Retirement Report

News and updates for Plan Sponsors and Fiduciaries of Defined Contribution Plans

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2008 Year End Market Review: One for the History Books

While the fourth quarter finished with some positive momentum across most equity categories, it was not enough to erase the damage sustained in October and early November. The fourth quarter ended down double digits for most equity markets, guaranteeing double digits losses for the year in most major market categories. The U.S. equity market finished the year off 37.3% (Russell 3000), capping off one of the largest drops in stock market history. International equity markets faired much worse, off 43.1% (MSCI EAFE) for the year. On the flip side, investment grade bonds experienced tremendous demand, propelling U.S. fixed Income markets higher in the quarter and helping them cap off the year as the best performing asset class. The U.S. fixed income market finished up 5.2% for 2008 (Barclays Capital Aggregate Bond Index). Below investment grade (high yield) bonds, however, produced returns more akin to the equity markets, posting negative double digit returns for both the quarter and the year. While diversification provided little to no protection in 2008 against negative return scenarios, it did help limit losses that could have otherwise been catastrophic. In some cases, certain asset classes posted negative returns as high as 50% (for the year).

Amid worsening economic conditions, there was some good news over the fourth quarter. Several indicators were showing that credit markets, once frozen, were beginning to thaw and operate more normally again. Equity market volatility, which had been at all time highs earlier in the quarter, began to fall, most notably in December. Equity market valuations appeared to be at levels that investors found attractive near the end of the quarter, as equities began to recover, posting positive, albeit small returns. Also notable was the Fed lowering interest rates to the range of 0 - 0.25%, which was just one of many unprecedented steps taken over the quarter by the Government to restore stability to the economy. All of these new developments are encouraging. As with any new year, 2009 brings hope that the markets and economy will recover, which, of course, they always do, in their own due course.

Litigation Update: Prudent Process Leads to Fiduciary Victories

As the 2008 calendar year wound to a close a couple of high profile excessive fee lawsuits reached their respective conclusion. The courts in both cases, *Kanawi v. Bechtel Corp.* (*Bechtel*) and *Braden v. Wal-Mart Stores, Inc.* (*Wal-Mart*), ruled in favor of plan fiduciaries.

In the *Bechtel* decision the court focused on whether plan fiduciaries met their duty of loyalty pursuant to ERISA Section 404(a) in their selection of mutual funds and payment of fund management fees. The court ruled that the plantiffs failed to prove that payment of the fees were imprudent. The court's decision was largely based on the fact that the committee met regularly to review plan investment performance and utilized the advice of third party consultants. Ultimately the court bolstered the standard of prudence being one of conduct rather than performance.

Similarly, the court in the *Wal-Mart* case concluded that plaintiff failed to prove that the plan fiduciaries breached their responsibilities resulting in $60 million in unnecessary expenses. The judge characterized the plaintiff's case as "conclusory allegations, without any factual support." The major thrusts of the plaintiff's case were that the majority of the funds available in the plan charged 12b-1 fees and that most of the funds were actively managed (verses index funds). The court based almost all of it's rulings on the plaintiff's failure to provide any evidence of fiduciaries' failure to conduct prudent investment research, fiduciaries' failure to meet regularly, or that fees were unreasonable. In the end the court reasoned that the mere existence of less expensive investment options alone, is insufficient evidence of fiduciary failure.

If you have any questions regarding either court's decision or their impact on your fiduciaries please contact your plan consultant for help or email Jennifer Eggers at jeggers@twgservices.com.

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DOL Finalizes Investment Advice Rule

The DOL said in a release that the rule will make investment advice more accessible for participants in 401(k) plans and individual retirement accounts (IRAs). The rule includes a regulation that implements the new statutory exemption for investment advice added to the Employee Retirement Income Security Act (ERISA) by the Pension Protection Act (PPA) and a related class exemption. The final rule provides general guidance on the exemption's requirements, including computer model certification and disclosures by fiduciaries. The regulation also includes a model form to assist advisers in satisfying the exemption's fee disclosure requirement, and a class exemption expanding the availability of investment advice. "Now more than ever, workers need independent, personally tailored investment advice to help them navigate the turbulent markets and safeguard their financial futures … These new regulations make our bipartisan promise of high-quality investment advice a reality," said House Republican Leader John Boehner (R-Ohio) in a statement.

Plan Reminders for the New Year

As we launch into a new year, it's an excellent time to check in with your 401(k) and payroll administration to make sure your participant deferrals are kept in line with the new cost of living adjustments and applicable plan limitations. For 401(k), 403(b), and 457(b) plans in 2009, participants can make elective deferrals ups to $16,500 and participants age 50 or older can defer an additional $5,500. Additional catch-ups are available under some 403(b) programs and section 457 plans. Does your payroll system automatically stop deferrals in excess of these amounts? Don't forget to verify if your plan allows for employer match on catch up contributions and make sure your payroll is set up accordingly. The new annual compensation limit is $245,000 which eliminates any employer match above this limit. For example, if your plan provides for a 3% employer match, the maximum total annual match cannot be in excess of $7,350 ($245,000 x 3% = $7,350). In this example, even if an employee was paid $400,000 in 2009, their match would be limited to $7,350. In general, employer contributions, employee post-tax and pre-tax contributions, and reallocated forfeitures (if any) to a participant during the 2009 limitation year (collectively referred to as "annual additions") are limited to the lesser of $49,000 or 100% of the participant's compensation. Please don't hesitate to call us at 1-800-322-9773 or email Jennifer Eggers at jeggers@twgservices.com with your questions or concerns.

Survey Says: Are Target Date Asset Allocation Funds Helping Participants?

Several recent studies have shown that Target Date funds helped participants achieve greater returns compared to participants who are attempting to select an investment portfolio on their own. The main reason for this result is that a professional money manager is ensuring the common mistakes chronically made by the typical investor are being eliminated. These common mistakes include: not asset allocating/diversifying effectively, not rebalancing their portfolio regularly, and not selecting funds based on quantitative criteria. The Vanguard Center for Retirement Research adds some detail to these prior conclusions by focusing on the single most important investment factor: asset allocation/diversification. Here they indicate that "participants who do not invest in target date funds tend to exhibit greater extremes in their equity holdings." The study also pointed out those non-target-date investors' allocations to stocks declined less than 10% between ages 25 and 65, while target-date investors' equity allocations declined more than 40% over the same age range, which seems much more prudent. The study goes on to conclude that "target-date funds help participants adhere to the principals of prudent investing … (they are) ... broadly diversified and reduce equity exposure over time in order to mitigate the risks associated with equity markets." It is anticipated that the benefits of these target-date funds, such as diversification and rebalancing, will be magnified for many equity investors during this period of market turmoil.

Communication Corner: Highly Compensated Employee Refund Notice

This month's sample participant communication memo is intended for the highly compensated employees (HCEs) in your plan who may be subject to a refund in 2009 due to failed ADP or ACP tests. Email Jennifer Eggers at jeggers@twgservices.com for copy that you can print and distribute to employees.

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