# Defined Contribution Insights

The Solution Source for Plan Sponsors

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PSCA
Plan Sponsor Council of America
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# Editor's Note

## An Avalanche of New Legislation

Though we have not yet needed to pull out the shovels here in Northern Virginia, we have needed them to dig into the more than 90 retirement-related provisions of the SECURE 2.0 Act this winter. As this issue's *Leadership Letter* claims, 2022 was the year of major retirement legislation that will shape and reshape the retirement landscape. Stay tuned to PSCA for more information on the provisions affecting your plan.

In this issue's *Plan Sponsor Perspectives* we asked plan sponsors what items are on their to-do-list this year, and what topics they would like to hear more, or less, about. Granted, recent legislation may have shifted those priorities as this was compiled before SECURE 2.0 was enacted.

Last year we asked a QOTW per a member request on how other plan sponsors handle very small account balances. The responses varied and many plan sponsors were asking what the best practice was on this, so we asked PSCA member, Adam Greetis, to write an overview of the options and pros and cons on how to handle this common plan administration dilemma.

In an article from the Education and Communication Committee, Beth Pattillo asked a variety of people — participants, retirees, other plan sponsors — what retirement readiness means to them. The results of this informal survey are illuminating in that there is still absolutely no consensus.

We have two articles about HSAs in this issue — one from the HSA committee regarding the challenges of HSA administration and a summary of the *2022 HSA Survey* — I hit the highlights of this year's survey results and show how HSA programs are starting to resemble 401(k)s.

Additionally, NQDC Committee Chair Matt Maier gives us the rundown on state source taxes for NQDC plans and some of the key timelines that participants should be aware of.

ICYMI, *PSCA's 65th Annual Survey* was released in December. I include the highlights from that survey and discuss some of the plan design trends that led to record contribution rates in 2021.

This issue's *Washington Watch* discusses the new ESG rule, though there have been very recent developments to this since the article was written in which several states are suing to prevent this rule from taking effect.

In this issue's *Retirement Read(y)* article, Nevin Adams takes on academics (again) — it could be argued that a paper provocatively titled "The Life-Cycle Model Implies That Most Young People Should Not Save for Retirement" was asking for it.

Get the shovels ready!

~ Hattie

### PSCA Mission Statement

The Plan Sponsor Council of America (PSCA) is a broadly based association of diverse businesses which believe that profit sharing, 401(k), and related savings and incentive programs strengthen the free-enterprise system, empower and motivate the workforce, improve domestic and international competitiveness, and provide a vital source of retirement income.


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# Leadership Letter

## 2022: The Year of Legislative Changes

**SECURE 2.0 passed after a year-long process of combining bills.**

Last year saw multiple pieces of legislation introduced in the House and Senate aimed at increasing the retirement security of Americans, and 2022 ended with the passage of SECURE 2.0 at the eleventh hour. SECURE 2.0 is a combination of multiple other pieces of legislation and includes more than 90 retirement-related provisions. Throughout the year, PSCA and ARA were on the hill advocating in the best interest of plan sponsors, ensuring that proposed provisions were aligned with plan sponsor priorities. PSCA's leadership committee met with key hill staffers in October to discuss their retirement plans and advocate for policy change that would help increase the retirement security of their participants.

As we look forward to 2023, we are excited about our in-person National Conference in Orlando in May, as well as continuing to provide the high-quality virtual education you have come to expect through webinars, virtual roundtables, coffee talks, and the CPSP virtual classrooms.

### Certified Plan Sponsor Professional Credential

We launched the first of its kind educational program and credential exclusively for retirement plan sponsors in April of 2019. To date, more than 1,350 professionals have earned this credential. The program has grown considerably since its inception and the addition of the virtual classrooms contributed to the growing success for this program. If you have not yet gone through the CPSP course, there will be multiple options to do so in 2023, both virtually and in-person.

### Education

PSCA continues to provide education tools for plan sponsors and participants. We added a new module to the Plan Sponsor Tool(k)it, bringing this comprehensive set of education tools to 11 modules on topics ranging from vendor searches, managed accounts, financial wellness tools, to pre-retirement participant resources, and modules on plan withdrawals and fiduciary governance. More modules are in the works for 2023.

PSCA also launched its annual 401(k) Day campaign, a "Know Your Numbers" worksheet to help participants determine what they have and what they need for a healthy financial future. The new campaign as well as past campaigns are available anytime to members on our website.

PSCA held eight webinars in 2022 and a new Virtual Investment Summit with four sessions, which all helped address the pressing concerns of plan sponsors, provide insights into what was happening in Washington that affects plans, and provide continuing education opportunities to plan sponsors.

Last but not least was PSCA's 2022 National Conference, held in-person with more than 300 people in attendance, including 190 plan sponsors engaging in general and breakout sessions and enjoying PSCA's 75th anniversary celebration. This year's conference will build on the excitement and engagement as we meet in person in Orlando, FL May 3–5, 2023. Don't miss out on what will be the largest PSCA National Conference we've held to date and register soon!

### Research

PSCA produced four annual surveys this year — industry-leading research on 401(k) Plans, 403(b) programs, nonqualified deferred compensation plans, and Health Savings Accounts.

PSCA also continued its Question of the Week (QOTW) in the weekly ICYMI newsletter. This new feature has been very well received and allows us to quickly gather and provide feedback for members and on current proposed legislation. At the end of 2022 we created a QOTW archive where there is a wealth of topical information gathered from more than 50 questions throughout the year. If you have any questions you'd like us to ask this year, send them to research@psca.org.

Thank you for your support of PSCA as we continue to work together to improve the retirement outlook for all. We look forward to seeing you at the National Conference in May!

# Plan Sponsor Perspectives

## 2023 Plan Priorities

### Plan sponsors weigh in on their retirement plan objectives for the new year.

*By Tobi Davis*

For this issue we asked our members the following questions: As we look ahead to next year, what are your retirement plan priorities? Are you planning any new initiatives? Are you concerned about the impact of inflation on plan participants? Are there any retirement plan topics you would like more resources/information about? Are there any topics that you are tired of hearing about?

The responses were as varied as our members. Starting with plan priorities and new initiatives for 2023, adding a match is on the to-do list for a few of the respondents. One person noted, "The thing that I've noticed recently is that potential hires are making acceptance decisions based on our 401k. Our match is not competitive so I am hoping that we can get this changed at some point very soon."

Implementing financial wellness resources is also important to a few plan sponsors. However, the largest area of focus for those who responded is education. This encompasses education on specific plan features, general education about saving for retirement, financial wellness, or communications around the market roller coaster and downturn and what participants should (or should not) be doing with their investments. One plan sponsor intends on doing a "full review and

update of our plan promotional materials for our entire employee lifecycle, from applicant to retirement." A few respondents are concerned about staying in compliance and one is doing a recordkeeper RFI to make sure they are "checking all the boxes" on compliance.

One plan sponsor will use their data to understand their participants' utilization of the retirement plan. "As a plan sponsor and fiduciary member, it's important to understand the data and how participants are utilizing the retirement plan in their wealth-building years. Reviewing participant elections across the contribution sources allows us the opportunity to understand the employee experience. Once the analysis is complete, opportunities become available to enhance the employee experience with enhanced education programs or even more robust plan design."

One person would like to add auto-enrollment but shared she needs "more information on how to build a business case for auto enrollment in a high turnover industry. How do you convince your employer that it's a good thing for the employees, and you are not forcing them into something they don't want? How do you get employees to see the value of a 401(k) and combine that with auto enrollment?

How do you convince your employer who questions if auto enrollment really will increase satisfaction and retention amongst employees?" Some plans will be adding Roth while another sponsor intends to make changes if SECURE 2.0 passes. Most likely a lot more plans will be adding Roth features if the legislation passes.

HSAs are top of mind for a few members. One plan sponsor shared, "Health Savings Accounts are powerful tools to save for healthcare expenses into retirement, and getting employees to see them as investment vehicles with ability to invest in the markets is the savings area outside of our 401(k) plan that we continue to focus on."

Other priorities for 2023 include considering CITs for investments, providing lifetime income to participants, and communicating the retirement plan benefit in order to recruit and retain talent.

## Inflation Impact

With the high inflation rate and economic uncertainty, plan sponsors are worrying about their participants and the financial effects they are feeling. As a member put it, "While I love the opportunity to help educate our employees on retirement and how important it is to save towards a future goal, with what our employees are facing currently in the areas of financial stress, we have pivoted to a different area to assist our employees. With the rising cost of heat, electricity, housing, and food, we've begun having in-person financial sessions on assisting our employees to help them create budgets and what they need to do to stick to the newly-drafted budget. Our hope is to continue the financial support for our employees and continually provide aids/discussions/tools to help them realize their financial goals, including their retirement."

Another plan sponsor is thankful that her plan has auto-enrollment and escalation features. She notes, "These features help decrease the likelihood of employees either not enrolling in the plan or enrolling at a lower rate." Other respondents shared a similar sentiment. One plan sponsor noted that the company has taken action with their compensation to address inflation. To address participants deterred by inflation from deferring in the plan, a plan sponsor has "recommended that a participant contribute one percent into the retirement plan so that they can receive the two percent employer match. We have had quite a few participants start their retirement plan journey by contributing the one percent. I think knowing that it's a pre-tax benefit and that they are receiving two percent from the employer helps."

Some people, while concerned about inflation's impact on their employees, have not seen changes in participation, deferrals, or loan and withdrawal activities. One plan sponsor is looking at "vehicles for either emergency funds or emergency (low interest) loans."

Another person explained, "Right now, we have been reinforcing the 'hang in there' approach with market volatility and to keep contributing to your 403(b). As food costs (or just about everything) continue to rise, well above any annual increases that they are receiving, and gas prices stay high, I do expect to see participation decrease in both the percent of staff in the plan and their level of contributions. Unfortunately, when difficult decisions must be made in the short-term, saving for retirement in 40-plus years doesn't have much appeal. I was hoping that we could start looking at auto escalation in the coming year, but I am not sure the timing is right to start those conversations."

One member shared, "I always get concerned when I see employees reducing their contributions or taking out large loans. This is where continuing education is key to helping them understand the market's 'peaks and valleys' and how not to make emotional decisions."

## Retirement Topics

Many members shared the topics they want more information about and which topics they are tired of hearing about. Fiduciary responsibility is still a requested topic by some, as explained by a respondent, "I constantly worry about fiduciary obligations and ensuring we are compliant. Please continue to let us know what's trending, important legal cases to note, etc." Other topics requested included: DEI resources (especially how to address barriers to saving), information on new legislation and PSCA's lobbying efforts, HSA information including the intersection with Medicare and how to guide employees, cryptocurrency, tools and planners for retirement readiness, ESG, how to monitor lifecycle funds, DOL complaints on 401(k) plans, how to engage young, lower-wage employees, and how to build long term financial wealth.

For topics that people are tired of hearing about, in contrast to the above, some people are sick of hearing about ESG and cryptocurrency. As one person put it, "Cryptocurrency! Enough said. Given the recent failure of FTX, it's time for the industry to take a step back to analyze and provide guidance to better educate plan participants."

PSCA will look into the topics that people want to learn more about and explore ways to offer information and resources to you, our members.

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*Tobi Davis is the Director of Operations for the Plan Sponsor Council of America.*

# Plan Administration

## Small Plan Balances — Choices and Compliance Risks

### A summary of best practices in handling small plan balances for terminated employees.

*By Adam Greetis*

Small account balances in 401(k) plans have forever been a challenge for plan sponsors. The challenge primarily arises from the participant's lack of interest in the small account balance. Amounts above a certain value tend to command the attention of the participant and the participant is likely to respond to distribution notices and instructions. But participants may ignore account values below a certain amount leaving the plan sponsor with administrative burdens and compliance concerns. Congress and the Department of Treasury have, over the years, attempted to help the situation by raising the automatic cash-out limit but no current regulatory solution exists for very small account balances that participants ignore. Plan sponsors have addressed this issue in a variety of ways. These ways include:

- Retaining small plan balances indefinitely.
- Forfeiting small plan balances for missing participants (but restoring them if the participant reappears).
- Retaining small plan balances and allowing the balance to be worn away by administrative fees.
- Automatically cashing out all amounts and using extra efforts to communicate with the participants.

There's no perfect solution and each option has advantages and disadvantages — some including legal compliance risks.

#### Follow the Plan Document

The primary legal concern that can arise with some of these "self-help" solutions is a failure to follow the terms of the plan document. Under ERISA, a plan administrator is obligated to follow the terms of the plan. Most prototype and volume submitter plan documents maintained by the large recordkeepers provide little flexibility when it comes to small balances. These plan documents typically automatically cash out all amounts below the chosen maximum (e.g., $5,000). A plan sponsor that adopts some administrative policy of retaining de minimis account balances to either forfeit them or allow them to be worn away with fees would violate the terms of these plans. That practice would invite a fiduciary breach claim.

Individually-designed plans offer a different alternative. We have worked with some individually-designed plans that do provide for the forfeiture of small plan balances (e.g., under $1,000) where the plan administrator reasonably determines that the participant is missing or unresponsive after conducting a diligent search. The balance would, of course, be reinstated if the participant later appeared. The Treasury regulations do support this approach. Nonetheless, it is critical that employers maintain complete and accurate records with respect to these participants and their account values and that the plan administrator follows current guidance on attempting to locate the missing participant. Further, the practice should be disclosed in the Summary Plan Description.

#### Act in the Best Interest of Plan Participants

Another legal risk with adopting a policy or practice of retaining de minimis accounts and forfeiting them or allowing them to be worn away with fees is a separate fiduciary risk. Under ERISA, a plan administrator must operate the plan and make discretionary decisions prudently and in the best interest of plan participants. A decision to retain these amounts is intended to primarily benefit the plan sponsor and plan administrator at the expense of the participant. Reasons given for this approach include being able to avoid dealing with uncashed checks and avoiding the search for missing participants. Retaining small account balances and not distributing them in no way benefits the participant. ERISA requires the plan administrator to place the interests of the participants first and a failure to do so again, gives rise to a fiduciary breach claim.

So, at the end of the day, we see no risk-free solution other than automatically cashing out all amounts consistent with the plan document or drafting your individually-designed plan to provide for a limited forfeiture right.

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*Adam Greetis is a Partner with Seyfarth Shaw LLP.*

# Academic Alchemy?

## Is retirement saving "wasted" on the young?

*By Nevin Adams*

In a paper provocatively titled, "The Life-Cycle Model Implies That Most Young People Should Not Save for Retirement," four academics take 48 pages to make that case.

Like most research, the conclusion is a premise based on assumptions. Here the most basic is that this thing called a "life-cycle model" is worth considering in the first place. Now, granted, it's a "Nobel Prize-winning theory" — so mere mortals might be inclined to give it some breathing room. But the underlying premise behind it is that individuals prefer to smooth out their consumption over their lifetimes, or — as the authors of the paper put it — it assumes that "rational individuals allocate resources over their lifetimes with the aim of avoiding sharp changes in their standard of living." Now, I don't know about you, but my aspirations — and I consider them rational — have always been a bit higher than that.

As it turns out, the authors do anticipate some growth in income over time — indeed, that's a contributing factor in their logic about putting off saving for retirement. Buttressing this are three basic arguments; first that high-income workers tend to experience "wage growth" over their careers and thus, for them "maintaining as steady a standard of living as possible therefore requires spending all income while young and only starting to save for retirement during middle age" — that's right, it *requires* spending. Second, that low-income workers "receive high Social Security replacement rates, making optimal saving rates very low" — which apparently means that if you're at a low income level now, you'd (only?) be looking to maintain that level into retirement. The final point has to do with what was then an artificially low interest rate environment that they claim "makes a front-loaded lifetime spending profile optimal" — basically, at least at that point in time, they argue you might as well spend the money because there's no economic advantage in saving. But what about market gains, you say? Hang on, we'll come back to that in a minute.

It seems to boil down to this — you'll get more "value" out of spending all of a smaller income now than you will suffer by depriving yourself so that you can spend later when you'll have more money to spend. But to put some numbers behind those assumptions, you have to do a little financial alchemy — create some sort of "value" for consumption — something beyond a mere price tag. How much *does* that cup of Starbucks that we're always telling people to forego actually mean to them in terms of what academics call "utility"? Indeed, that's another required assumption here — and it is key in terms of assessing the perceived trade-offs.

What's also odd here is that they actually talk about the "welfare costs" of automatic enrollment — essentially treating an individual who has been defaulted into saving as the equivalent of being scammed by a Nigerian prince.

For those of you wondering what happened to the "magic" of compounding those savings, the authors have a direct, but quizzical response: "…there is no power of compound interest when real interest rates are zero. While individuals could invest in risky assets with higher expected returns (which we do not model), those higher returns are merely compensation for taking on the additional risk." So, basically, in this magical theoretical world … it's a "wash."

Oh — and leakage? Well, in this imaginary world, having that savings returned to you for spending is a *good* thing (doubtless the taxes and penalties are considered a well-deserved "punishment" for the mistake of saving).

That said, the authors do offer some caveats — they admit that they're focused on saving for retirement, and that there may indeed be reasons for saving earlier for non-retirement purposes. But they also admit that their model "does not account for uncertainty about future wages, employment, or health." They acknowledge that "if the wage profile is uncertain, or if there is a risk of future unemployment, individuals may wish to begin saving for retirement earlier in life in case future earnings do not turn out as expected."

Ya think?

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*Nevin E. Adams, JD, is the Chief Content Officer for the American Retirement Association.*

# Challenges of HSA Administration

## Many employers face administrative, education, and engagement challenges with their HSA programs.

*By Blanca Gonzalez Karim, Carol Sedlako, and Alyona Richey for PSCA's HSA Committee*

Health Savings Accounts (HSAs) have been around since they were established into federal law in 2003. The HSA has been gaining more popularity and many employers offer this option as part of the total benefits package due to its many tax-advantages. With an increase in popularity of HSAs, employers are now facing additional challenges, including administration, employee education, and employee engagement.

Employers face many administrative challenges with HSA accounts. Some of the most common challenges are:

- Time, workload, and costs involved in managing these accounts — can include software, personnel, enrollment meetings, and expense certification.
- Managing excess contributions and the required corrective processes when contributions are made outside of the payroll process.
- Additional administrative responsibilities when employees don't open an account when required and contributions bounce back.
- Service issues when mistakes happen.

There are some ways employers can prevent or minimize these challenges. First, it is important to select the right vendor with technology and processes to support the HSA administration and to make the process streamlined. For example, the medical insurance plan might be able to have an integration with an HSA vendor which streamlines the enrollment process. It might also allow the medical provider to feed the eligible enrollment data directly to the HSA vendor.

Second, the benefits department should create an internal process to communicate the deadlines related to enrollment in the HSA accounts and the importance of meeting the deadlines. Part of this process should include auditing of the HSA contributions at least quarterly to avoid making corrections later in the year. Lastly, a good communication strategy will help with reminding employees to review their HSA accounts and any contributions they may make outside of their payroll process. This approach will avoid any excess contribution issues later in the year.

Another common challenge for employers is employee education, which can include topics such as:

- Understanding contributions can be adjusted throughout the year.
- Relying only on employer contributions and choosing not to contribute on their own.
- Making cost efficient decisions when it comes to receiving care since they're relying on employer contributions which are not their own (which negates the "consumerism" intent of these plans).
- Understanding the triple tax advantages of these accounts.
- The beneficial impact HSAs have at retirement for qualified health care expenses not covered by Medicare — such as dental and vision.
- Understanding the long-term advantages of saving and using the HSA for LTC or Medicare premiums.
- Making catch-up contributions (at age 55 or older) to take advantage of tax savings.
- Understanding post death benefits — spouse can assume the HSA upon death, or it can be transferred to one's estate where it's taxed at market value.

One approach to handle the education challenge is to create an ongoing communication plan to address all of these issues. The communication plan can be targeted to new employees and existing employees in the form of a webinar which can be recorded and posted to the intranet for future use and include the use of reminder emails, posters and flyers with QR codes so that employees can easily access content with their phones, and a speaker to highlight the HSA benefits and address all the questions that may come from the employees during the session. This communication strategy will need to adjust annually based on the employee feedback and the interest for future sessions.

In addition to the education and communication challenges, there is also a challenge with employee engagement. It is common for employees to only review their benefits once a year during open enrollment or when they first join the company. Benefits professionals will need to find creative ways to keep the momentum going post new hire enrollment or post annual open enrollment by reminding employees about all the benefits and resources available to them, including their HSA accounts. This goes back to setting the right communication strategy described earlier. A lack of engagement from employees can result in:

- Not opening the account when required.
- "Set it and forget it" attitude after account is opened.
- Not exploring the investment options offered to maximize earnings.

A couple examples of common challenges and how to handle them:

1) Because IRS rules allow for prior year HSA contributions up to and including April 15th of the following year, this can cause multiple administrative burdens if an employee's HSA account was not opened prior to the April 15th cutoff date for contributions. If employee and/or employer contributions were deducted from the prior year's pay, those amounts will need to be corrected and a W2-C may be needed to correct the affected employee's taxable income as well as a 941X to correct the employer's tax return.
2) For employees covering a spouse — if a spouse becomes eligible for other coverage and enrolls separately in a HDHP with a Health Savings account, this may cause an employee to overcontribute to their HSA. Should it be discovered there was an overcontribution:
   1. IRS rules state that it is acceptable for the employee to remove the excess contributions and any net income resulting from the excess contribution before filing their federal income tax return; the employee would pay income tax on the excess amount removed; and,
   2. The employee can leave the excess contributions in the HSA and pay a 6 percent excise tax on excess contributions. (Source: irs.gov)

HSAs have many advantages and there are many benefits with making it available to employees. As with any other benefit plan and program, there will be some challenges for employers to overcome. However, these challenges can be resolved with the right process, vendor, and a solid communication strategy.

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# Retirement Leakage: Who's Got a Wrench?

## Balancing immediate and future needs of participants can be a true balancing act.

*By Lenora Hernandez and Jeffery Kowalczyk for PSCA's Education & Communication Committee*

What is retirement leakage? It is the loss of assets from a defined contribution plan due to a non-retirement event. There are several reasons that these distributions occur which include: premature distributions from a retirement account while employed but prior to reaching retirement age (these distributions are normally taxed and more often than not are penalized), participant loans and the default of a loan upon the employee's separation of employment, hardship withdrawals, and distributions upon termination instead of rollovers.

Professionals in the qualified retirement plan space understand the nuts and bolts of managing an ERISA-qualified retirement plan, which always requires great care, skill, and judgment. It is also well understood that participant behavior and employee engagement can be challenges to the plan sponsor's fiduciary responsibility, especially when managing participant loans, distributions, and hardship withdrawals in difficult times.

Let's begin the plan leakage conversation by considering loan provisions. Loan provisions may be restrictive or more permissive — the plan sponsor should consider the provision for the benefit and wellbeing of its plan participants and beneficiaries. Some plans allow participants to have multiple loans outstanding at the same time, whereas some plans limit participants to one loan outstanding at a time.

There are borrowing limits associated with each loan provision and over time Congress has added new legislation for plan sponsors to consider. The standard limit allows for as much as 50 percent of the vested account balance to be borrowed or $50,000, whichever is less. However, in 2019, the Secure Act further expanded these, based on presidentially-declared disaster areas, and allowed greater limits, which may or may not have been adopted by plan sponsors. Furthermore, in 2020, the CARES Act doubled the maximum loan amount to $100,000 or 100 percent of the account balance. The repayment option, under the provisions of the CARES Act, also permits plan participants to defer their loan payments for up to three years without penalty. When considering loan provisions, the plan sponsor should look at data in the plan to consider how participants are using or will use the provision.

### Participant Impact

Repayment of a loan will put borrowed funds, as well as loan interest, back into the participant's account; however, there are additional considerations. Participants with an outstanding loan may not be financially able to make deferrals during the loan period, and without deferrals they will not receive the employer match. Compounding the situation, investment growth is not maximized during the loan period because assets are no longer in the account and able to compound. It may appear that the repayment of a loan is a benefit for the participant; as a plan fiduciary it is also important to consider the possible negative impact on participants as well.

Are you questioning how to explain the risk of investment loss to the participant? It is a required explanation governed by the Department of Labor and the Internal Revenue Service in the form of a participant notice — *The Comparative Chart of Plan Investments*. Plan investment information, including past investment performance, expense ratios, shareholder fees, and any trade restrictions must be disclosed to new participants within 90 days of becoming eligible to contribute to the plan. All participants must receive updated notices within 14 months of the date they had previously received notice.

### Plan Impact

One of the many core elements to successfully operating a retirement plan is asset growth. If the plan is leaking assets through loan benefits, distributions, and hardship withdrawals, the problem impacts the plan sponsor's ability to negotiate pricing for the purpose of providing retirement benefits and defraying the reasonable expenses that may be impacting all participants within the plan. Also, institutionally-priced services and investment products are known to be offered at lower fees based on the size of the plan's assets, and assets increase

the plan's buying power — like shopping at Costco, the bigger the bulk, the more bang for your buck! It seems fair enough to say plan asset leakage can impact all plan participants with respect to overall plan cost and fees.

## Availability and Use of Loans and Withdrawals

PSCA's *65th Annual Survey*, reflecting 2021 plan data, showed that 83.6 percent of plans allow loans and 90 percent allow hardship withdrawals. *See Exhibits 1 and 2.* The *64th Annual Survey* reported the impact of the pandemic on plans, "Some of the negative financial aspects of the pandemic can be seen in the lower average company contribution, and the slight uptick in loans and withdrawals." Data further showed "more than 90 percent of plans now allow hardship withdrawals, up significantly, and likely spurred by CARES Act provisions aimed at providing financial relief to participants impacted by the corona virus pandemic." Though the use of plan loans and hardship withdrawals dropped in the *65th Annual Survey* report, the percent of plans allowing them remained high, and it's likely plans permanently adopted provisions enacted during the pandemic.

Research at the Transamerica Center for Retirement Studies, gathered in 2020, found that Millennials are taking out loans against their retirement savings at almost double the rate of older generations. What has impacted the Millennial generation? Several issues could be considered, such as greater college loan balances, high levels of unemployment during their early work years, and the Great Recession. Nonetheless, the concerning trend should not be dismissed. What can be done? Plan sponsors should make the effort to understand the generation's retirement financial objectives to determine what appropriate information they will need to make better decisions.

In 2021, the Congressional Joint Committee of Taxation reported 22 percent of net contributions made by plan participants at age fifty and younger left their retirement plans between the years of 2010 through 2015. Additionally, $9.8 billion was withdrawn from retirement plans by participants between the ages of 22 to 25, and these funds did not roll over to another qualified retirement plan or IRA. Leakage defeats the primary advantage of retirement savings. Consider these savings compounding over decades, which can yield dramatically large accumulations of assets. With each leak another cascading stream of growth is removed from the retirement portfolio.

As we look back on 2022 or forward to 2023, the employee choice market (a.k.a., the great resignation), will continue to challenge the plan sponsor with asset growth as well as the separating participant maximizing their retirement savings opportunities.

Employment change is a common factor for retirement leakage as it results in some form of a distribution choice. The most desired choice is to roll over funds to a qualified plan that supports asset growth. Rolling funds to a qualified IRA is also favorable.

The unfavorable, due to employment change, is a distribution that results in tax penalties, fees, and removes growth from the retirement portfolio. An employment separation as it relates to unpaid loans triggers either a very short repayment period, generally 60 days, or the amount still owed on the loan and/or loans (not forgetting certain plans offer up to three loans) converts to a withdrawal.

**Exhibit 1: Plans Permitting Participant Loans by Plan Size**

| | Plan Size by Number of Participants | | | | | |
|---|---|---|---|---|---|---|
| **Availability** | **1–49** | **50–199** | **200–999** | **1,000–4,999** | **5,000+** | **All Plans** |
| Loans Permitted | 72.4% | 79.8% | 85.7% | 91.1% | 95.5% | 83.6% |
| Loans Not Permitted but Under Consideration | 1.5% | 0.8% | 2.7% | 1.1% | 0.0% | 1.3% |
| Loans Not Permitted nor Under Consideration | 26.1% | 19.3% | 11.6% | 7.8% | 4.5% | 15.1% |
| | 100.0% | 99.9% | 100.0% | 100.0% | 100.0% | 100.0% |

**Exhibit 2: Percentage of Plans Permitting Hardship Withdrawals**

| | Plan Size by Number of Participants | | | | | |
|---|---|---|---|---|---|---|
| | **1–49** | **50–199** | **200–999** | **1,000–4,999** | **5,000+** | **All Plans** |
| All Plans | 86.5% | 89.8% | 89.3% | 91.1% | 94.4% | 89.9% |

**Exhibit 3: Percentage of Plans That Allow Participants to Continue to Make Loan Repayments Following Termination of Employment**

| | Plan Size by Number of Participants | | | | | |
|---|---|---|---|---|---|---|
| | 1–49 | 50–199 | 200–999 | 1,000–4,999 | 5,000+ | All Plans |
| All Plans | 86.5% | 89.8% | 89.3% | 91.1% | 94.4% | 89.9% |

## Steps Plan Sponsors Can Take to Reduce Leakage

There are many reasons why participants borrow against their retirement savings, and we are not able to fully address every reason within one article. In this challenging economy it is of best interest for the plan sponsor to take a proactive approach with participants in assisting them with minimizing leakage. Below are some examples that may pertain to plan sponsor asset growth objectives:

- Some plan sponsors have begun to leverage their vendor partners to assist with transitioning outstanding loan balances to the participant's personal financial institution. Offering the separating participant this option may allow them to continue making loan repayments as compared to deeming the loan a distribution. PSCA's *65th Annual Survey* showed that more than a third of plans (34.8 percent) allow repayment of loans after separation of service — this jumps to 63.6 percent of plans with 5,000 or more participants and half of plans with 1,000–4,999 participants. *See Exhibit 3.*
- Plans permitting more than one loan may want to consider reducing the number of loans available to the participant. This could preserve plan assets while minimizing any potential risk by the participant because of loan leakage.
- As previously mentioned, plan sponsors are not required to adopt loan provisions within the plan design. If the plan offers loans, consideration can be made to amending plan design to remove the loan provision.
- Consider emergency savings account services that can help reduce the need for a loan or hardship withdrawal.
- It might be prudent to provide another copy of the Comparative Chart of Plan Investments notice when the participant applies for a loan. Taking time to educate on the investment process may be the difference between borrowing from the retirement account as compared to take a loan with a financial institution.
- Consider percentages for both auto enrollment as well as an annual auto escalation that works within the budget parameters within your company.
- Allowing qualified rollovers, without a wait period, is another way to increase plan asset growth. Rolling assets into the plan should be a regular talking point with existing employees as well as new employees. Human Resources professionals might consider building these talking points into their open enrollment and new-hire orientation processes. Another option is to leverage recordkeepers and have them engage with participants to determine who may hold account balances they may want to rollover.
- Performing a review of your plan with your plan advisor supports identifying design gaps that may promote an increase in plan participation. An engaging campaign raises awareness and knowledge while outlining the rewards of being offered a defined contribution plan. Consideration should be made for all plan participants, including those currently taking distributions.
- Developing more than one strategic educational solution which promotes financial awareness across each of the generations may provide sufficient information for the participant's decision.
- Consider educational opportunities within other areas of retirement such as social security, aging in place, independent living, and assisted living.
- Consider reviewing all employment benefits to identify what may be diluting your core offering. Proactively review non-retirement benefits and consider eliminating and reallocating dollars to enhance the participant's retirement benefit.

## Conclusion

It is ultimately up to the plan sponsor to identify opportunities within the plan or other retirement related benefits that will prevent plan asset leakage and promote asset growth. Yes, it can be a fine line when the plan must align with your workforce goals, must be a benefit within a budget, and meet the expectations of the participants.

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*This article should not be considered legal compliance or advice. We recommend contacting your financial advisor or an ERISA attorney for further guidance. The views expressed in this article are those of the authors individually and should not be construed to be the position of The PNC Financial Services Group, Inc. or any of its affiliates.*

# Source Taxes…Timing Is Everything!

## Potential tax strategy for structuring distributions from the NQDC plan.

*By Matt Maier for PSCA's NQDC Committee*

**Key Takeaways:**

- The structure of your nonqualified deferred compensation plan distribution provisions is important. How participants receive that money can potentially impact their tax liability for many years.
- Participants may want to work with a financial and tax advisor to explore a potentially tax efficient distribution structure.

Each fall, many participants choose how much they will be deferring into their NQDC plan for the upcoming year. Generally, nonqualified plans allow for the pre-tax deferral of base salary, performance bonus, certain types of equity, commissions, and Board of Director fees. That said, many participants do not spend sufficient time choosing a strategy on how they will receive those dollars in the future.

Modern plans typically allow individuals the ability to schedule distributions during their working years "in-service" and/or at separation from service — which is IRS-speak for when you terminate employment.

The in-service distributions are generally paid-out as a lump-sum or in annual installments of up to five years. These distributions are typically designed to pay for something specific, such as a vacation home, to help with a child's college tuition, something fun, etc. As with all cash payments from an NQDC plan, they are taxed as ordinary income when the distribution is received.

For distributions scheduled at separation from service, participants generally have more options. When it comes to taking distributions and paying taxes, having options is a good thing. Most plans today allow for some mix of a lump-sum payment and/or annual installments over a set period of time. In some plans those distributions can be spread over 15 to 20 years. Remember, all cash payments from an NQDC plan are taxed as ordinary income.

Now, here comes the interesting bit. Back in the mid-1990s, when grunge rock and Dr. Martens shoes were popular, the Clinton Administration passed a law that in-part allowed individuals who deferred tax in one particular state and subsequently moved to another state with lower tax rates, to benefit from the lower rates when their deferrals were paid assuming certain conditions are met.

When participants schedule payments throughout 10 years or more, they have the option to take a special tax treatment that is commonly referred to as source tax tracking. If they meet the eligibility requirements, they will only pay taxes in the state of residence when paid and not in the state where the income was earned and deferred.

To illustrate this, let's assume a participant lives in New York with a 10.9 percent state tax rate. If they select installments to be paid over 10 years or more and subsequently move to a state with no state income tax prior to receipt of the first payment, the source tax tracking rules could potentially save them $100,900 per million dollars. That's a lot of Dr. Martens shoes!

**TIP:** Once participants chose a distribution option, it's difficult to change the schedule. Under IRC § 409A, subsequent distribution elections are permitted if allowed by the plan. These changes do not allow the payment to be made earlier than originally elected except in cases of extreme hardship, death, or disability. Unfortunately, simply changing your mind doesn't qualify.

Remember, your plan can allow postponement of scheduled distributions. However, participants must be careful to follow the strict re-deferral rules under IRC § 409A. The request to push back a distribution must be made at least 12 months before the planned date, they must stay employed with the company for the full 12 months, and they must defer the compensation for at least five additional years beyond the original distribution date.

Before participants are required to make annual elections into the deferred compensation plan, consider providing education around this topic or recommending that participants discuss this with a financial advisor. When it comes to selecting distribution payments, timing is everything.

*Matt Maier is Vice President, Lockton Investment Securities, LLC and Chair of PSCA's NQDC Committee.*

# Are HSAs Starting to Resemble 401(k)s?

## PSCA's 2022 HSA Survey is available now.

*By Hattie Greenan*

Health savings accounts (HSAs) may still be used more as spending accounts than savings accounts, but the Plan Sponsor Council of America's (PSCA) 2022 Health Savings Account Survey, sponsored by HSA Bank, finds signs that retirement plans are starting to influence HSA program designs.

Most noticeably, half of large employers — and more than a third of respondents overall — indicate that they do or will position the HSA as part of a retirement savings strategy to employees, according to the PSCA survey, which reported on the 2021 plan-year experience of more than 450 employers. (*See Exhibit 1.*)

One key design strategy employed by more than four-in-ten respondents is the use of automatic enrollment — up from 35.3 percent in 2020 and 32.2 percent in 2019. (*See Exhibit 2.*) Automatically opening HSAs and enrolling employees dramatically increases the savings rate. This includes more than half of small organizations that automatically open an HSA for employees when they enroll in the HDHP. Moreover, nearly six-in-ten (57.2 percent) allow rollovers from HSAs for newly-hired workers, and nearly two-thirds (61.9 percent) educate and encourage rollovers from other HSAs — moves that support the growth of these savings accounts.

Those supportive structures notwithstanding, education remains a significant challenge for the employers that sponsor and look to encourage participation in these programs and continues to be the top HSA concern of employers.

### Differences From 401(k) Plans

One notable area where the design of most HSA programs differs from 401(k) programs is investment of assets — HSAs are still largely treated by participants as short-term spending accounts for healthcare. While more than 60 percent of employers offer investment options for the HSA (with

**Exhibit 1: Percentage of Organizations That Position the HSA as Part of a Retirement Savings Strategy**

| | Organization Size (Number of Total Employees) | | | | | |
|---|---|---|---|---|---|---|
| **HSA As Retirement Strategy** | **1–49** | **50–199** | **200–999** | **1,000–4,999** | **5,000+** | **All Plans** |
| Yes | 24.0% | 25.4% | 28.1% | 25.0% | 50.0% | 27.2% |
| Not Yet, But Planning To | 6.4% | 8.5% | 11.5% | 14.6% | 7.1% | 9.2% |

**Exhibit 2: Percentage of Organizations That Automatically Enroll Employees in the HSA if They Enroll in the HSA-Qualifying Health Option**

| | Organization Size (Number of Total Employees) | | | | | |
|---|---|---|---|---|---|---|
| | **1–49** | **50–199** | **200–999** | **1,000–4,999** | **5,000+** | **All Plans** |
| Percentage of Organizations | 52.3% | 39.7% | 40.9% | 31.1% | 25.0% | 41.5% |

### Exhibit 3: Primary and Secondary HSA Concerns

| | Priority Level | | |
|---|---|---|---|
| Concern | Primary | Secondary | Primary or Secondary |
| Difficulty of Administration | 11.7% | 15.6% | 27.3% |
| Compliance | 13.7% | 16.8% | 30.5% |
| Employee Education | 51.4% | 18.3% | 69.7% |
| Employee Funding Resources | 6.6% | 13.5% | 20.1% |
| Investment Options | 4.6% | 9.0% | 13.6% |
| Fiduciary Liability | 5.4% | 9.3% | 14.7% |
| Medicare Eligibility | 5.4% | 13.8% | 19.2% |
| Other | 1.1% | 3.6% | 4.7% |

wide variability by employer size), just 20 percent of account holders invest their assets in something other than money market funds. (*See Exhibits 4 and 5.*) More than 80 percent of responding organizations still have a $1,000 minimum cash balance as a threshold for directed investments, which could contribute to the low percentage of participants investing assets.

Incorporating HSA education as part of a broader financial wellness program throughout the year with multiple touch points, perhaps alongside your retirement plan education, would go a long way towards reframing HSAs.

Other data highlights from the survey include:

- The average participant contribution in 2021 was $2,958, down from the last few years.
- The average account balance at the end of 2021 was $4,237, down from $6,318 in 2020.
- Three-quarters of employers make contributions to the HSA. Most provide a set amount per coverage level.
- Nearly 70 percent of respondents indicated that employee education is a top concern with half of respondents indicating it is their primary concern regarding their HSA programs. Compliance, Medicare eligibility, and difficulty of administration distantly vie for top secondary concerns.
- More than half of organizations cover HSA maintenance fees themselves. The fees are generally assessed monthly (79.4 percent of plans), and cost less than $3 a month/participant, on average.

The full report can be accessed at https://www.psca.org/research/HSA.

*Hattie Greenan is the Director of Research and Communications for PSCA.*

### Exhibit 4: Percentage of Organizations That Offer Investment Options for HSA Contributions

| | Organization Size (Number of Total Employees) | | | | | |
|---|---|---|---|---|---|---|
| | 1–49 | 50–199 | 200–999 | 1,000–4,999 | 5,000+ | All Plans |
| Percentage of Organizations | 44.7% | 57.9% | 69.0% | 78.3% | 80.0% | 61.0% |

### Exhibit 5: Average Percentage of Participants Who Invested, and Percentage of Assets Invested

| | Year | |
|---|---|---|
| | 2020 | 2021 |
| Average Percentage of Participants Who Invested Assets | 19.3% | 21.5% |
| Average Percentage of Assets Invested in Something Other Than Cash | 28.7% | 27.0% |

# Retirement Readiness: A Point of View

## Participants weigh in on what retirement readiness means to them.

*By Beth Pattillo*

Retirement readiness is a popular conversation topic among my peers and within the financial industry. But what does it mean? Who gets to define it and is there a definition that works for everyone? Who actually owns the responsibility for getting ready for retirement? I set out to see if I could at least come up with a working definition for my organization.

We all see our recordkeepers and consultants come up with tools, recommendations, and educational pieces — most of it helpful. But for me, I struggled with the answers I was seeing for our population. Our organization acquires companies, and we win projects that bring in new employees — in both cases, we provide for prior service. So that means we may end up with Employee A who is 52 years old, has 30 years of credited service, and a balance in our 401(k) plan of $10,000. On the surface, we would all be worried for this person's retirement readiness! In truth, though, Employee A has been with us for six months. They have not rolled over assets from their prior employer. They have not used the data aggregator tool. Employee A could have a million dollars in savings, a possible pension, a partner with retirement savings, rental income … the list goes on, but what it means is that as an employer, I have no idea if our employees are "retirement ready."

### A Very Non-Scientific Survey

So, knowing that I can't get an accurate read on whether or not our employees have saved enough, I wanted to figure out what retirement readiness means. I have been embarking on a very not-scientific survey of random co-workers, friends (both retired and actively working), and strangers. I've posed the question to my Facebook friends. I've asked taxi drivers, wait staff, airline attendants, peers, and several employees. I also asked myself!

As you might expect, the answers ranged from, "Having a good idea about your finances," "Do what I want, when I want," "Stop working so hard and live for me," to more specific items like, "Having no outstanding debt and enough savings to cover unknown challenges while embracing new adventures." One astute respondent said, "Retirement readiness is akin to gambling. I am making choices today that hopefully pay out dividends and puts me in a good spot to handle the unknown."

There was also concern. Some folks said that they were afraid that they would be bored. They didn't want to stop working and be alone. Many brought up concerns about medical coverage. Many others said, "Who knows?!" and will live day-to-day and "hope it works out."

Retirement readiness did not include retirement income. I don't think one person mentioned anything about wondering or planning how to create an income stream to cover 30-plus years in retirement. Most everyone I spoke with focused on themselves — what they want to do, or not do. No one mentioned family financial security or leaving money to heirs. I'm not saying that people are not thinking about these items, I'm sure many may be, but I do believe when we ask an employee, "What does retirement readiness look like to you and how can we help?" employees are mostly focused on an esoteric and idyllic vision of relaxing, having no worries, having fun. I'm not sure how many of these people have actually defined what those things look like, where they will occur, how they will pay for them, and what happens when they may be too old or physically challenged to live that idyllic vision.

One interesting note — several people mentioned that they trust the recordkeeper's retirement readiness

model that says 'You need this much to retire'— even though these folks admitted that they haven't used the data aggregator, or considered all of the expenses they will have in retirement, which could include funding their own medical coverage, continuing to pay a mortgage, caring for a family member, etc. It seems to me, when asked what retirement readiness means, there is no consideration for real planning, just a desire for a good life.

## How To Help

So now what? Going back to my initial challenge to define what retirement readiness means, and who should own the responsibility for aiding people in their quest for retirement, it's clear to me that there isn't one answer, nor is it a single point of responsibility. To set up our collective employees for success:

- **We need to rely on our recordkeepers to help with the tools.** Employees trust and rely on them. That means it is incumbent on us as plan sponsors to understand exactly what is and is not part of the analytics behind the results. Is there enough information around that tool to help an employee know what is and isn't included? Could the tool be more robust? Is there a way to help an employee start with one tool that leads to the next tool, and to the next to help build that fuller picture without overwhelming them?
- **Communication is key.** We need to work together with our recordkeepers to strengthen the messaging and education to help employees engage with the tools, seek advice, understand everyone's role: their role, the employer role, and the recordkeeper role. Employees need to have more understanding and input into planning for their financial success post-employment. It must be part of the culture and benefits discussions early and often.
- **Consider your plan design.** Do you encourage participants to remain in your plan post-employment? Do you offer a breadth of distribution options? Do you continue to reach out to these former employees that have a balance in your plan post-employment? Doing so can be a huge win for both you and the employee. Having more assets in your plan means lower fees and potentially more services from your recordkeeper. We allow our former employees to rollover qualified monies into our plan post-employment. This makes it simpler too for them when really considering all of their assets, getting a better picture of their retirement paycheck opportunities, and helps with managing required minimum distributions. We even allow them to take out ßa new loan and repay themselves. Why? It reduces permanent leakage and encourages them to keep building their nest egg.
- **Engaging family members.** When possible, we need to engage with and include family members in the conversation. Invite others to attend special webinars or education sessions for retirement planning. This is not a decision to make in isolation. Encouraging discussion within the family can help the employee create a better plan.
- **Provide access to resources.** Provide access to a website or even a printed brochure with helpful resources — and consider the breadth of benefits you may already offer and how those vendors can partner with you in a holistic message. For example, your employee assistance program may have some great resources for financial planning. Your legal services may be able to assist with estate planning. Your medical carrier may have information about Medicare plans and post-employment healthcare options.

What is retirement readiness to me? It depends on if I am answering that for my organization or for myself. Ironically, it is a different answer. As a plan sponsor, retirement readiness means that I understand my employee demographics and that I provide the education, tools, resources, and opportunities to pull that information together at the individual's level so that each employee can define what they need, and then help them achieve their goal. As an individual, retirement readiness to me means having a good life.

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*Beth Pattillo is the Director of Retirement and Financial Wellness Programs at Leidos.*

# In Wake of COVID-19, Retirement Savings Surge

## PSCA's *65th Annual Survey* shows record contributions in 2021.

*By Hattie Greenan*

Though we are again facing financial stressors, this time from high inflation, in 2021 organizations were recovering from the (financial) stressors of the pandemic and meeting the challenge of a worker "shortage" by increasing wages and benefits. As such, 2021 saw the highest employer contribution rate to date (5.6 percent of pay), and employers were enhancing their retirement benefits with features such as investment advice, financial literacy education, and financial wellness programs. These factors will all contribute to help buffer accounts, and the system, from the impact of current economic conditions in the long run.

Participant and employer contribution rates were at all-time highs — and nearing that 15 percent of pay many experts state as a goal — with a combined savings rate of 13.9 percent of pay. Not only did most employers make planned contributions in 2021, 13 percent increased profit sharing contributions, and 5 percent increased the match. Nearly 90 percent of eligible participants made plan contributions, and at high rates, and the use of plan loans and hardship withdrawals dropped.

Plan sponsors are continuing to add plan design features to boost both worker retention and savings rates including moving towards immediate vesting (10-point jump in three years), adding investment advice (a nearly 12-point jump from 2020), adding Roth as an option (a slight increase in 2021 after a 10-point jump in 2020), and auto-enrolling participants at the maximum match rate.

Employers are also moving to increase supports for participants with education and financial wellness tools. The primary goal of participant education has historically been to increase participation rates but that shifted to increasing financial literacy of employees in 2020, and that shift held for 2021 with 77.4 percent of organizations stating that as their primary educational goal. The secondary goal was increasing appreciation for the plan (likely as a retention method) followed by providing retirement planning to employees. The percent of organizations offering financial wellness programs increased to 27.0 percent, including more than half of large employers.

The 401(k) was built to be flexible, customizable to employee demographics and needs, and this flexibility has allowed it to change and adapt over time, and through economic downturns, coming out stronger for the lessons learned. The very quick bounce back from the COVID-19 pandemic impact, and the dramatic recovery and growth after other recessions, gives us every reason to believe that any impacts to the retirement system as a whole will be short-lived, and because of the lessons learned and the preemptive movement of companies to help support participants through enhanced education, the impact to employees' retirement readiness and long-term financial security will (likely) be minimal.

Other data highlights include:

- **Participation:** Participant contributions and their deferral rates are at record highs — 89.2 percent of eligible employees made contributions to the plan in 2021 (up from 88.5 percent in 2020) with an average deferral rate of 8.3 percent of pay (up from 8.0 percent in 2020).
- **Roth:** Roth availability continues to climb and is now an option in 87.8 percent of plans. Additionally, the percentage of participants making Roth contributions increased to 27.7 percent. The recent legislative changes in SECURE 2.0 requiring Roth treatment of catchup contributions, may push the adoption of Roth even higher.
- **Distributions:** Just 1.9 percent of participants took a hardship withdrawal in 2021 (down from 2.6 percent in 2020 and 18 percent borrowing against their account balances (down from 23.6 percent in 2020).
- **Vesting:** The use of immediate vesting increased from 41.0 percent in 2020 to 44.0 percent of pay in 2021.

**Exhibit 1: Percentage of Employees Eligible To Participate in the Plan Over Time**

| | Year | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
| Percentage of Employees | 89.8% | 89.4% | 90.9% | 89.4% | 90.1% | 90.2% | 90.7% | 88.4% | 92.7% | 92.1% |

**Exhibit 2: ADP Test Results Over Time**

| | Year | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
| Higher Paid | 6.6% | 6.6% | 6.9% | 7.0% | 7.0% | 7.1% | 6.8% | 7.3% | 7.1% | 7.2% |
| Lower-Paid | 5.2% | 5.3% | 5.8% | 5.5% | 6.1% | 6.0% | 6.3% | 6.7% | 6.7% | 6.8% |

**Exhibit 3: Availability of Roth Over Time**

| | Year | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
| Percentage of Plans | 53.8% | 58.2% | 62.0% | 59.9% | 63.1% | 69.6% | 69.1% | 75.1% | 86.3% | 87.8% |

- **Managed Accounts:** Nearly half of plans offer managed accounts (48.8 percent), up from 43.6 percent in 2020.
- **Investment Advice:** Nearly 45 percent offer investment advice, up from 32.3 percent last year.

A summary of the detailed survey findings follows:

## Employee Eligibility

Ninety-two percent of U.S. employees at respondent companies are eligible to participate in their employer's DC plan. *(See Exhibit 1.)* Nearly all plans permit full-time salaried and full-time hourly employees to participate in the plan. The percentage of plans allowing part-time employees to participate continues to climb, continuing to show the impact of 2019's SECURE Act eligibility rules for permanent part-time employees. Nearly eighty percent of plans now allow salaried part-time employees to participate, up from 73.6 percent in 2020 and 69.1 percent in 2019. Nearly three-fourths of plans allow hourly part-time employees to participate, up from 69.4 percent in 2020 and 63.7 percent in 2019.

## Participation

2021 was another record year for participant contributions. More than 90 percent of employees eligible to participate in their employer's plan have an account balance. An average of 89.2 percent of eligible employees made contributions to the plan in 2021 — the highest recorded in the history of this survey. The average percentage of salary deferred (pre- and after-tax) for all eligible participants in this survey was 8.3 percent.

Non-highly compensated participants (as defined by the Average Deferral Percentage (ADP) tests) contributed an average of 6.8 percent of pay, while higher-paid participants contributed an average of 7.2 percent of pay. *(See Exhibit 2.)*

## Roth 401(k)

The percentage of plans offering Roth 401(k) contributions continues to increase — they are now allowed in 87.8 percent of plans, including in more than 93.4 percent of large plans. Nearly 60 percent of plans that allow Roth contributions also allow for in-plan Roth conversions. The percentage of participants making Roth contributions increased in 2021 to 27.7 percent. *(See Exhibit 3.)*

## Rollovers

Nearly all plans allow rollovers into the plan from other 401(k) plans, 43.8 percent allow rollovers from 457 plans, 55.4 percent allow rollovers from 403(b) plans, and 64.6 percent allow rollovers from IRAs. A third of plans allow rollovers prior to plan eligibility, though the majority require participants to wait to roll assets into the plan until they are eligible to make elective deferrals. Forty-five percent of plans actively

**Exhibit 4: Company Contributions as a Percentage of Payroll Over Time**

| | Year | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Plan Type** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **2018** | **2019** | **2020** | **2021** |
| 401(k) Plans | 2.7% | 2.9% | 3.2% | 3.8% | 4.6% | 4.3% | 5.1% | 5.2% | 4.0% | 4.4% |
| Combination Plans | 5.4% | 5.6% | 5.5% | 5.4% | 4.8% | 5.7% | 5.2% | 5.3% | 5.4% | 6.4% |
| All Plans | 4.5% | 4.7% | 4.7% | 4.7% | 4.8% | 5.1% | 5.2% | 5.3% | 4.9% | 5.6% |

**Exhibit 5: Percentage of Plans With Immediate Vesting Over Time**

| | Year | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Contribution Type** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **2018** | **2019** | **2020** | **2021** |
| Matching Contributions | 40.6% | 37.5% | 41.8% | 38.9% | 41.2% | 38.5% | 34.0% | 38.1% | 41.0% | 44.2% |
| Non-Matching Contributions | 25.6% | 29.7% | 26.6% | 31.2% | 32.1% | 31.7% | 26.6% | 31.3% | 30.7% | 30.3% |

**Exhibit 6: Availability and Usage of Target-Date Funds Over Time**

| | Year | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Target-Date Fund** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **2018** | **2019** | **2020** | **2021** |
| Availability | 64.5% | 66.6% | 69.9% | 63.2% | 73.1% | 70.6% | 68.6% | 80.4% | 82.9% | 82.3% |
| Average Allocation | 13.4% | 16.7% | 15.8% | 19.8% | 22.2% | 22.1% | 20.7% | 23.7% | 23.9% | 28.1% |

encourage participants to roll assets into the plan.

## Company Contributions

After dipping in 2020 due to the financial impact of the pandemic, the average company contribution was at a record high in 2021 of 5.6 percent of gross annual payroll. *(See Exhibit 4.)*

A quarter of respondents contributed less than three percent of pay in 2021, down from a third of plans the year before, while 12.3 percent contributed 10 percent of pay or more, up from 9.6 percent.

## Vesting

The trend towards immediate vesting for matching contributions continues, with a ten-point jump in just three years to 44.2 percent of plans. Thirty percent of plans provide immediate vesting for non-matching contributions. *(See Exhibit 5.)*

## Investments

After an increase in 2020 in the average number of funds offered for the first time in more than a decade, the average number held steady at 21 funds. Assets are most frequently invested in target-date funds (28.1percent), actively managed domestic equity funds (20.1 percent of assets), indexed domestic equity funds (19.5 percent), and stable value funds (9.0 percent).

Eighty-three percent of plans offer target-date funds with an average of 28.1 percent of plan assets invested in them, up from 23.9 percent of assets in 2020. *(See Exhibit 6.)* Most companies offering target-date funds use a packaged product (88.1 percent), rely upon funds with a "though retirement" glide path (56.5 percent), and are actively managed (51.1 percent).

Nearly half of plans offer a professionally managed account alternative to participants (48.8 percent), up from 43.6 percent in 2020. Fewer than 10 percent of plans offer an in-plan annuity option to participants. Nearly all plans use a Qualified Default Investment Alternative (QDIA) (83.8 percent) — and for 87.3 percent of those plans, the QDIA is a target-date fund.

## Investment Advice

Investment advice is offered by 44.2 percent of respondent companies — a more than 10 point jump from 32.3 percent in 2020. Though investment advice is provided via a variety of mediums, there was an increase in one-on-one advice with a professional, and a third-party web-based provider use. The most common delivery methods for advice are one-on-one counseling (77.7 percent), Internet providers (49.0 percent), and telephone hotlines (55.4percent).

## Automatic Features

Nearly 60 percent of plans have an automatic enrollment feature. Nearly thirty percent of plans use a default deferral rate of six percent of pay (28.2 percent) while a similar percentage use three percent of pay (31.1 percent of plans). Sixty-three percent of plans use a default rate more than three percent of pay. Sixty-five percent of plans set the default deferral rate high enough so that participants receive the maximum possible company matching contribution, up from 57.1 percent in 2020.

More than three-fourth of plans with automatic enrollment also facilitate increasing those deferral rates over time. More than 40 percent automatically increase the default deferral rate for all participants, while 11.3 percent escalate it for under-contributing participants only. The cap on auto-escalation is increasing, likely due to the QDIA provision in the SECURE Act increasing the cap from 10 percent to 15 percent — 37.3 percent now have a cap greater than ten percent.

## Plan Loans

Most plans (83.6 percent) permit participants to borrow against their plan accounts. For those that do, most permit participants to have only one loan outstanding at a time (59.1 percent), while 34.8 percent permit two loans. The percentage of participants with a loan outstanding dropped from 23.6 percent in 2020 to 18.0 percent in 2021. The average loan balance is $10,854, and 2.8 percent of total plan assets is currently loaned to participants. *(See Exhibit 7.)*

## Distributions and Withdrawals

Ninety percent of plans permit hardship withdrawals. Hardship withdrawals were taken by an average of 1.9 percent of participants in 2021. In-service distributions other than hardship withdrawals are permitted in 70.9 percent of plans.

## Participant Education and Communication

The most common reasons for providing plan education are to increase employees' overall financial literacy (77.4 percent), increase appreciation for the plan (73.5 percent), increase participation (70.7 percent), and to increase deferrals (67.6 percent).

Twenty-seven percent of respondent organizations offer a comprehensive financial wellness program to employees, including 55.4 percent of large organizations. Of those that do, most address budgeting and debt management.

## Plan Changes

More than 70 percent of organizations made changes to the plan in 2021 — 53.3 percent made minor changes to the investment lineup (up from 43.8 percent in 2020), 9.0 percent changed providers or advisors, and 10.6 percent made other plan design changes. Though only 5.8 percent of organizations made changes to employer contribution formulas in 2021, 6.9 percent planned changes in 2022, including 13.7 percent of large plans.

The *65th Annual Survey* is available for purchase online at psca.org/research/401k/65thAR

*Hattie Greenan is the Director of Research and Communications for PSCA.*

**Exhibit 7: Plan Loan Usage Over Time, for Plans Permitting Loans**

| | Year | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
| Percentage of Participants With Loans | 24.0% | 26.2% | 14.6% | 25.0% | 25.8% | 30.6% | 23.2% | 20.9% | 23.6% | 18.0% |
| Average Loan Amount Per Borrower | $9,503 | $10,385 | $6,216 | $9,390 | $8,042 | $9,330 | $10,642 | $10,972 | $10,589 | $10,854 |
| Percentage of Plan Assets Loaned | 2.2% | 1.8% | 0.7% | 1.6% | 0.8% | 1.2% | 1.8% | 1.4% | 1.0% | 2.8% |

# Washington Watch

## The DOL's New ESG Rule

### The new rule walks back previous restrictions on ESG funds.

*By Andy Remo*

On November 22, 2022, the Department of Labor (DOL) issued its final rule on Prudence and Loyalty in Selecting Plan Amendments and Exercising Shareholder Rights. This rule is the latest DOL product in a long history of prior non-regulatory (and then eventually regulatory) guidance on how the core principles of the Employee Retirement Income Security Act's (ERISA) fiduciary duties of prudence and loyalty apply to considering environmental, social, and governance (ESG) factors in plan investments.

These issues stayed mostly under the radar for decades until the last year of the Trump Administration in 2020. Then, the Department of Labor issued a final rule that amended ERISA's "Investment Duties" regulation to require ERISA plan fiduciaries to select investments based solely on consideration of "pecuniary factors."

In March 2021, the American Retirement Association wrote to the then newly confirmed Biden Administration Labor Secretary Marty Walsh to express deep concern that the 2020 rule will restrict investments with ESG objectives that will curtail, if not eliminate, important investment options for retirement plan participants. Specifically, ARA asked DOL to change the 2020 rule to allow ESG investments to be permitted as qualified default investment alternatives (QDIAs) and to establish a clear policy that ESG investments should not be discouraged or treated differently than other retirement plan investment options. The ARA also advocated that DOL adopt an approach that reflects ERISA's longstanding principle of neutrality in the application of the prudence and loyalty duties regarding the factors for a fiduciary investment analysis.

Fortunately, the DOL adopted our policy positions in the latest rule.

1. The final rule retains the core principle that the duties of prudence and loyalty require ERISA plan fiduciaries to focus on relevant risk-return factors and not subordinate the interests of participants and beneficiaries (such as by sacrificing investment returns or taking on additional investment risk) to objectives unrelated to the provision of benefits under the plan.
2. The final rule makes it clear that ESG factors do not have to be considered for every plan investment but rather that they may be considered if the plan fiduciary determines them to be relevant as part of a principles-based fiduciary analysis.
3. The final rule removes the special rules for QDIAs that applied under the 2020 rule. Under the final rule, standards applied to QDIAs are no different from those applied to other investments.

### Participant Preferences

One innovative aspect of the new rule is a provision that adds new regulatory language about investment alternatives in participant-directed individual account plans — like 401(k) plans. The provision clarifies that fiduciaries do not violate their duty of loyalty solely because they take participants' non-financial preferences into account when constructing a menu of prudent investment options for participant-directed individual account plans.

In practice, this provision opens the door to ESG-type options to be added to retirement plan investment menus, provided a prudent process is followed. The determination of these additional options should be based on some reasonable assessment of participant preferences like 1) an investment committee consisting of employee representatives and/or (2) a poll of participants. Also, a prudence assessment should be based on a comparison of "like-to-like" investment alternatives. For example, a large cap "green fund" should be benchmarked against other large cap "green funds." The financial services industry will need to develop benchmarking tools to facilitate.

*Andy Remo is Director of Legislative Affairs for the American Retirement Association.*

# New Members

## Corporate Members

**Anti-Defamation League**
*New York, NY*
*Industry: Non-Profit Organization*
*Contact: Amy Lieberman*

**Jackson Lewis P.C.**
*Greenville, SC*
*Industry: Legal Services*
*Contact: Suzanne Odom*

**M Financial**
*Charlotte, NC*
*Industry: Insurance Services*
*Contact: John Boulware*

**National Technology & Engineering Solutions of Sandia**
*Albuquerque, NM*
*Industry: Government Contractor*
*Contact: Nancy Muller*

## Certified Plan Sponsor Professionals

**Guiselle Albritton**
*Dalcor Management Company*

**Elena Bahn**
*Thermolift*

**Virginia Blair**
*Blair and Company*

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*Paul Hemmer Company*

**Katie Broderick**
*O.C. Tanner*

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*Redlands Community Hospital*

**Gayle Cipriani**
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**Anna Cruz-Morales**
*Carabotta Steakley PLLC*

**Marilea De Faria**
*Hunter Industries*

**Kathy de la Garza**
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**Theresa Eckenrode**
*Digging & Rigging, Inc.*

**Alora Edwards**
*B Capital Group*

**Jim Gellatly**
*Carolina Rehabilitation and Surgical Assoc.*

**Holly Grant**
*Kennedy-Donovan Center*

**Regina Grillo**
*Incyte*

**Lily Harada**
*Smart & Final*

**Tineka Hardwrick**
*Summit Vista Employee Co., LLC*

**Shelby Hayes**
*West Central Inc*

**Jason Herndon**
*CBL & Associates Management, Inc.*

**Jana Hottel**
*Woodgrain Inc*

**Cara Hutchison**
*Aludyne*

**Alexis Jones**
*Rental One*

**Jazzlynn Kusch**
*Clear Guidance Partners*

**Laurie Langella**
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**Jessica Leatherman**
*Alderfer Glass Co*

**Deborah Manning**
*Glatfelter Insurance Group*

**Heather Mathews**
*Waddell Serafino*

**Cassandra McIntyre**
*Science Systems and Applications, Inc.*

**Gary Moak**
*Magnolia Electric Power*

**Karen Piper**
*Tipping Point Solutions Inc.*

**Rachina Randolph**
*Quantum Water & Environment*

**Shalie Reich**
*Destinations, Inc.*

**Melissa Romig**
*Baywa R.E. Solar Projects*

**Heather Rowbury**
*Citidev*

**Lynn Sacia**
*Nesnah Ventures*

**Christopher Sietins**
*Solidifi Title & Closing, LLC*

**Mike Smallwood II**
*The Gateway Company of Missouri, LLC*

**Shawnie Smith**
*Merritt Aluminum Products*

**Jecobi Swafford**
*Signal Energy Constructors*

**Rhonda Thomas**
*Neat Companies*

**Chad Trochlil**
*Bremer Bank, National Association*

**Tanya Ulrich**
*Presbyterian SeniorCare Network*

**Melissa Van Brunt**
*Resolution Economics, LLC*

**Lisa Winters**
*McNair, McLemore, Middlebrooks & Co., LLC*

Changes in member contacts should be sent to psca@psca.org.

PSCA
Plan Sponsor Council of America

# Upcoming Dates & Events

### PSCA's 2023 National Conference

May 3–5, 2022
Marriott Orlando World Center, Orlando, FL
www.pscanational.org/

### 2023 Virtual Plan Sponsor Roundtables

February 15, 2023, 4:00–5:00 p.m. ET
June 20, 2023, 4:00–5:00 p.m. ET
August 16, 2023, 4:00–5:00 p.m. ET
November 8, 2023, 4:00–5:00 p.m. ET

Register at psca.org/plan-sponsor-roundtables

## PSCA Member Benefits and Resources

**Conferences and Training**
*National and regional conferences designed for defined contribution plan administrators and sponsors.*
Our must-attend events provide education from industry leaders and peer networking.

**Signature Awards**
*Peer and industry recognition for employee communication and education.*
Recognizing outstanding defined contribution programs implemented by plan sponsors, administrators, and service providers.

**Research and Benchmarking**
*PSCA surveys: Most comprehensive and unbiased source of plan benchmarking data in the industry.*
Annual surveys of profit sharing, 401(k), 403(b), and NQDC plans, as well as HSAs, created by and for members. Current trend and other surveys available throughout the year. Free to members that participate. Surveys currently available include:

- *65th Annual Survey of Profit Sharing and 401(k) Plans*
- *2022 403(b) Plan Survey*
- *2022 NQDC Plan Survey*
- *2022 HSA Survey*

**Executive Report**
*A monthly electronic legislative newsletter.*
Providing concise, current information on Washington's most recent events and developments.

**Media Outreach**
*PSCA works to ensure fair coverage of the DC system in the media.*
PSCA continually speaks to reporters to provide and promote accurate, concise, and balanced coverage DC plans and responds to negative press with editorials and letters to the editors. PSCA is also active on social media — follow us on twitter at @psca401k and on LinkedIn.

**Washington Representation**
*Your direct connection to Washington DC events and developments affecting DC plans.*
PSCA works in Washington to advocate in the best interests of our members and bring you the latest developments that will impact your plan. PSCA is a founding board member of the Save Our Savings Coalition that is currently working in Washington to preserve plan limits amongst tax reform.

**Quarterly Magazine, *Defined Contribution Insights***
*An award-winning and essential 401(k) and profit sharing plan resource.*
Featuring nationally-respected columnists, case studies, the latest research, and more. Providing practical and constructive solutions for sponsors.

**Professional Growth — Join a Committee!**
*For plan sponsors, administrators, and service providers.*
Many opportunities for PSCA members to serve on committees, speak at regional and national conferences, and write articles for *Defined Contribution Insights*.