

# Retirement Report

*News and Updates for Plan Sponsors and Fiduciaries of Defined Contribution Plans*

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## **The DC Plan Challenge: Better Returns**

As the retirement industry shifts from defined benefit (DB) plans in favor of defined contribution (DC) plans, the burden of asset management falls to the plan participant. DB plans have typically hired and relied on outside expertise to help allocate and manage the plan's assets, which has subsequently led to better plan returns for DB plans as compared to their DC plan counterparts.

According to a recent study conducted by Watson Wyatt, DB plans experienced a 14% improved cumulative performance over DC plans for each dollar invested over the period between 1995-2006 (DB beats DC in returns and security, 6/19/08, [globalpensions.com](http://globalpensions.com)). Even in bull markets, the study found DB plans had higher returns of approximately 1% each year (from 2003-2006). Jeffrey Elvander, Chief Investment Officer, 401(k) Advisors commented: "While the study may be general in its scope and conclusions, the results highlight the challenge confronting DC plan participants, many with little to no expertise in managing diversified portfolios, in their efforts to maximize returns and assets for retirement."

Recently, the retirement plan industry has experienced an influx of more investment products that help address a DC plan participant's need for an overall portfolio solution. These portfolios are typically referred to as "age-based" or "risk-based" funds. Recent legislation has helped endorse these investments as the default option within a DC plan. Elvander commented: "The greater selection and higher caliber investment solutions in the managed portfolio space should help decrease the performance gap between DB and DC plans, however, this will be dependent on acceptance and utilization by plan participants. While the Pension Protection Act goes a long way in helping to close this gap, only in combination of extensive education or investment advice and total portfolio solutions and investment offerings will the DB/DC gap be a thing of the past."

For more information on this topic, please contact your plan consultant or email [bwright@twgservices.com](mailto:bwright@twgservices.com).

## **Extended Deadline for Correcting ADP and ACP Test Excesses**

Each year, EACA (Eligible Automatic Contribution Arrangement) plans are required to complete non-discrimination testing, where the average contributions of highly compensated employees are compared to the average contributions for non-highly compensated employees. The IRS only allows highly compensated employees to contribute a minimal amount above what the non-highly compensated employees have contributed. If the tests fail, highly compensated employees may receive a taxable refund back from their account.

Effective for 401(k) plan years beginning after December 31, 2007, a later deadline for making corrective distributions (refunds) of excess contributions from failed ADP Tests (employee contributions) and excess aggregate contributions from failed ACP Tests (employer matching) applies. Plan sponsors will not have to pay the 10% excise tax on these excesses if the plan makes the corrective distributions by the last day of the sixth month following the end of the plan year (June 30 for most plans). In addition, excess amounts and related earnings paid out within this six month period will be taxable in the year distributed, regardless of the amount distributed.

Please note that the new six month deadline is only available to plans using EACA – plans applying the auto enroll feature to all participants, newly eligible and current participants, at any rate of pay, have a QDIA as the default investment for "auto-enrolled" monies, have the 90 day opt distribution feature, and meet the annual notice requirements. For more information, please contact your plan consultant or email [bwright@twgservices.com](mailto:bwright@twgservices.com).

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## IRS & DOL Updates (Part I)

From May 8-10 in Washington, DC, both IRS and Department of Labor (DOL) representatives attended and spoke at the American Bar Association's Tax Section May Meeting. Although all representatives carefully couched their thoughts as their own, and not as official representations of their respective regulatory agencies, their words provide both practitioners and plan sponsors with insight into opinions regarding multiple issues. The following are a few of the topics covered:

- Plan audits – all opened for a reason (DOL)
- 75% of 3000+ cases opened had monetary results and 188 criminal cases resulted in 115 indictments (DOL)
- Use of rollovers for start-up businesses was a target for investigation (DOL)
- "Compliance checks" will be conducted by the Employee Plans Compliance Unit are not technically audits, but may grow into some (IRS)
- Reasonable contracts (as dictated by pending regulations for ERISA section 408(b)) are a present focus of the DOL
- An "abandoned plan program" for assets held by a custodian with no direction from participants or trustees in regards to investment is provided (DOL)
- Untimely remittance of contributions still a focus of investigation (DOL)
- 403(b) favorable determination letter process currently being designed (IRS)

If you have any interest in any topics listed above, or would like to learn more how the IRS/DOL's opinions may impact your plan please contact your plan consultant or email [bwright@twgservices.com](mailto:bwright@twgservices.com). Part II of this article will be published in our July edition.

## Advantages of Investing in Turbulent Markets

Are your participants contacting you about the drops in account value? Are they asking to stop contributing to the plan altogether? Our consulting practice receives calls every week from worried participants concerned about the declining value of their accounts. These conversations revolve around the merits of investing in different types of funds offered in their retirement plan. We also discuss the dynamics of investing in these turbulent markets, in many cases introducing the concept of Dollar Cost Averaging.

It is encouraging to invest in a 401(k) when the economy is strong and funds are growing; there is often a sense from participants they want to join the ride. On the other hand, it is during the times when the markets drop that can really be of value to participants building for a future retirement. When the markets are down, so are the prices of many mutual funds. If participants continue deferring the same amount into the 401(k) the money often purchases more shares of a fund than it could have when the prices are climbing. This goes back to the basic goal of investing, "buy low and sell high."

Remember if you plan on investing \$5,000 into your 401(k) plan in 2008, you might ask yourself when would be the best time to do so? The answer is nobody really knows for sure. Overtime, by spreading out purchases, and taking advantage of markets like today, this allows you to purchase more shares when the prices are lower and fewer when the prices are higher. In effect your investment dollar goes further during these times. If you have questions on this topic, please contact your plan consultant or email [bwright@twgservices.com](mailto:bwright@twgservices.com).

## Communication Corner: Dollar Cost Averaging

This month's sample participant memo introduces the concept of Dollar Cost Averaging. Now is a great time to remind your participants to "stay the course" during down markets! Email [bwright@twgservices.com](mailto:bwright@twgservices.com) for assistance.

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