# ERISA-Extra®

**In this issue**



## Consistency counts

If your company sponsors a 401(k) retirement savings plan, you probably make a concerted effort to get your employees into the plan. But once they've enrolled, do employees contribute regularly and invest appropriately? A recent study from the Employee Benefit Research Institute (EBRI) and the Investment Company Institute (ICI) highlights just how important consistency can be when saving and investing for retirement.[1]

The study tracked the accounts of 6.1 million individuals who consistently participated in their employers' 401(k) plans for a six-year period, from 2010 through 2016. The group was a subset of the larger EBRI/ICI database of 27.1 million participant accounts. Following are some of the study's key findings.

**Account growth**

As noted in the study, three factors affect the change in a participant's account balance:

- New contributions made by the participant, the employer, or both
- Total investment return on the account balance, which is a function of the account's asset allocation and financial market performance
- Any withdrawals, borrowing, and loan repayments

The *average* account balance of the consistent participants more than doubled during the period studied, rising from $75,378 at year-end 2010 to $167,330 at year-end 2016. This represents a compound annual average growth rate of 14.2% over the six-year period. The consistent participants' average account balance was more than two times larger than the average balance of the larger participant group.

**Average 401(k) account balance 2016—Consistent participants**

| Age group* | 2010 | 2016 |
|---|---|---|
| 20s | $3,998 | $34,956 |
| 30s | $21,804 | $77,927 |
| 40s | $57,117 | $146,624 |
| 50s | $99,388 | $217,447 |
| 60s | $117,139 | $204,783 |
| All | $75,378 | $167,330 |

* Based on participant age at year-end 2016.

Similarly, the *median* account balance among consistent participants more than doubled during the six-year period, from $30,114 to $82,338 by the end of 2016 (a compound annual average growth rate of 18.3%). This median balance was almost five times the $16,836 median balance for participants in the entire database.

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**Average asset allocation**
Although many participants held a range of investments, their account balances tended to be weighted toward equities, through investments in equity funds, the equity portion of target-date and balanced funds, or company stock. At year-end 2016, equities represented approximately two-thirds of the account assets for both the consistent participant group and participants in the larger database, with younger participants tending to hold higher concentrations of equity investments than older participants.

**Average asset allocation 2016—Consistent participants**

| | |
|---|---|
| Equity Funds | 46.3% |
| Target-date Funds | 17.5% |
| Non-target-date Balanced Funds | 5.1% |
| Bond Funds | 8.4% |
| Money Funds | 2.7% |
| GICs/Other Stable Value Funds | 6.3% |
| Company Stock | 7.1% |
| Other | 5.6% |
| Unknown | 0.9% |

The researchers observed that the general rise in the stock market over the six-year period tended to boost the account balances of participants who held equities in their accounts.

## Know your fiduciary responsibilities

As a plan sponsor, you want your retirement plan to serve as a competitive employee benefit—one that assists the company in recruiting and retaining the workers needed to help drive business success and helps them accumulate the savings they'll need for the future. But as worthwhile as offering a workplace retirement plan can be, it also involves specific fiduciary responsibilities that are important for employers to understand.

**Identifying plan fiduciaries**
A plan's fiduciaries are the individuals (and entities) who exercise discretion or control over the plan. The list of fiduciaries typically includes the plan's trustee and investment advisors, any other individuals who exercise discretion in the administration of the plan, all members of the plan's administrative committee (if there is one), and the individuals who select committee officials.[2]

Plan fiduciaries who fail to follow certain standards of conduct may be held personally liable to restore any losses to the plan, or to restore any profits made through the improper use of the plan's assets resulting from their actions.[3] The potential for personal liability makes it all the more critical for fiduciaries to be familiar with their roles and responsibilities to the plan and its participants.

**Fiduciary duties**
Federal pension law requires plan fiduciaries to fulfill their duties to the plan solely in the interest of plan participants and beneficiaries.[4] There are four primary responsibilities:

1. *Act for the exclusive purpose of providing benefits to plan participants and beneficiaries and defraying reasonable plan administrative expenses*[5]
   Plan fiduciaries must avoid acting in their own interest rather than in the best interest of the plan's participants and beneficiaries. Assets of the plan may be used to pay for plan administration, but the costs must be reasonable.

   In addition to evaluating the reasonableness of plan administrative expenses, fiduciaries should consider how the expenses are allocated. For example, it may be appropriate to pay certain expenses, such as a fee for processing a hardship withdrawal, from the account of the affected participant while allocating other expenses, such as plan auditing fees, among all participants' accounts. The plan document may describe the appropriate method for allocation.[6] Note also that certain costs related to the establishment, design, and termination of a plan—so-called "settlor" functions—may not be paid from the plan.[7]

2. *Act prudently with respect to plan assets*[8]
   This duty requires expertise in various areas, such as investments. Implicit in the prudence requirement is the need to monitor plan investment options. The ongoing investment review should generally encompass various measures, such as a comparison of recent performance data relative to an appropriate peer group and benchmark indexes and an assessment of any changes to portfolio managers, investment strategy, or fees.

   Plan sponsors who don't have the expertise necessary to carry out investment or other plan-related functions prudently can hire outside parties with professional knowledge to assist them. However, the plan sponsor remains responsible for following a prudent selection process. This generally entails vetting several potential providers, outlining specific requirements, and requesting the same information from each candidate so that a meaningful, objective comparison that considers all relevant factors can be made. The selection process, including the basis for any decisions made, should be documented and the selected provider's services should be reviewed at reasonable intervals to ensure the provider is performing the agreed-upon services.[9]

3. *Diversify the assets of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so*[10]
   Fiduciaries generally should avoid investing a disproportionately large amount of the plan's assets in a single security or single type of security, unless the investments themselves are adequately diversified (as may be the case with mutual funds, for example).[11] Similarly, a participant-directed plan should provide adequate opportunity for participants to diversify their account investments.

   Where Section 404(c) compliance is sought, the plan should have a core investment menu consisting of at least three diversified alternatives, each having different risk and return characteristics.[12] In addition, participants must be given sufficient information to make informed decisions about the plan's investment options and be allowed to give investment instructions at least once a quarter, or perhaps more frequently if the investment option is volatile.[13]

4. *Comply with the provisions of the plan*[14]
   Because the plan document serves as the foundation for plan operations, plan fiduciaries should be familiar with its terms. It's also important to review the plan document periodically and to make sure that any amendments necessary to keep it current are made in a timely manner.[15]

## When should 401(k) contributions be deposited?

Among their other fiduciary duties, 401(k) plan sponsors are responsible for ensuring that employees' plan contributions and loan repayments are deposited into the plan trust in a timely manner. The sooner funds are deposited in the plan, the earlier they can be invested on plan participants' behalf. Late deposits of salary deferral contributions must be reported on Form 5500, Annual Return/Report of Employee Benefit Plan, and are considered "prohibited transactions" that can give rise to fiduciary liability and excise taxes.

**Know the rules**
Under the applicable Department of Labor regulations, participant contributions to a 401(k) plan, as well as amounts representing repayment of participant loans, become assets of the plan as of the earliest date on which they can reasonably be segregated from the employer's general assets.[16] However, in no event may deposits be made later than the 15th business day of the month following the month in which the employer receives the amounts or withholds them from participant wages.[17]

It is important to recognize that the 15th business day represents an outside limit of the time that may be considered for segregation of the assets. If contributions and loan repayments can reasonably be segregated and deposited into the plan sooner, they must be. Many employers have payroll and accounting systems that make it possible for contributions and loan repayments to be segregated from general assets and deposited within a matter of days.

**Safe harbor for small plans**
The regulations provide a safe harbor period for employers to submit employee contributions and loan repayments to a plan that has fewer than 100 participants at the beginning of the plan year. Under this safe harbor, employers that deposit these funds within seven business days after the amounts are withheld from employees' wages or received by the employer will automatically satisfy the law's requirements. If a deposit is made later than seven days after the payroll date, it will not be considered a prohibited transaction as long as the deposit was made as soon as the contributions could reasonably be segregated from the employer's assets (and not after the 15th business day of the month following the payroll month).[18]

**Voluntary correction**
Delinquent participant contributions and participant loan repayments are on the list of transactions that may be corrected under the Department of Labor's Voluntary Fiduciary Correction Program (VFCP).[19] To use the VFCP program, an applicant must restore the plan, participants, and beneficiaries to the condition they would have been in had the breach not occurred. An application is then submitted to the Employee Benefits Security Administration demonstrating that the violation has been self-corrected in accordance with the required correction method, which includes restoring any lost earnings to the plan. Upon successful completion of the VFCP process, the Department of Labor may issue a "no-action" letter with respect to the violation.

[1] VanDerhei, Jack, Sarah Holden, Luis Alonso, and Steven Bass. "What Does Consistent Participation in 401(k) Plans Generate? Changes in 401(k) Plan Account Balances, 2010-2016." EBRI Issue Brief. No. 464. November 6, 2018. Web. Date of Access 2/18/2018. *https://www.ebri.org/docs/default-source/ebri-issue-brief/ebri_ib_464_long-k-6nov18.pdf?sfvrsn=f5773e2f_6*.
[2] U.S. Department of Labor, Employee Benefits Security Administration. "Meeting Your Fiduciary Responsibilities." September 2017. Web. Date of Access 2/18/2018. *https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/publications/meeting-your-fiduciary-responsibilities.pdf.*
[3] Ibid.
[4] ERISA Section 404(a)(1).
[5] ERISA Section 404(a)(1)(A).
[6] U.S. Department of Labor. Field Assistance Bulletin 2003-03. May 19, 2003.
[7] ERISA Opinion Letter 97-03A. 1997.
[8] ERISA Section 404(a)(1)(B).
[9] U.S. Department of Labor, Employee Benefits Security Administration. "Meeting Your Fiduciary Responsibilities." September 2017.
[10] ERISA Section 404(a)(1)(C).
[11] ERISA Opinion Letter 75-93, 11/4/1975.
[12] Labor Regulation Section 2550.404c-1(b)(3).
[13] Labor Regulation Section 2550.404c-1(b)(2).
[14] ERISA Section 404(a)(1)(D).
[15] U.S. Department of Labor, Employee Benefits Security Administration. "Meeting Your Fiduciary Responsibilities." September 2017.
[16] Labor Regulation Section 2510.3-102(a).
[17] Labor Regulation Section 2510.3-102(b)(1).
[18] Department of Labor Regulation Section 2510.3-102(a)(2).
[19] U.S. Department of Labor. Voluntary Correction Program Fact Sheet. December 2018. Web. Date of Access 2/18/2019. *https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/vfcp.pdf*.



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