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Moving Parts of a Retirement Plan

Plan Design Trends & Hot Topics

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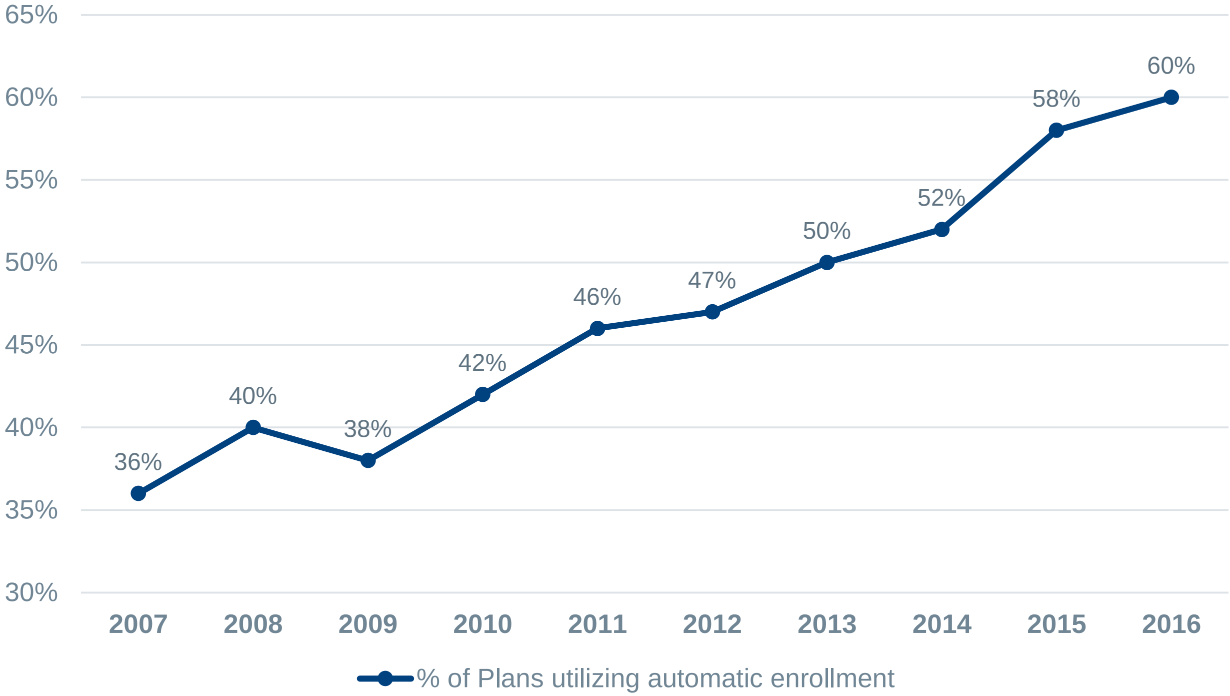
Moving Parts of a Retirement Plan
Trends & Hot Topics

1. Trends
2. Hot Topics
3. Plan Design Statistics
4. Questions

Plan Design Trends

Plan Trends & Hot Topics
Trends

Trend #1: Plans are embracing automatic enrollment



Source: PSCA 60th Annual Survey

Plan Trends & Hot Topics
Trends

Benefits of Automatic Enrollment

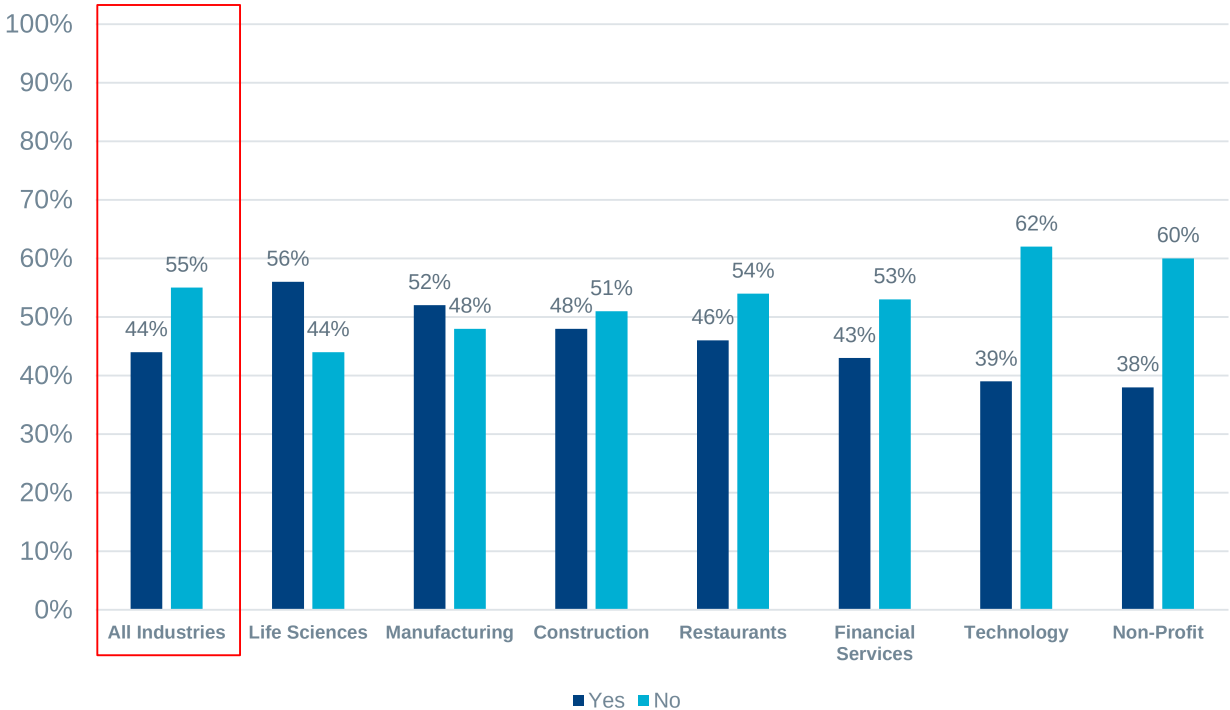
1. Streamlines the enrollment process / administrative burden (usually)

2. Improves plan testing (usually)

3. Allocates participants into QDIA-compliant investments (always)

Plan Trends & Hot Topics
Trends

Automatic Enrollment By Industry **($5-50 million in assets)**



Source: PLANSPONSOR Defined Contribution Survey, 2017

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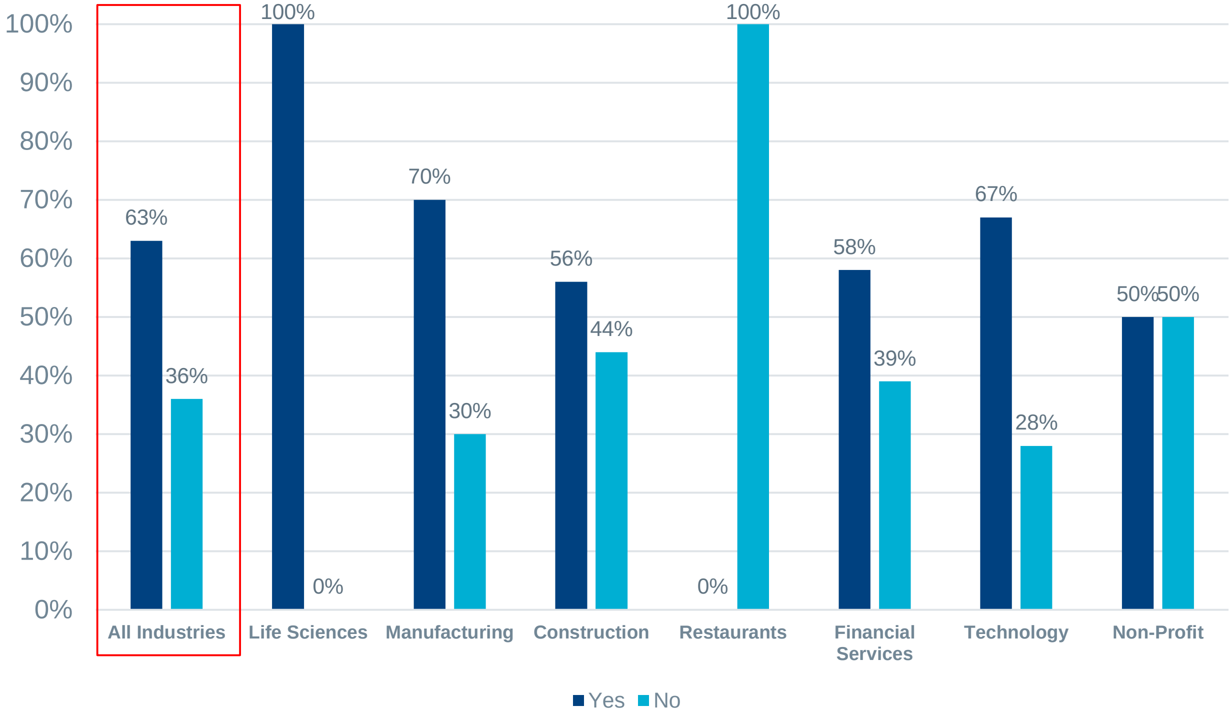
Automatic Enrollment By Industry ($50-200 million in assets)



Source: PLANSPONSOR Defined Contribution Survey, 2017

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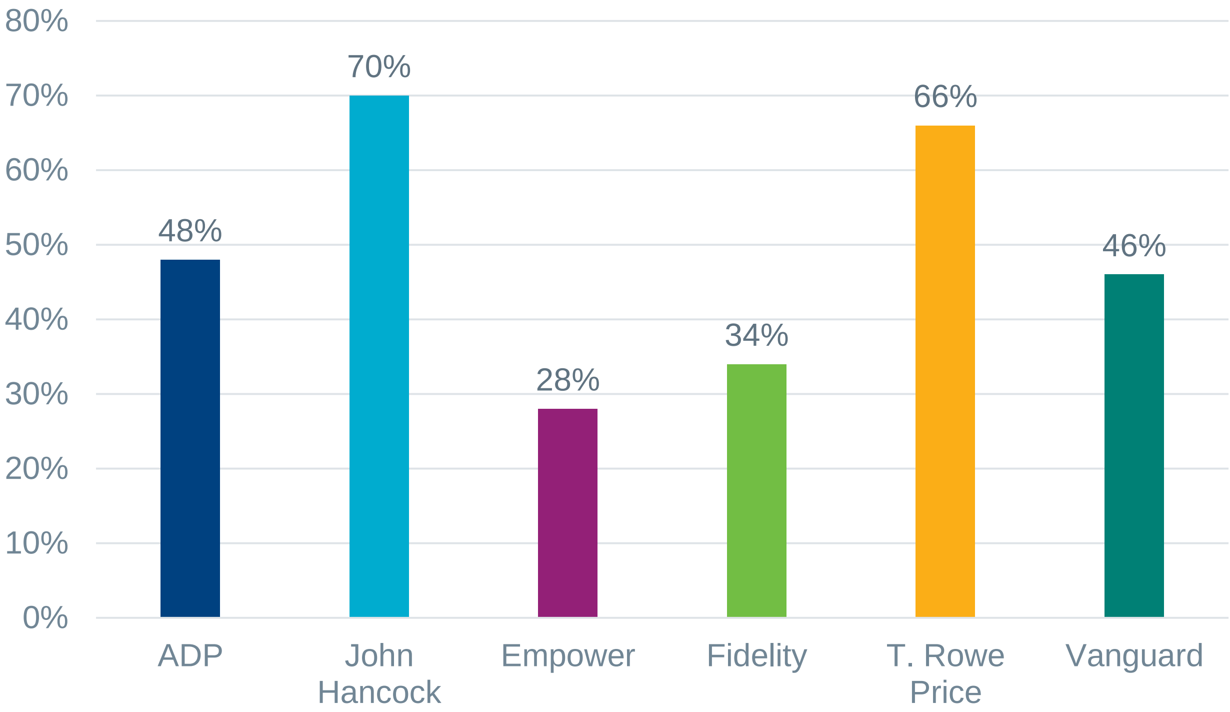
Trends

Automatic Enrollment By Provider



Source: Vendor Plan Statistics Reports

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Trends

Impacts of Automatic Enrollment

1. **Employers are increasing default savings rates**
   In addition, the number of employers that default at 6% or more has more than doubled over the last decade – now almost 1 in 5 employers (19%) utilize a default savings rate of 6% or higher.

2. **Employees who are automatically enrolled stay in the Plan**
   Plans with AE have an average participation rate of 87% (vs. 52% for those without).

3. **Employees who are automatically enrolled tend to save more**
   Since 2008, automatically enrolled employees have increased their savings from 4.0% to 6.7%, with 2/3 (63%) increasing their savings rate on their own.

Source: Fidelity' "Building Futures" Report, 2018

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Trends

Best Practices for Automatic Enrollment

1. **Choose a higher default rate**
   - Studies have shown that 80-90% of employees stay in the Plan regardless if the default is 1-9% of pay.
   - If possible, tie the default percentage to the company match.

2. **Add an Automatic Increase provision**
   - 73.4% of plans with automatic enrollment add auto increase.
   - Allows participants to grow their deferral rate over time (target a total savings rate in the 12%-15%).
   - Helps participants capture the full match over time (if applicable).

3. **Also add Automatic Cashout to the Plan to account for turnover**
   - Terminated participants with balances <$1,000 receive a check
   - Terminated participants with balances between $1-5k are rolled to an IRA

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Trends

Takeaways for Automatic Enrollment

1. Company size, industry and plan demographics matter

2. Some vendors are better suited for automatic enrollment

3. Automatic enrollment is a best practice that generally improves plan statistics and testing, and can streamline the enrollment process

4. Participants are embracing automatic enrollment and using it as a starting point to save more

Note: Automatic enrollment can potentially increase employer contribution costs as more participants capture matching contributions

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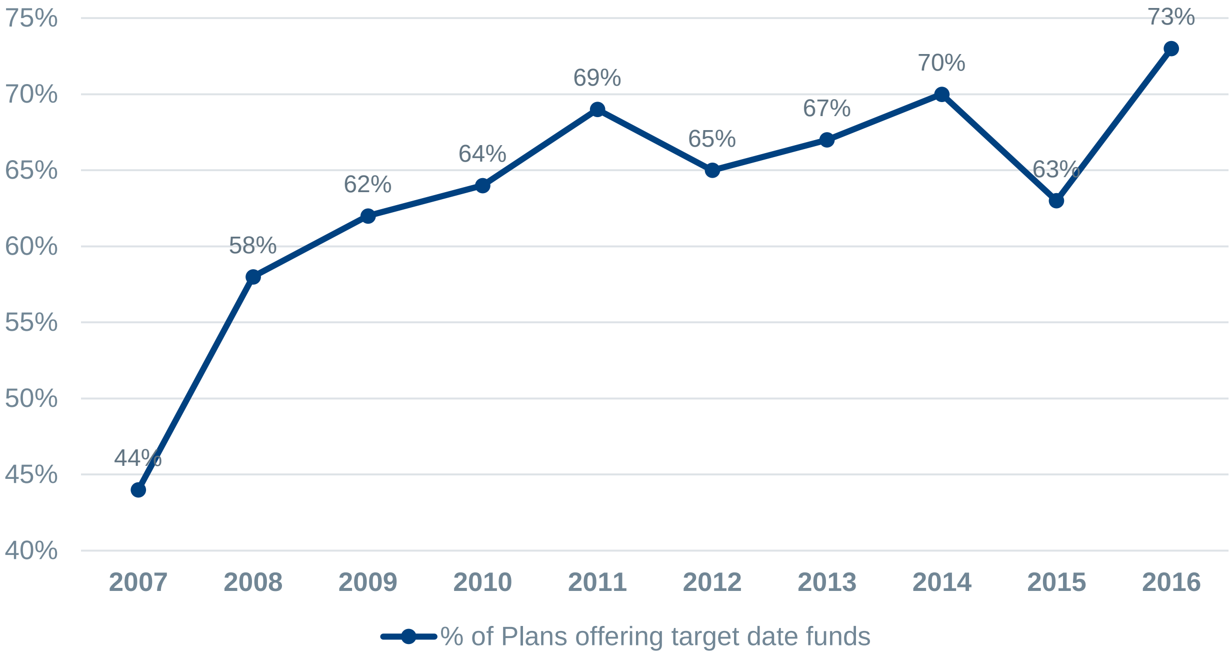
Trends

Trend #2: Target date funds are becoming the most popular asset category in retirement plans



Source: PSCA 60^{th} Annual Survey

Plan Trends & Hot Topics
Trends

Why Are Target Date Funds So Popular?

1. They are one of only a few funds that are QDIA-eligible

Traditional Balanced Fund	Target Date Funds	Risk-Based Funds	Managed Accounts

2. They are easy for participants to understand

I am 43 years old →	I will retire around age 65 →	I will be 65 in the year 2040 →	Choose the 2040 Fund

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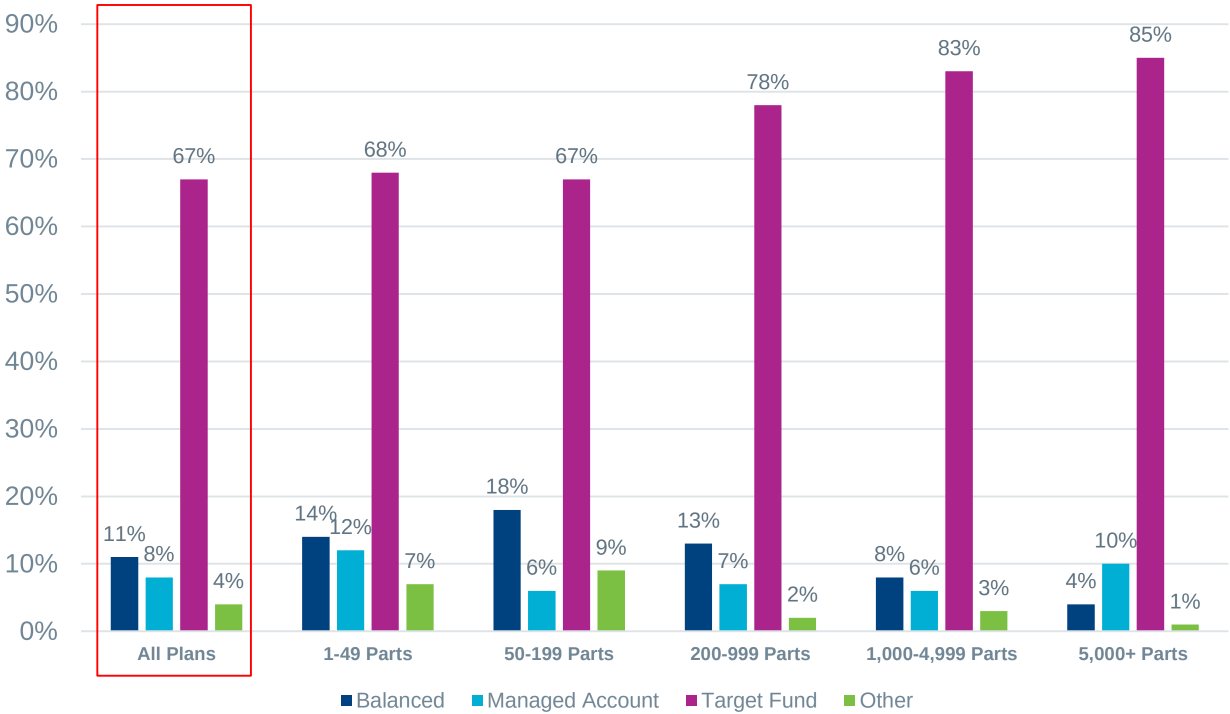
Trends

QDIA Defaults by Plan Size



Source: PSCA 60th Annual Survey

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Trends

Best Practices for Choosing a QDIA

1. Establish a process for comparing and selecting options
   - The DOL has provided “tips” to help Plan Sponsors determine suitability
   - Plan asset allocation, demographics, fees, provider offering and portability are all factors to consider
2. Develop effective employee communications
3. Periodic review the QDIA’s suitability for the Plan
4. Document the process

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Trends

Target Date Trends

1. Target date fund assets eclipsed $1 trillion in 2017 after seeing an all-time high of $70 billion in estimated net flows last year

2. In 2017, target funds focused on index (passive) strategies attracted nearly 95% of the $70 billion in estimated net flows to target date funds

3. Fees continue to decrease for target date funds. The average expense ratio fell to 0.66% at the end of 2017, from 0.91% just five years earlier

4. When launched, additional lower-cost series have generally been the most popular, but not all have produced better performance results than older, more-costly ones

Source: Morningstar target date Fund Landscape Report, 2018

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Trends

Takeaways for Target Date Funds

1. Target date funds are quickly gaining a majority of retirement plan assets and are amongst the most widely used funds in a plan

2. Target date funds allow participants an easy to understand solution for picking investments

3. As a QDIA-compliant option, target date funds give Plans Sponsors protection for usage with features like automatic enrollment

4. Plan Sponsors should periodically review their target date funds and document that funds used are still suitable for the Plan

Hot Topics

Plan Trends & Hot Topics
Hot Topics

Hot Topic #1: New Hardship Distribution Rules

The Bipartisan Budget Act of 2018 included changes to 401(k) Hardship Withdrawals.

1. Request Hardship Withdrawal without first exhausting available loan from the plan (permitted change).

2. Expanded the types of contributions and earnings available for hardship distributions (permitted change).

3. Eliminate the safe harbor requirement to suspend participant contributions for six months (mandatory change).

4. Add ‘expenses due to a federally declared disaster’ as an eligible reason for hardship (mandatory change).

5. Amend for Plan Year 2019.

Plan Trends & Hot Topics
Hot Topics

Takeaways about the Hardship Withdrawal changes

1. Not all the changes are good ones when considering the impact on the Retirement Savings of a participant.
   - No disturbance to savings rate
   - A need for a loan may only exacerbate the financial need
   - May elect to take hardship when a loan may be more appropriate

2. Based on statistics from vendors,
   - The number of hardship withdrawals taken in the first months of 2019 jumped significantly over the previous year (i.e., 40%)
   - During same time period, rate of participants taking loans has fallen (some say by at least 7%)

3. There is a 2-year remedial amendment period (must adhere to the changes even if plan is not yet amended).

Plan Trends & Hot Topics
Hot Topics

Hot Topic #2: Utilizing the HSA for Medical or Retirement Savings

The Health Savings Account can be a powerful savings tool – if you approach it the right way.

1. **Tax Efficiency**: Only triple tax-free retirement investment vehicle available.
2. **No RMDs**: Not required to take distributions once you turn 70½
3. **No Income Limits**: Unlike some savings options, there are no income limits (i.e. ROTH IRAs)
4. **Portability**: The individual keeps the account HSA should their employment status change due to job loss, changing company, or retirement
5. **Carry-Over**: No length of time or age restrictions on when you can reimburse (as long as you keep your receipts)
6. **Investment Options:** Available to grow your balance and keep up with healthcare inflation

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Hot Topics

No One Option is Perfect

Account Types	Pre-Tax DC Plan or IRA	Roth DC Plan or IRA	HSA
Contributions	Pre-Tax	Post Tax	Pre-Tax
Maximum Annual Contributions	$19,500 Retirement Plan $6,500 IRA	$19,500 Retirement Plan $6,500 IRA	$3,550 individual $7,100 family
Early Distribution Penalty	10%	10%	20%
Early Distributions	Limited access	Limited access	Qualified medical expenses (QME), no tax or penalty
Taxes on Distributions	Ordinary Income rate	Tax-fee if qualified	Tax-free if used to pay QME
Required Minimum Distributions (RMDs)	Age 70½	Age 70½ in Retirement Plan (none in IRA)	None
Tax Treatment for Non-spouse Heirs	Ongoing tax deferral (subject to RMD requirement)	Ongoing tax-free (subject to RMD requirement)	Value immediately subject to ordinary income tax

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Hot Topics

Retirement Savings Hierarchy

- 401k – Up to the Match
- HSA (Triple Tax Benefit)
- Max out 401k / IRA
- Taxable Accounts (Brokerage, etc.)

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Hot Topics

HSA integration with 401(k) Plan Service Providers to enhance Financial Wellness tools and projections

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Hot Topics

Hot Topic #3: Student Loan Repayment Programs

- Undergraduate Class of 2018:
  - 69% took student loans
  - Average debt = $29,800 (private and federal)
  - 14% of parents took an average of $35,600 in federal loans
- 44.7 million Americans currently have student debt
- Student loan debt = $1.56 trillion, or **$521 billion MORE** than total U.S. credit card debt
- 86% of employees said they'd stay with a company for at least 5 years if their employer helped pay down their student loans
- 40% of employees said student loan debt stopped them from saving for retirement

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Hot Topics

Things to Keep in Mind with Student Loan Repayment Programs

1. Employee demographics – how many have student loans?
2. There are no tax benefits for employer contributions – must pay payroll taxes
3. Contributions are taxable income to employees
4. Highly recommend surveying employees before rolling out the program
5. Do human resources and other relevant departments have capacity?

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Employers Offering Student Loan Repayment Programs

- Fidelity – $2,000/year - $10,000 total
  - Originally used tuition.io, recently Fidelity built and rolled out their own tool
  - An employee who leaves Fidelity does not have to repay the benefit
- PricewaterhouseCoopers - $1,200/year - $7,200 total
  - Uses Gradifi
- First Republic
  - Tiered Program: $1,200 in year 1; $1,800 in year 2; $2,400 thereafter
  - No lifetime limit; part-time employees are eligible
- Carhartt - $50 a month up to $10,000 for eligible part-time and full-time workers
  - One of the first companies in Michigan to offer the program!
  - Uses tuition.io

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Hot Topics

Regulatory Guidance for Plan Sponsors Considering Student Loan Repayment Programs

- In a Private Letter Ruling for Abbott Laboratories released in August 2018, the IRS permitted the employer to make 401(k) contributions for participants who repay student loans
  - Employer makes a 5% of pay match for any participant who contributes at least 2% of pay
  - If a participant makes a student loan repayment equal to at least 2% of pay, the employer will make a non-elective contribution of 5% (receiving no other matching contributions)
  - IRS rules that the program does not violate the rule that prohibits conditioning any benefit (directly or indirectly) on a participant's electing to make or not make a plan contribution
- **Note:** Private Letter Ruling is only applicable for the specific plan that requested the ruling. It is NOT broad guidance
- However since then, other companies like Travelers and Stanley Black & Decker have moved forward with implementing their own student loan repayment programs
- New proposed legislation may allow matching contributions into 401(k) and 403(b) plans for employees who make payments toward their student loans

Plan Trends & Hot Topics
Hot Topics

Hot Topic #4: Proposed E-Delivery Safe Harbor

- Recently proposed regulations will allow plan sponsors to default to electronic delivery of retirement plan notices and disclosures if the following conditions are satisfied:
  - Participant must first be notified by paper that notices will be sent electronically
  - This initial notice must include right to request paper copy (free of charge) or to opt out of electronic delivery
  - Participants can't be defaulted to electronic delivery if they do not have an electronic address
  - Email address or smartphone number (for texting) may be used, whether personal or employer-provided
  - Plan sponsors may also satisfy disclosure requirements by posting the notices online and letting participants know they've been posted and how to access the electronic notices

Plan Design Statistics

Plan Trends & Hot Topics
Plan Design Statistics

Common Areas of Focus for Plan Sponsors

Is my investment offering strong?

- Most plans offer between 11-25 investment options
- Because of the increased usage of target funds and other managed account options, assets in traditional asset classes continue to decrease
- CITs, index funds and lower expense ratios have become more commonplace as Plan Sponsors focus more on fees
- The usage of revenue sharing has decreased due to a lack of transparency
- Self-directed brokerage windows and company stock are less common than in the past and bring an additional level of fiduciary concern

Source: PSCA 60th Annual Survey

Plan Trends & Hot Topics
Plan Design Statistics

How Does Your Plan Stack Up?

Provision	Common Plan Design
Eligibility: Service Requirement	• Immediate: 58.8% • 3 months: 17.1% • 6 months: 8.1% • 1 year: 13.0%
Eligibility: Age Requirement	• No Age: Requirement: 30.3% • Age 18: Requirement: 31.0% • Age 21: Requirement: 38.2%
Eligibility for Employer Contributions	• Immediate: 45.6% • 1 year: 28.7%
Automatic Enrollment	• 59.7%: Have auto enrollment • 50.6%: New hires only
Automatic Increase	• 32.7% of Plans w/ Auto Enrollment also have Auto Escalation
Catch-Up Contributions	• 95.2% of all Plans allow catch-up
Rollover Contributions	• 93.6% of all Plans allow rollovers

Source: PSCA 60th Annual Survey

Plan Trends & Hot Topics
Plan Design Statistics

How Does Your Plan Stack Up?

Provision	Common Plan Design
Roth	• 63.1% of all Plans offer Roth
Roth In-Plan Conversion	• 36.1% of all Plans now permit in-plan Roth conversions
Match	• 94.4% of plans provide a company contribution
Safe Harbor	• 23.0% of Plans are Safe Harbor
Company Contributions	• 49.1%: Match Only • 12.1%: Non-Elective Only • 33.3%: Both Match & Non-Elective • 5.6%: No Company Contribution **NOTE: Includes Discretionary**
Vesting	• 41.2%: Immediate Vesting • 17.1%: 5 Year Graded Vesting • 10.9%: 6 Year Graded Vesting • 13.3%: 3 Year Cliff Vesting

Source: PSCA 60th Annual Survey

Plan Trends & Hot Topics
Plan Design Statistics

How Does Your Plan Stack Up?

Provision	Common Plan Design
Loans	• 88.9% of Plans permit loans
# of Loans at a time	• 55.1% of Plans only allow 1 loan • 36.3% of Plans allow 2 loans • 8.6% of Plans allow 3 or more loans
In-Service Distributions	• 60.9% of Plans allow in-service distributions
Age to Allow In-Service Withdrawal	• 79.3%: After Age 59½ • 4.2%: Before Age 59½
Hardship Distributions	• 79.5% of Plans allow hardships
Processing of Hardship Distributions	• 52.0% Must be approved by Sponsor • 36.4% Process Automatically
Automatic Cashout	• 53.7%: Under $5k Cashout • 27.9%: Under $1k Cashout • 18.5%: No Cashout Provision
Managed Accounts	• 39.0% of Plans offer Managed Accounts

Source: PSCA 60th Annual Survey

Plan Trends & Hot Topics
Plan Design Statistics

Other Statistics

1. Only 74.6% of companies evaluate whether their plan is successful (meeting company's objectives)

2. Only 56.2% of companies utilize a 3(21) or 3(38) fiduciary as advisor
   — 43.9% are unsure of their advisor's liability

3. 35.7% of companies now also offer a Non-Qualified Deferred Compensation (NQDC) Plan for a select subset of employees (executives)

Source: PSCA 60th Annual Survey

Questions?

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