RETIREMENT INSIGHT

4TH QUARTER 2019

Financial Literacy: Employees Who Know More Save More

The assumption when plan sponsors began to include auto features in their 401(k) plans was that participation rates and deferral amounts would increase — but no one knew for sure. As time has passed, it appears the assumption was good: auto-enrollment and auto-increases have had very positive results overall.

Plans that include auto-enrollment enjoy an average participation rate that is nearly double that of plans not using this feature: 85.6% participate in plans that include auto-enrollment, compared to 43.7% for those without. Even better, more than one-third (37%) of plans using auto-enrollment have a default deferral rate of 6% or higher.

On average, 401(k) plans saw their pretax deferral rate increase to 8.6% of pay in 2018, up slightly from 8.3% a year earlier. Employers added to employee savings via an increased company match, perhaps due to the reduced corporate tax rate. In 2018, 11.8% of plans matched 100% of the first 6% of salary; 14.2% matched 100% up to 4% of pay; and 27.2% set their matching formula at 50% of the first 6%.

Further, Roth account contributions rose by 10% compared to 2017. Still, Roth accounts may be underutilized, with usage at just 7.6%. This may be due to a lack of understanding by employees, which suggests that education on the topic could benefit them. Young Millennials, between the ages of 20 and 29, contribute to a Roth account at a rate of 8.8%, compared to almost 10% by elder Millennials, between 30 and 39.

However, 2018 wasn't all rosy. According to T. Rowe Price. In their December 31, 2018, Reference Point, the company saw a significant increase in the number of participants contributing nothing to their plan, from 33.9% in 2017 to 35.6% in 2018. This may have played a role in an overall decrease in account balances, from $92,402 in 2017 to $85,336 in 2018. The decrease was most pronounced among Millennials, who lost the highest percentage in account balances over the year.

Market fears seem to have been a deciding factor in plan participants shifting from stocks to cash within their 401(k) plan accounts. Overall, investment in stocks dropped 4.9% in 2018, whereas investment in money market or stable value funds increased just over 10%. Target date funds (TDFs) continue to be popular with retirement investors; investments in TDFs rose slightly in 2018, from 41.2% in 2017 to 42.2% — an increase of 2.4%.

Get more insights on 2018 plan participation in T. Rowe Price's report, available for download at https://trowe.com/2yJnFg4. ■

For 25 years, Asset Strategy Consultants has been providing investment management consulting to fiduciaries of retirement plans, endowments, and foundations. ASC assists clients with managing the risk and responsibility of sponsoring retirement and investment programs while helping their employees achieve a successful retirement outcome. Headquartered in Baltimore, ASC has over $9 billion under advisement throughout their five offices on the East Coast.

ASSET STRATEGY CONSULTANTS

Clever Tactics To Help Employees Achieve Retirement Success

Behavioral finance strategies improve the odds

Applying a few innovative moves in your 401(k) plan could result in increased retirement savings for your employees. That's because, when it comes to money, subconscious perceptions can torpedo a plan participant's success.

Applying behavioral finance principles may help employees overcome obstacles that often keep them from making rational financial decisions. Here are a few financial behaviors that could be sabotaging employee retirement savings, along with ideas from the International Foundation of Employee Benefit Plans (IFEBP) that may serve to counter them.

Loss Aversion

People tend to dislike loss more than they like gains. As an employer, you can capitalize on this tendency with the language you use to communicate about the plan. For example, "Would you rather pay yourself or the government?" or " Increase your retirement savings and cut your taxes," is much more effective than "Stop missing out on your retirement plan match." Although both communicate the same message, says the IFEBP, the former packs a more powerful punch.

Herd Mentality

We all like to be included, and that means we look to others to figure out our next move. As you communicate about your 401(k) plan, take advantage of this tendency by discussing what others are doing with regard to saving. For example, say something like, "80% of ABC employees contributed to their retirement plan last year." Or get even more specific about the group you're targeting with this message: "Nine out of every ten new hires say "yes" to saving 15% of their pay for retirement." The IFEBP says that breaking down the message to specific groups — such as new hires, people over age 50, or those working at a specific location — can be most effective.

Order for Advantage

Faced with a long list of choices, most people hone in on entries at the top. Unless the list is particularly long, they may recall only the last few items. When providing a list, consider the order in which you include entries. For example, if you present a list of investment funds available in the plan, the tendency may be to list the choices from least risky to most risky. As a result, you may find the majority of participants select very conservative investments or, if the list is long, very aggressive ones because they only remember the last few funds on the list. Instead, consider reserving the top of the list for investments that are likely to be appropriate for most participants, such as target date or balanced funds.

There are many more principles of behavioral finance that may help in your 401(k) plan communication efforts. Find out more about the IFEBP's suggestions at https://tinyurl.com/IFEBP-Beh-Fin. ■

Web Resources for Plan Sponsors

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

U.S. 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 Benefit Research Institute
www.ebri.org

Plan Sponsors Ask...

Q: We keep hearing about participant lawsuits against 401(k) plans, and strive to do our best to avoid situations that could lead to one. Part of that is using prudent processes in the plan. We have asked our advisor and done some searching on our own, but haven't been able to define what processes are truly prudent in this context.

A: Since the inception of the Employee Retirement Income Security Act of 1974 (ERISA), the prudent person rule has provided a good rule of thumb. To paraphrase, it states that an appropriate decision is one that a prudent person, with similar skill and circumstances, would make. You are correct that it lacks precision, and that's why process is so important; the Center for Retirement Research at Boston College studied the major causes of 401(k) lawsuits, and determined that they often hinge on whether or not a prudent process was followed. The study found that the most common reasons for participant legal action are excessive plan fees, poor investment options, and self-dealing behaviors. To illustrate: some plan sponsors fear incurring the higher fees associated with actively managed funds, so they offer only passive funds. But courts don't automatically consider higher fees to be excessive, as long as they are clear and provide value in exchange for the fees. In fact, a too-conservative approach may also be detrimental to participants. A prudent process for selecting the funds may provide a satisfactory defense if a participant decides to sue. Our best suggestion is to thoroughly review all processes in the plan with prudence in mind. Read more at https://tinyurl.com/CRR-Prudent-Process.

Q: I overheard a surprising conversation between two of our employees. In short, one told the other that his 401(k) account at his former company just goes back to his ex-employer. I brought the employee in and gave him the contact information for our plan's advisor so he can get correct information. But it made me wonder how we're really doing in educating employees about our plan.

A: Communicating with employees about the plan is at least a two-part process. Part 1 is providing the education, and part 2 is determining how well it works. You are fortunate to have stumbled upon Part 2. Don't feel bad if your education efforts are falling short, though, because you aren't alone. Fisher Investment 401(k) Solutions found some holes in participants' understanding of their 401(k) plans, through their *401(k) Wellness in the Workplace Survey*, covered in 401kSpecialist Magazine, https://tinyurl.com/Fisher-Workplace-Wellness.

The knowledge gaps uncovered by Fisher may help you determine the next topics to address for your employees. A few subjects on which you may want to educate employees include loans, taxes, and asset classes. One-third of Fisher's survey respondents thought that most plans don't allow loans, 23% did not know their contributions reduce their taxable income, and 77% could not accurately define "mutual fund" when presented with a list of descriptive statements.

Q: Our 401(k) plan has decent participation and contribution rates. Unfortunately, we also notice a lot of loan activity. Informal discussions suggest that employees are using their retirement savings to fund emergencies. Any ideas for how to help?

A: Lots of Americans are finding it difficult to fund even small emergencies from their bank accounts, as demonstrated by the proliferation of payday loans and — as you have discovered — early withdrawals and loans from 401(k) plans. One way to help may be the sidecar IRA, an account to which employees can direct after-tax money through payroll deduction. Once the account is funded to the extent desired by the employee, the payroll deductions can then be directed toward pretax retirement savings. Check out related statistics and more information from studies by Transamerica Center for Retirement Studies, Prudential, and AARP by reading the MarketWatch article here: https://tinyurl.com/Market-Watch-Sidecars. ■

Pension Plan Limitations for 2019

401(k) Maximum Elective Deferral (*$25,000 for those age 50 or older, if plan permits)	$19,000*
Defined Contribution Maximum Annual Addition	$56,000
Highly Compensated Employee Threshold	$125,000
Annual Compensation Limit	$280,000

Auto-Features Accomplished; What's Up Next?

Retirement income options may be coming soon

You can almost hear the retirement plan consultants ticking the boxes on their to-do lists: auto-enrollments? Check. Auto-increases? Check. With widespread implementation of these features firmly entrenched, the next focus may be retirement income options in 401(k) plans. That's one of the findings from recent queries of 238 consulting and advisory firms. Roughly two-thirds of the consultants who were asked about the future of plan design said they believe their plan sponsor clients want to retain retirees in their plans. One way to do that is to figure out ways defined contribuiton plans can provide income. They also favor adding distribution flexibility, access to education, and retiree-focused investment options.

Asked what they believe their clients' priorities would be for 2019, 63% of the consultants placed a review of the plans' target date funds at the top of the list. Second came an evaluation of investment fees at 44%, and evaluation of administration fees in the number three spot, with 28%.

Although interest in financial wellness programs remains strong, a large majority of consultants participating in the PIMCO DC Consulting Study (https://tinyurl.com/PIMCO-next-up), released April 2019, are unimpressed. At least 74.9% of study participants said the results of such programs are only somewhat effective (74%), 9% stated that they are very effective, and 17% said these programs are not very effective. ■

PLAN SPONSOR'S QUARTERLY CALENDAR

JANUARY

- Send payroll and employee census data to the plan's recordkeeper for plan-year-end compliance testing (calendar-year plans).
- Audit fourth quarter payroll and plan deposit dates to ensure compliance with the U.S. Department of Labor's rules regarding timely deposit of participant contributions and loan repayments.
- Verify that employees who became eligible for the plan between October 1 and December 31 received and returned an enrollment form. Follow up for forms that were not returned.

FEBRUARY

- Update the plan's ERISA fidelity bond coverage to reflect the plan's assets as of December 31 (calendar-year plans). Remember that if the plan holds employer stock, bond coverage is higher than for nonstock plans.
- Issue a reminder memo or e-mail to all employees to encourage them to review and update, if necessary, their beneficiary designations for all benefit plans by which they are covered.
- Review and revise the roster of all plan fiduciaries and confirm each individual's responsibilities and duties to the plan in writing. Ensure than each fiduciary understands his or her obligations to the plan.

MARCH

- Begin preparing for the timely completion and submission of the plan's Form 5500 and, if required, a plan audit (calendar-year plans). Consider, if appropriate, the U.S. Department of Labor's small plan audit waiver requirements.
- Review all outstanding participant plan loans to determine if there are any delinquent payments. Also, confirm that each loan's repayment period and the amount borrowed comply with legal limits.
- Check bulletin boards and display racks to make sure that posters and other plan materials are posted and readily available to employees, and that information is complete and current. ■

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

Kmotion, Inc., 412 Beavercreek Road, Suite 611, Oregon City, OR 97045; 877-306-5055; www.kmotion.com