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Steps to Make DC Plans Good (and Avoid Bad or Ugly Outcomes)

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Remember the 1966 spaghetti western "The Good, the Bad, and the Ugly"? The promise of a vast fortune creates a partnership between the Good (Clint Eastwood), the Bad (Lee Van Cleef), and the Ugly (Eli Wallach) before pitting them against one another in the search for the loot, with plenty of gorgeous cinematography and gun-slinging to keep viewers on the edge of their seats.

(Estimated reading time: 4 min 9 sec)

I recently wrote a white paper that riffed on that classic, and in this post I wanted to share some of the key findings from my research to help defined contribution (DC) plan sponsors take steps to stay on the good side and avoid bad or ugly outcomes.

1. **Ongoing plan maintenance**

This includes reevaluating the fund lineup, reviewing service providers, and documenting plan administrative decisions. DC plans that offer company stock, managed account options, or self-directed brokerage services have extra due diligence to conduct and document.

What to do and when: Consider including an investment structure evaluation, fee benchmarking study, vendor search, managed account service provider evaluation, or independent fiduciary engagement in your long-term fiduciary forecasting. To schedule them, plan sponsors can use a calendar-based approach or project list to ensure a consistent process. If none of these actions are needed, document why not.

2. **Effective governance steps**

The governance structure should meet the fiduciary requirements of the relevant governing law (e.g., ERISA), and address both investment and administrative duties and actions in a way that fosters prudent decision-making and effective management without being overly complex.

What to do and when: Plan sponsors should periodically review the governance model, including the roles and responsibilities of all parties.

3. **Evaluate employee demographics and participant behavior**

Sponsors should review their plan demographics to determine whether a spike in employee retirements may be pending, or if an anticipated wave of retirements has not yet occurred.

What to do and when: Consider how your retirement program supports long-term labor planning and assess options for employees approaching retirement on an annual basis.

4. **Support participants with plan decisions**

One of the biggest risks in a DC-centric retirement model is the reliance on participants to make complex financial and investment decisions. Behavioral finance has driven plan innovations that support effective participant actions—including automatic enrollment, automatic deferral rate increases, and automatic rebalancing (e.g., target date funds).

What to do and when: Plan sponsors should assess the plan design, the intent behind the design, and the actual use of different features. Plan sponsors should also evaluate the suitability of the asset classes in the plan, including the QDIA, assess any asset category overlap or gaps, and analyze actual usage. This assessment would be appropriate when demographics change (e.g., after a merger), when the employer modifies other benefits, or every five years or so.

5. **Looking beyond retirement**

Plan sponsors are increasingly linking retirement benefits with health savings accounts (HSAs), which are intended to pay for medical expenses. HSAs are not “welfare benefit plans” subject to ERISA, *contingent on the employer’s limited involvement with the HSA.* But ERISA may be triggered if an employer attempts to influence the scope of investments available to its employees by requiring an HSA trustee or custodian to offer investments that they would not typically offer to other account holders. If that happens, the employer would have to maintain a plan document and summary plan description and file a Form 5500 with the Department of Labor annually.

What to do and when: Plan sponsors may want to combine messaging about HSAs and DC plans, especially during annual enrollment when participants are most likely to be engaged in benefit planning, to highlight and reinforce positive saving behaviors in both plan types.

6. **Upgrade the tech**

Plan sponsors should consider how technology can be used to promote overall financial wellness and improved retirement outcomes.

What to do and when: Plan sponsors can work with their service providers during annual planning to target specific employee groups with relevant communications.

7. **Study for tests**

Nondiscrimination testing for plans subject to it should be completed by March 15, 2019; if the employer doesn’t distribute or recharacterize excess contributions by then (six months for plans with certain eligible automatic contribution arrangements), the employer is liable for a 10% tax on those excess contributions.

What to do and when: Work with your DC plan service provider to conduct nondiscrimination testing for 2018 and look into running a projected test for 2019 in August or September to allow sufficient time to prevent or correct failures prior to year-end.

8. **Get it in writing**

Plan Documentation: Most sponsors must maintain a document that describes the plan design and operations. Prior to the close of the plan year, sponsors should review their plan documents to make sure any amendments are reflected.

Participant Notices: Sponsors can also plan for the future year, integrating the process of drafting QDIA notices, safe harbor notices, and fee disclosure notices to manage the timing and coordination with other communications. The QDIA and safe harbor notices are tied to the end of the plan year, while the fee disclosure is not.