeakage.

Q: We hear a lot about differences between the generations; is there something different we should do to encourage our younger employees to save?

A: Actually, millennials are off to a pretty good start in terms of saving. Most of these young people have not known a time when they weren't expected to save for their own retirement. In fact, 63% of millennials who responded to a recent survey said they started saving before they reached age 25. However, less than a third of them are saving at least 10% of their salary through their employer-sponsored retirement plan. The survey reported that millennials who are offered an employer-matching contribution are very likely to take full advantage of it; 83% of them do so. That's great, but because a traditional match may help them reach only 3% or 4% of pay when 10% should probably be their goal, the match only gets them part of the way there. Employers may be able to help millennials (and all other employees) save more by changing the formula for the employer match to one that provides, for example, 25% of the first 12% of pay contributed by the employee. This kind of "stretch" feature may entice more participants—including millennials—to contribute the full 12% of pay.

You can learn more about how the youngest workers save by reading the study, available online at http://tinyurl.com/PrincipalMillennials.

Annual Participant Fee Disclosures

The participant fee disclosure regulations require participant-directed defined contribution plans to make annual disclosures. These disclosures include basic information regarding the plan, its expenses and investments. Previously, the Department of Labor required Plan Administrators to provide the disclosures at least annually, meaning that disclosures had to be distributed no later than one year (e.g., 365 days) after the prior year's disclosures were provided. As a result, Plan Administrators had to keep track each year of the date the disclosure was given in order to distribute the subsequent year's disclosure in a timely manner, within the 365-day period.

The DOL has issued new regulations that provide that the annual disclosure must be given within 14 months of the prior year's disclosure. As a result of this change, Plan Administrators have needed flexibility to distribute their disclosures at approximately the same time each year. More information can be found on the DOL Fact Sheet:
http://www.dol.gov/ebsa/newsroom/fsdirectfinalrule.html

Please contact your TRA Client Relationship Manager at 888.872.2364 if you have any questions or would like to discuss further. ■

Web Resources for Plan Sponsors

Internal Revenue Service, Employee Plans
www.irs.gov/ep

Department of Labor,
Employee Benefits Security Administration
www.dol.gov/ebsa

401(k) Help Center
www.401khelpcenter.com

PLANSPONSOR Magazine
www.plansponsor.com

BenefitsLink
www.benefitslink.com

Plan Sponsor Council of America
www.psca.org

Employee Benefits Institute of America, Inc.
www.ebia.com

Employee Benefit Research Institute
www.ebri.org

PLAN SPONSOR'S QUARTERLY CALENDAR

OCTOBER

- Audit third quarter payroll and plan deposit dates to ensure compliance with the Department of Labor's rules regarding timely deposit of participant contributions and loan repayments.
- Verify that employees who became eligible for the plan between July 1 and September 30 received and returned an enrollment form. Follow up for forms that were not returned.
- For calendar-year safe harbor plans, issue the required notice to employees during October or November (within 30-90 days of the beginning of the plan year to which the safe harbor is to apply). Also, within the same period, distribute the appropriate notice if the plan features an EACA (Eligible Automatic Contribution Arrangement), QACA (Qualified Automatic Contribution Arrangement) and/or QDIA (Qualified Default Investment Alternative).

NOVEMBER

- Prepare to issue a payroll stuffer or other announcement to employees to publicize the plan's advantages and benefits, and any plan changes becoming effective in January.
- Conduct a campaign to encourage participants to review and, if necessary, update their mailing addresses to ensure their receipt of Form 1099-R to be mailed in January for reportable plan transactions in 2014.
- Check current editions of enrollment materials, fund prospectuses and other plan information that is available to employees to ensure that they are up to date.

DECEMBER

- Prepare to send year-end payroll and updated census data to the plan's recordkeeper in January for year-end compliance testing (calendar-year plans).
- Verify that participants who terminated during the second half of the year selected a distribution option for their account balance and returned the necessary form.
- Review plan operations to determine if any ERISA or tax-qualification violations occurred during the year and if using an IRS or DOL self-correction program would be appropriate.

Consult your plan's financial, legal or tax advisor regarding these and other items that may apply to your plan.

Survey Submission Winner

Enter to win a prize by clicking on the survey link in our emails and completing the survey. A winner is picked quarterly! This quarter's winner is

Christina S with Inter Tribal Council of Michigan.

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