PLAN SPONSOR
outlook
A Resource on Current Issues for Plan Sponsors and Administrators
Second Quarter 2014

Plan Distributions Are Being Saved

In recent years, plan sponsors and the retirement plan industry have been increasingly concerned about the rising number of plan participants terminating employment who take their 401(k) account distribution in cash, since many of those dollars will not find their way into other retirement savings arrangements. Two new studies indicate that there is reason to be more optimistic today about those disappearing retirement savings dollars.

The Vanguard Center for Retirement Research has found that retirement-age defined contribution plan participants are preserving their assets at an encouraging rate. About 70% of participants are preserving their savings in a tax-deferred arrangement for at least five years after terminating employment.

The study of 267,000 participants age 60 or older who terminated employment in 2004 through 2011 also revealed that 90% of dollars saved in a retirement plan were preserved, either in an employer-sponsored plan (35%) or an IRA (55%).

Small accounts cashed out

Around 30% of retirement-age participants who took cash distributions after terminating employment usually had small account balances. The average amount cashed out was about $20,000.

Participants who preserved their savings had average balances ranging from $150,000 to $225,000.

Most assets leave the plan over time

Although nearly three-quarters of retirement-age participants kept their retirement savings intact, only about 20% of these employees still had plan account balances five years after termination. And only 20% of assets remained in the employer-sponsored plan after five years.

Vanguard's report, "Retirement distribution decisions among DC participants," is at http://tinyurl.com/RetirementDistribution.

The EBRI analysis had similar findings

The Employee Benefit Research Institute (EBRI) studied lump-sum distributions of retirement savings plan account balances

across a broader range of participants (those who reported having ever received a distribution). The researchers obtained results similar to Vanguard's: More workers seem to be saving, not spending, the distributions they receive from their retirement saving plans.

Half completed at least a partial rollover

Almost half of the group studied reported rolling over at least some of their most recent distribution to a new employer-sponsored plan or IRA, and nearly all of these participants rolled over the entire amount.

Fewer than 16% reported using some of their distribution for consumption (for example, paying bills, major purchases, etc.). Only 7% said they used the entire amount for consumption.

EBRI's "Lump-Sum Distributions at Job Change, Distributions Through 2012," is available at http://tinyurl.com/EBRILumpSum.

What are the top 10 steps you, as a plan sponsor, want to take this year regarding your company's retirement plan? See Mercer's list at http://tinyurl.com/Mercer2014Steps.

Equities Continued to Attract Contributions

At the end of 2012, 61% of 401(k) plan assets were invested in equities, according to the Investment Company Institute's "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2012" report. This included equity funds, the equity component of target-date and balanced funds, and employer stock.

Among participants who were under age 40, almost 75% of assets were in equities. Those in their 60s had less than half of their plan assets in this asset class.

Target-date funds remained popular

Almost three-quarters (72%) of 401(k) plans had target-date funds among their investment options at the end of last year. Target-date funds were used by 41% of participants, and these funds held 15% of total 401(k) plan assets.

New hires chose balanced funds

More than half (54%) of the account balances of new hires in their 20s were in balanced funds, including target-date funds, at year-end 2012. About 43% of the balances of this group were in target-date funds.

The average account balance rose

Compared to the end of 2011, the average participant account balance rose 8% to $63,929 at year-end 2012. Of course, investment performance and many other factors affect account balances, so the average amount must be viewed with caution.

The Investment Company Institute (ICI) report, using data from the Employee Benefit Research Institute/ICI database of 24 million 401(k) plan participants in nearly 65,000 plans, is at http://tinyurl.com/ICIPlanData2012.

The expected retirement age of workers continues to rise, according to the Employee Benefit Research Institute. Visit http://tinyurl.com/EBRIRetAgeRising for this snapshot report.

Pension Plan Limitations for 2014	
401(k) Maximum Participant Deferral	**$17,500*** **$23,000 for those age 50 or over, if the plan permits*
Defined Contribution Maximum Annual Addition	**$52,000**
Highly Compensated Employee Threshold	**$115,000**
Annual Compensation Limit	**$260,000**

Financial Wellness Is Focus of Plan Sponsors

Aon Hewitt's *2014 Hot Topics in Retirement* survey found that retirement plan sponsors will continue to emphasize the overall financial wellness of employees this year.

Advice options expected to grow

Nearly half (44%) of responding employers currently make investment advice available to employees, and an additional 14% are very or somewhat likely to add this service this year.

About one-third (35%) of companies offer access to third-party advisors by phone. Another 14% are somewhat or very likely to provide this support in 2014.

Almost one-quarter (23%) make in-person meetings with financial advisors available. About 10% of employers are very or somewhat likely to offer this support this year.

Other support is or will be offered

About 25% of companies say they are very likely to offer budgeting advice to employees so that they can handle expected expenses and still have money for savings.

Aon Hewitt's report is at http://tinyurl.com/2014HotTopics.

Social Security Remains Primary Income Source

According to the AARP Public Policy Institute's "Sources of Income for Older Americans, 2012" report, Social Security remained the major source of income for individuals age 65 or older in 2012. The average annual amount received by Social Security retirement beneficiaries was $14,229.

About 38% of total income of the 65-or-older population was from Social Security. It accounted for 80% of income for people with low or moderate incomes.

Other income sources were important

Interest income was the second most important source. Nearly half (46%) of those in this age group reported income from interest.

About 30% of this group had income from pensions and retirement savings.

Earnings from employment were received by 22% of people age 65 or older.

This report, compiled from U.S. Bureau of the Census data, is at http://tinyurl.com/AARPIncomeSources.

Plan Sponsors Ask...

Q: Are predictions about the retirement prospects of Americans as dire as the headlines would make them seem?

A: At least one industry expert, Nevin Adams, co-director of the Employee Benefit Research Institute's Center for Research on Retirement Income, thinks not. Adams says that these gloomy predictions likely over-state the situation. He cites estimates of retirement savings shortfalls from the Center for Research at Boston College and other authoritative sources. These and other researchers estimate a total shortfall of at least $6 trillion for those in the 55-to-64 age group.

Adams notes that data from an older Federal Reserve study have been used, along with assumptions about assets from defined benefit plans and target savings needs. Also, some estimates of shortfalls are based on other factors that don't appear to be related to actual income or spending in retirement. These and other data used in predicting shortfalls may not be appropriate, he notes.

He reports that the EBRI's latest projection regarding the gap between needs and available financial resources is only about two-thirds of other widely publicized gap estimates. While this is, of course, still a figure that should raise concern, Adams cautions that individual shortfall amounts are a combination of circumstances, preparation, financial needs and access to help.

See Nevin Adams' blog post at http://tinyurl.com/NevinAdamsPost.

Q: What is the latest estimate of how much retirees will need in order to cover their healthcare expenses during retirement?

A: Fidelity Benefits Consulting, which has calculated this figure since 2002, reports that a 65-year-old couple who retired in 2013 will need about $220,000 to pay for healthcare costs throughout their retirement. This figure excludes nursing-home care, and only applies to those with traditional Medicare coverage.

This represents an 8% decrease from the 2012 projection of $240,000. Fidelity noted that the decline is due to a reduction in utilization of healthcare services in an uncertain economy, smaller payment increases to healthcare providers and demographic changes. It also anticipates smaller provider payment increases in the coming years.

Fidelity points out that many people under-estimate the savings they will need to cover healthcare in retirement. A recent survey of pre-retirees (those age 55 to 64) revealed that half of the respondents felt they would need only $50,000 for healthcare.

Fidelity's announcement is at http://tinyurl.com/FidelityMedExpenses.

Q: What concerns does Generation X have about retirement?

A: The *2013 Employee Financial Wellness Survey* conducted by PricewaterhouseCoopers (PwC) indicates that Generation X struggles with competing financial priorities long before retirement. They think it's likely that they'll have to take money out of their retirement savings for non-retirement purposes. In fact, 30% reported already having done so.

Generation X (those born in the early 1960s to the early 1980s) has pressing financial concerns, according to survey results. Almost half (49%) have difficulty meeting household expenses on a timely basis each month, 58% maintain credit card balances on a consistent basis, and almost half have trouble making minimum payments on time each month.

This age group's top five concerns about retirement are:

- Running out of money (45%)
- Healthcare expenses (38%)
- Being unable to maintain current standard of living (26%)
- Health concerns (25%)
- Inability to handle monthly expenses (21%)

PwC's survey report is at http://tinyurl.com/GenXSurvey.

Few 401(k) plan participants take loans, a pattern that has continued for 20 years. See the Employee Benefit Research Institute's Fast Facts at http://tinyurl.com/EBRILoans.

Guidance on In-Plan Roth Rollovers Issued

Among other clarifications, the Internal Revenue Service's Notice 2013–74 notes that an in-plan Roth rollover of an otherwise non-distributable amount can be made only by direct rollover, which is not subject to tax withholding. However, the taxable amount is to be included in the participant's income.

A qualified distribution from a designated Roth account is one due to death, disability or reaching age 59½, and must be made after a five-year period. This notice confirms that an in-plan Roth conversion qualifies as a first contribution that begins the five-year period, effective on the first day of the plan year in which the rollover is made.

Sponsors choosing to permit in-plan Roth rollovers must separately account for rollover amounts. Also, they will have to track contributions that have different withdrawal restrictions to ensure proper tax treatment and adherence to distribution restrictions.

(Amounts rolled over, and related earnings, are subject to distribution rules that applied to those amounts prior to the in-plan Roth rollover.)

Notice 2013–74 is at http://tinyurl.com/IRSNotice2013–74.

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
BenefitsLink	www.benefitslink.com
PLANSPONSOR Magazine	www.plansponsor.com
Plan Sponsor Council of America	www.psca.org
Employee Benefits Institute of America	www.ebia.com
Employee Benefit Research Institute	www.ebri.org

Plan Sponsor's Quarterly Calendar

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

JULY

- Conduct a review of second-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 April 1 and June 30 received and returned an enrollment form. Follow up for forms that were not returned.
- Ensure that the plan's Form 5500 is submitted by July 31, unless an extension of time to file applies (calendar-year plans).

AUGUST

- Begin preparing for the distribution of the plan's Summary Annual Report to participants and beneficiaries by September 30, unless a Form 5500 extension of time to file applies (calendar-year plans).
- Submit employee census and payroll data to the plan's record-keeper for mid-year compliance testing (calendar-year plans).
- Confirm that participants who terminated employment between January 1 and June 30 elected a distribution option for their plan account balance and returned their election form. Contact those whose forms were not received.

SEPTEMBER

- Send a reminder memo or email to all employees to encourage them to review and update, if necessary, their beneficiary designations for all benefit plans.
- Begin preparing the applicable safe harbor notices to employees, and plan for distribution of the notices between October 2 and December 2 (calendar-year plans).
- Distribute the plan's Summary Annual Report by September 30 to participants and beneficiaries, unless an extension of time to file Form 5500 applies (calendar-year plans).

Kmotion, Inc., P.O. Box 1456, Tualatin, OR 97062; 877-306-5055; www.kmotion.com

LPL Financial