

# RETIREMENT Plan Trends



A benefits update

Volume 52, Number 12

## Employers Seek Alternatives To Help Workers Save For Retirement

While most sponsors of 401(k) plans view matching contributions as the best way to support employees in saving for retirement, the need to reduce or suspend matches due to the economy could provide employers with the opportunity to adjust their retirement benefit strategies, according to a study released by human resources consultancy Towers Perrin.

In the white paper, "Alternatives to the Traditional 401(k) Match Can Meet Longer-Term Objectives for Attracting and Retaining Talent," researchers observed that the account balances of many 401(k) plan participants have fallen sharply over the past year due to stock market declines and, in many cases, cuts in matching contributions by employers. According to the report, a recent survey of 500 U.S. companies showed that

employees have changed their retirement savings habits in response to the downturn, with 59% reporting that workers are postponing retirement, 48% saying 401(k) plan participants are moving to fixed-income investments, and 43% observing an increase in the number of workers taking loans and withdrawals from their retirement accounts. In addition, 38% of the plan sponsors said

they have seen a reduction in plan participation levels, and 34% said there has been an increase in the number of employees requesting financial education or retirement planning assistance.

The report also cited a series of surveys taken over the last few years showing that employees' workplace priorities have recently shifted away from concerns about work/life balance and the opportunity to do exciting and challenging work, and toward concerns about job security and adequate benefit protection. Given this change in priorities, researchers said, a change in the types of benefits offered may be required.

As the economy improves, the study's authors pointed out, some companies that have recently cut matching contributions "are taking the opportunity to look at the structure of their benefit programs and ask whether

### *Also In This Issue*

- Fees Vary Among Retirement Plans
- Consistent Contributions Pay Off Despite Bear Market

**Furr &  
Associates**  
*Insurance and Investment Services*

5575 Garden Village Way  
Suite C-102  
Greensboro, NC 27410

(336) 852-4554  
(336) 698-3180 *fax*  
(877) 273-7755

[www.furrandassociates.com](http://www.furrandassociates.com)

Securities and investment Advisory Services offered through Woodbury Financial Services, Inc. Member FINRA/SIPC, and Registered Investment Advisor, PO Box 64284, St. Paul, MN 55164 (800) 800-2000



*The current situation could provide plan sponsors with an opportunity to formally link 401(k) matching contributions to specific business metrics, the authors asserted.*

simply restoring matching in its earlier form is the most efficient way to provide for their employees' retirement, and whether by doing so they are meeting longer-term objectives for attracting and retaining talent."

Several opportunities may be of particular interest to employers moving forward, the report said. First, companies may consider linking 401(k) matches to profitability. "Suspending 401(k) matching contributions in response to the economy revealed the extent to which benefit programs are linked to company profitability—even if the companies themselves had not explicitly said so beforehand," researchers noted. The current situation could provide plan sponsors with an opportunity to formally link 401(k) matching contributions to specific business metrics, the authors asserted. For example, the plan could specify that the company match will equal 75% of employees' contributions if earnings per share exceed a certain level, or that matches will be reduced to 50%, 25%, or even zero at lower specified levels. Researchers also noted, however, that the uncertainty associated with this approach could make long-term financial planning more difficult for employees.

Second, plan sponsors may consider new ways to ensure total retirement adequacy. For example, they may provide a portion of the employer contribution regardless of the employee's own contributions or reallocate some of the funds currently used for matching contributions to pay for retiree health care benefits. This type of financial support can help to minimize the savings inadequacies that often develop over the course of an employee's career, the report said. Researchers also pointed out that, by redirecting benefits to retiree health care funding, employers save on FICA contributions that would otherwise be due on 401(k) contributions, and health care benefits would be free from Federal income taxes when used by retirees.

Finally, retirement plan sponsors may consider reallocating 401(k) matching contributions away from retirement and toward other forms of rewards, especially health initiatives focused on encouraging

more cost-conscious behavior by current employees. For example, the report said, companies may want to provide employees with funds to open a tax-advantaged Health Savings Account (HSA), which can help accrue savings that can ultimately be used in retirement, or offer workers incentives to maintain their health as part of wellness and other consumer-driven health care programs. Employers could also use the funds previously devoted to 401(k) matches to introduce or expand incentive pay programs that reward business-focused behaviors or performance outcomes.

As the economic climate shifts, employees increasingly value the ability to choose the benefits of greatest use to them, researchers concluded. By reassessing the structure, cost, and benefits of the company's retirement income program, the study's authors said, employers "may be able to address many issues at once: the 'deal' around retirement income responsibilities, the effectiveness of the retirement program, the line of sight between organizational performance and total remuneration, and the links among health, wellness, productivity, and wealth, among others."

## Fees Vary Among Retirement Plans

As sponsors of 401(k) plans appear to be taking steps to minimize the investment management fees charged to participants, improved guidance may be needed to reduce fees for participants in individual IRAs and some other types of defined contribution plans, especially 403(b) plans, a report published by the U.S. Government Accountability Office (GAO) has indicated.

The report, "Better Information and Sponsor Guidance Could Improve Oversight and Reduce Fees for Participants," was prepared in response to a request made by the House Ways and Means Committee. In recent years, the study's authors said, policymakers have increasingly focused on the oversight of 401(k) plans and the fees charged to 401(k) plan participants. While

the focus of research into the impact of fees has so far been primarily on 401(k) plans, the GAO expanded its investigation of the issue in this latest study to include a more detailed look at the types of fees charged not only to participants in 401(k) plans, but also to investors in IRAs, 401(a) plans, 403(b) plans, and 457 plans.

Even as participants in defined contribution plans and IRAs accrue earnings on their investments, researchers explained, they also pay a number of fees to the service providers that manage their plan's mutual funds or other investment products, including expenses, commissions, or other charges associated with investments and plan operation. "Fees are one of many factors—such as the historical performance and investment risk for each plan option—participants should consider when investing in a retirement plan because fees can significantly decrease retirement savings over the course of a career," researchers advised.

Based on interviews with service providers and other retirement planning experts, the study found that, generally, defined contribution plan participants pay the same types of fees, regardless of the type of plan in which they are enrolled, and that traditional IRA account owners generally pay the same types of investment fees as defined contribution plan participants.

However, researchers also found that 403(b) plan participants and IRA owners are more likely than participants in 401(k), 401(a), and 457(b) governmental plans to invest in products with higher fees, such as variable annuities. Whereas most defined contribution plan participants tend to invest in mutual funds, which have no insurance guarantees—and hence lower fees—403(b) plan participants have higher rates of investment in variable annuities, which charge not only investment fees for the underlying mutual funds, but also fees associated with the insurance portion of the product. In addition, 403(b) plan participants were also shown to be more likely than other defined contribution plan participants to invest in individual

annuities, which generally charge higher fees than group annuity products.

In investigating why participants in 403(b) plans purchase more variable annuities, researchers found that individual participants often have a more central role in choosing investment options than participants in other types of plans, with each participant having a one-on-one relationship with their service provider. Results further showed that annuity providers are more likely than mutual fund providers to market directly to 403(b) plan participants, when permitted to do so.

Meanwhile, the findings also indicated that IRA owners tend to pay higher fees because they are retail, or individual customers, and therefore lack the bargaining power of larger institutional investors. Indeed, the report noted, one expert explained that it is common for individuals rolling over their assets from a defined contribution plan into an IRA to see an increase in investment fees, largely because individuals no longer have the group's bargaining power to purchase lower-cost investment products.

The study's authors observed that retirement plan sponsors can take a number of actions to reduce participants' fees, such as offering relatively low-cost mutual funds and other investment products, or by pooling assets to obtain pricing advantages. The study's findings showed, however, that while 401(k) and 401(a) plan sponsors frequently pool assets to obtain lower mutual fund fees, 403(b) plan sponsors often fail to do so. Instead, they said, "many 403(b) plan sponsors keep sponsor involvement to a minimum, which limits the opportunities to pool assets and decrease fees."

To help address this problem, the report's authors recommended that the U.S. Department of Labor (DOL) and the Internal Revenue Service (IRS), which are jointly responsible for overseeing various aspects of defined contribution plans and enforcing requirements for fee disclosure, provide guidance to all sponsors about the role they can play in reducing



*Researchers also found that 403(b) plan participants and IRA owners are more likely than participants in 401(k), 401(a), and 457(b) governmental plans to invest in products with higher fees, such as variable annuities.*

fees. The authors further advised Congress to consider amending the Employee Retirement Income Security Act (ERISA) to require all sponsors of defined contribution plans to disclose fee information.

## Consistent Contributions Pay Off Despite Bear Market

Retirement savers who held 401(k) accounts consistently from 2003 through 2008 saw their balances decline by an average of 24.3% in 2008, but saw overall gains over the five-year period, according to a report published by the Employee Benefit Research Institute (EBRI) and the Investment Company Institute (ICI).

The study's findings are based on information drawn from the EBRI/ICI 401(k) database, which includes records on 24 million participants, of whom 6 million consistently had 401(k) accounts with the same employer each year from year-end 2003 through year-end 2008. An analysis of data on 401(k) account balance performance among this group of participants between 2003 and 2008 showed that the average account balances increased at an annual rate of 7.2% over five years, even after the 2008 losses.

Results showed that the average account balance at year-end 2008 came to \$45,519, down substantially from \$65,454 at year-end 2007. Researchers noted that this 30.5% decline in the average balance from 2007 to 2008 reflects changes in the composition of the participant and plan sample, as well as worker contributions, employer contributions, and investment gains and losses. Over the same period, the Standard & Poor's 500 stock index fell 37%.

Yet, for consistent participants, the average account balance came to \$86,513

at year-end 2008, up from \$61,106 at year-end 2003, and the median account balance among this group grew to \$43,700 at year-end 2008, up from \$25,507 at year-end 2003, representing an annual increase of 11.4% over the five-year period.

The analysis showed that different cohorts of 401(k) participants fared differently last year, and that variation is largely based on age and tenure of the individual worker, Jack VanDerhei, EBRI director of research and co-author of the report, noted. For example, he pointed out, "mid-career workers with larger balances suffered larger percentage losses overall last year, because the share of equities in their account allocation was relatively high and their ongoing contributions were small relative to their existing balances." Among the consistent participants, VanDerhei added, those in their twenties saw their average account balance fall by 18.6% in 2008, while those in their forties experienced an average decline of 26.4%.

The study also found that, despite the downturn, the bulk of 401(k) assets continued to be invested in stocks. At year-end 2008, an average of 56% of assets were invested in equity securities through equity funds and company stock, while 41% were invested in fixed-income securities, such as stable value investments and bond and money market funds.

Moreover, three-quarters of 401(k) plans included lifecycle, or target date, funds in their investment selection at year-end 2008. Also, at year-end 2008, nearly 7% of the participants' assets were invested in lifecycle funds, and 31% of 401(k) participants held lifecycle funds.

Finally, the analysis showed that 401(k) loan activity was in line with historical experience: In 2008, 18% of 401(k) participants eligible for loans had a loan outstanding against their 401(k) account, the same percentage as at year-end 2007 and year-end 2006.



*An analysis of data on 401(k) account balance performance among this group of participants between 2003 and 2008 showed that the average account balances increased at an annual rate of 7.2% over five years, even after the 2008 losses.*

The information contained in this newsletter is for general use, and while we believe all information to be reliable and accurate, it is important to remember individual situations may be entirely different. The information provided is not written or intended as tax or legal advice and may not be relied on for purposes of avoiding any Federal tax penalties. Individuals are encouraged to seek advice from their own tax or legal counsel. This newsletter is written and published by Liberty Publishing, Inc., Beverly, MA. Copyright © 2009 Liberty Publishing, Inc. All rights reserved.