# The Five Pillars of a Retirement Plan

## An employee retirement plan can help:

- Recruit and retain valuable employees
- Bridge the gap between Social Security and retirement income needs, which are estimated to be 85 percent of current income[1]
- Reduce tax liability — contributions to employee accounts are tax-deductible from business income

The American workforce is aging — from 2010 to 2020, 65- to 74-year-olds will occupy the fastest-growing segment of the population, while 55- to 64-year-olds will be the largest segment of the population.[2] In light of the aging population and Congress' recent focus on the integrity of retirement plan administration, design and investment monitoring, it's more important than ever for your company to have a competitive, compliant retirement plan.

As your advisor, our goal is to provide you the tools and resources that can help you build and maintain a successful plan for your employees.

1. Aon Hewitt. "The Real Deal: 2012 Retirement Income Adequacy at Large Companies." 2012
2. U.S. Census Bureau. "Census 2010." www.census.gov.

## As a decision-maker, it's important to understand how a successful retirement plan can help benefit you and your employees.

# The Five Pillars of a Retirement Plan

There are five pillars upon which a successful retirement plan can be built:

### 1. The Plan Fiduciary
Understand the role and responsibilities of a fiduciary.

### 2. Plan Design and Compliance
Select the appropriate plan type and design for your employees and help ensure plan compliance.

### 3. Selection and Monitoring of Plan Investments
Develop an investment policy statement, select a balanced investment lineup and designate a default investment option for your plan.

### 4. Plan Participation and Education
Implement strategies that can help your employees meet their financial retirement goals.

### 5. Service, Technology and Day-to-day Administration
Select a provider whose plan administration capabilities and level of service fits best with your organizational needs.

Understanding the principles necessary for establishing and maintaining a successful retirement plan can be a daunting task for fiduciaries. That's why many plan sponsors rely on the guidance and expertise of a plan consultant.

Through process-driven, timely and comprehensive delivery of services, the plan consultant's goal is to help plan fiduciaries limit and manage personal and corporate financial liability while enhancing investment opportunities and improving overall plan value. Our comprehensive investment due diligence process, employee communication programs, plan design analysis and vendor benchmarking capabilities provide solutions that are designed to enable plan fiduciaries to meet their obligations.

# The Plan Fiduciary

Understand the role and responsibilities of a fiduciary.

## What is a fiduciary?

A fiduciary is someone who exercises discretionary authority or control over the management of a retirement plan or its assets.

*Fiduciaries are typically responsible for:*

- Making decisions regarding the selection and retention of plan fiduciaries
- Evaluating and selecting plan investment vehicles
- Providing investment advice to the plan for compensation
- Acquiring or disposing of plan assets
- Making discretionary decisions regarding the plan (for example, authorizing or disallowing benefit payments)

## What is a named fiduciary?

A “named fiduciary” is the person who is primarily responsible for the overall operations and administration of a company’s retirement plan. Usually the plan sponsor, plan administrator, trustee, plan committee or administrative committee serves as the named fiduciary.

*Named fiduciaries are typically responsible for:*

- Selecting an investment provider and investment options
- Keeping a due diligence file for fiduciary decisions
- Appointing other plan fiduciaries as needed
- Evaluating plan needs
- Maintaining an investment policy statement
- Researching and selecting an investment provider
- Finalizing plan features, including investment options and services
- Communicating information about the plan to employees
- Monitoring investment options and plan operations

# Plan Design and Compliance

## Select the appropriate plan type and design for your employees and help ensure plan compliance.

## Plan Types

Your company has individual needs and your retirement plan must be responsive to them. Key issues, such as cash flow and organizational structure and size, factor into the type of plan design you select.

| The most common plan types are: | |
|---|---|
| **401(k)** | A defined contribution plan that allows an employee to save for retirement while deferring income taxes on the saved money and earnings until withdrawal. The employee elects to have a portion of his or her wages paid directly (or "deferred") into their 401(k) account. |
| **Roth 401(k)** | Like a traditional 401(k), except payroll deferrals are taxed in the year that they are earned instead of when they are distributed. Neither principal nor earnings are taxed, when taken as part of a qualified distribution. |
| **Profit-sharing Plan** | A defined contribution plan that permits the employer to make discretionary, tax-deferred contributions on behalf of employees, based on a pre-determined formula. These plans are often used in conjunction with 401(k) plans. |
| **403(b)** | A tax-advantaged retirement savings plan available for certain schools, hospitals, nonprofit employers and self-employed ministers. The deferred taxation of contributions and earnings is similar to that of a 401(k) plan. |
| **Defined Benefit** | A traditional pension plan that defines the benefit amount that an employee will receive upon retirement. |
| **Simplified Employee Pension (SEP) IRA** | A retirement program that permits an employer to make discretionary, tax-deductible contributions to Individual Retirement Accounts (IRAs) established by eligible employees. |
| **Savings Incentive Match Plan for Employees (SIMPLE) IRA** | A retirement program that permits eligible employees to make salary deferral contributions to their own IRAs, and the sponsoring employer to make matching or non-elective contributions. |
| **Nonqualified Plans** | These plans are typically used to provide additional benefits to key or highly compensated employees. They do not have the restrictions that qualified plans carry. Therefore, they do not meet the guidelines required to receive the tax advantages that a 401(k), 403(b), SEP IRA or SIMPLE IRA does. |

## Plan Design

Within each plan type is a plan design. For example, when sponsoring a profit sharing plan an employer may choose between different allocation methods. Some of the popular choices include: salary ratio, permitted disparity, age-weighted and new comparability. These different plan design options may help the employer meet various testing formulas that are required to maintain the plan's tax-advantaged status. The following chart provides information on key plan types and designs.

| Choosing the Right Retirement Plan | |
|---|---|
| **401(k) Plan** | |
| Who Can Establish | Partnerships, corporations and nonprofit groups (no government entities) |
| Key Features | 1. Permits pretax salary deferral contributions<br>2. Designated Roth contributions offer tax-free qualified distributions (salary deferrals and employer contributions are included in the participant's taxable income the year that they are earned)<br>3. Employer matching and profit-sharing contributions may be discretionary<br>4. Vesting schedule on employer contributions is determined by the employer<br>5. Participant loans are available<br>6. Due to complicated discrimination testing and tax reporting, third-party administrative services are recommended |
| 2015 Annual Contribution Limit | • Employees can defer up to $18,000 ($24,000 if 50 or older)<br>• Deferrals and employer contributions cannot exceed the lesser of 100 percent of compensation or $53,000 per employee; catch-up deferrals are not included in this limit<br>• Total employer contributions to the plan cannot exceed 25 percent of total eligible compensation. (Employer contributions exclude employee deferrals)<br>• Maximum eligible compensation: $265,000 |
| **Safe Harbor 401(k) and Super Comparability 401(k)** | |
| Who Can Establish | Partnerships, corporations and nonprofit groups (no government entities) |
| Key Features | 1. Safe Harbor 401(k) permits employers to choose either a 3 percent profit sharing contribution or a 4 percent match on a 5 percent deferral<br>2. Super comparability 401(k) combines the features of a new comparability plan with 401(k) safe harbor provisions<br>3. Employer contribution must be made each year to maintain safe harbor provisions<br>4. No 401(k)-type discrimination testing for either plan<br>5. Participant loans are available for either if permitted by the plan<br>6. Due to the complexity of the contribution calculation, retirement plan administrative services are required |
| 2015 Annual Contribution Limit | • Employees can defer up to $18,000 ($24,000 if 50 or older)<br>• Deferrals and employer contributions cannot exceed the lesser of 100% of compensation or $53,000 per employee; catch-up deferrals are not included in this limit<br>• Total employer contributions to the plan cannot exceed 25 percent of total eligible compensation (Employer contributions exclude employee deferrals)<br>• Maximum eligible compensation: $265,000 |
| **Tax-Sheltered Annuity Plan (403(b) Plan)** | |
| Who Can Establish | Universities, colleges, hospitals, churches, schools and other nonprofit 501(c)(3) groups |
| Key Features | 1. Participants can make pretax salary deferral contributions<br>2. Permits higher contribution limits than traditional IRAs<br>3. Employer matching or discretionary contributions are optional<br>4. Participant loans are available if permitted by the plan |
| 2015 Annual Contribution Limit | Up to the lesser of 100 percent of eligible compensation or $18,000 ($24,000 if 50 or older) |

# Choosing the Right Retirement Plan *continued*

## Traditional Profit-sharing Plans, Age-weighted and New Comparability

| | |
|---|---|
| Who Can Establish | Self-employed persons, partnerships, corporations and nonprofit groups |
| Key Features | 1. Profit-sharing contribution requirements are set in the plan document; contributions may be discretionary<br>2. Age-weighted formula is determined by the salary range and age of employees<br>3. New comparability formula groups employees into categories and then bases the formula on each group as governed by nondiscrimination regulations<br>4. Employers may add a 401(k) salary deferral feature for all plans<br>5. Participant loans are available for all if permitted by the plan<br>6. Vesting schedule is determined by the employer for all plans<br>7. Due to the complexity of the contribution calculation and nondiscrimination testing, retirement plan administration services are required |
| 2015 Annual Contribution Limit | • Up to the lesser of 100 percent of eligible compensation or $53,000 per employee; total employer contribution cannot exceed 25 percent of total eligible compensation<br>• Maximum eligible compensation: $265,000 |

## SIMPLE IRA

| | |
|---|---|
| Who Can Establish | Self-employed persons, partnerships, corporations, nonprofit groups; tax-exempt institutions and government entities with 100 or fewer employees. Generally, the employer may not maintain another plan. |
| Key Features | 1. Inexpensive 401(k)-type plan for the smaller business owner<br>2. No 401(k)-type discrimination testing<br>3. Deductible employer contributions are made directly to employees' IRAs<br>4. Employer contributions are mandatory<br>5. All contributions are immediately 100 percent vested |
| 2015 Annual Contribution Limit | 1. Employees can defer up to $12,500 ($15,500 if 50 or older)<br>2. Employer must choose one of two options:<br>• Match employee's contribution dollar for dollar, up to 3 percent of compensation (no salary maximum; match cannot exceed deferral limit)<br>• Contribute 2 percent of each eligible employee's compensation (maximum eligible compensation:$265,000) |

## SEP Plan

| | |
|---|---|
| Who Can Establish | Self-employed persons, partnerships, corporations and nonprofit groups |
| Key Features | 1. Deductible employer contributions are made directly to employees' IRAs<br>2. Employers can change their annual contributions<br>3. All contributions are immediately 100 percent vested<br>4. Minimal paperwork and reporting |
| 2015 Annual Contribution Limit | Up to the lesser of 25 percent of an employee's eligible compensation or $53,000 |

SOURCE: www.irs.gov

**One size does not fit all when it comes to retirement plans. As your advisor, we can help you determine the design that can maximize your contributions and minimize your tax liabilities.**

## Compliance

No matter which plan you choose, it must be compliant with various Employee Retirement Income Security Act (ERISA) laws and Internal Revenue Service (IRS) regulations. Compliance questions you should consider include:

- Do you have a written plan document and an IRS determination letter?
- Are you familiar with the terms of the plan, and is the plan being administered in accordance with those terms?
- Is a written investment policy statement being utilized?
- Does the plan pass its discrimination tests?
- Is the ERISA Form 5500 prepared annually?
- Does your plan require a CPA audit?
- Do you have a fidelity bond?
- Have plan service providers been evaluated against competitors for cost and quality of service?

# Selection and Monitoring of Plan Investments

Develop an investment policy statement, select a balanced investment lineup and designate a default investment option for your plan.

## Investment Policy Statement

An investment policy statement (IPS) provides general guidelines that govern the selection and management of available investment options within a retirement plan. Adopting and following such a statement can help to significantly protect the plan sponsor and other fiduciaries from liability for plan investment performance. Specifically, an IPS provides policy direction and procedural guidelines that allow for:

- The selection and ongoing monitoring of investment options and service providers
- Compliance with the fiduciary responsibility standards imposed by ERISA
- Meeting the plan's overall objective of helping employees prepare for their retirement

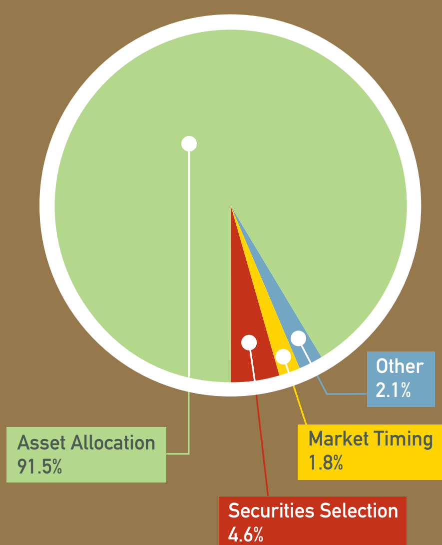
## Balanced Investment Lineup

A retirement plan must provide a balanced selection of investment options that have a track record of strong performance when compared to benchmarks. When looking into investment providers, consider those that offer a variety of investment options within different asset classes. This provides participants with the ability to diversify their investment mix. Some retirement plan vehicles also offer model portfolios and bundled asset allocation investment options.

## Diversification vs. "Picking Winners"

In the late 1980s and early 1990s, Gary Brinson, L. Randolph Hood, and Gilbert Beebower conducted two studies that significantly affected the way that financial advisors, portfolio managers and financial academicians look at portfolio theory and methodology. These studies, published in 1986 and 1991, examined the performance of 91 large U.S. pension plans between 1974 and 1983 and found that, on average, more than 90 percent of the variability in portfolio performance was determined by asset allocation[1]. Of the remaining determinants, the group found that security selection determined approximately 5 percent of performance, while market timing accounted for just under 2 percent. A follow-up study by Roger Ibbotson and Paul Kaplan (published in 2000) that examined returns of 94 stock/bond hybrid funds supported this conclusion.[2]

## Determination of Portfolio Performance




[1]Brinson, Gary P., L. Randolph Hood, and Gilbert L. Beebower. 1986. "Determinants of Portfolio Performance." *Financial Analysts Journal* (July/August).

[2]Ibbotson, Roger G. and Kaplan, Paul D. 2000. "Does Asset Allocation Policy Explain 40, 90, or 100 Percent of Performance?. " *Financial Analysts Journal* (January/February).

## Qualified Default Investment Alternatives

The Pension Protection Act of 2006 (PPA) created the Qualified Default Investment Alternative (QDIA) largely to promote the offering of automatic enrollment into 401(k) plans. The QDIA provides employers a safe harbor from fiduciary risk when selecting an investment for a participant or beneficiary who fails to elect his or her own investment. Employers following the QDIA regulations will have no legal liability for market fluctuations when providing a QDIA for employees who do not choose their own investments.

The PPA's goal for a QDIA is for it to meet a worker's long-term retirement savings needs, rather than just preserving capital. The final regulations provide four QDIA mechanisms:

1. A product with a mix of investments that takes into account the individual's age, retirement date or life expectancy (for example, a life-cycle or targeted retirement date fund).

2. A product with a mix of investments that takes into account the characteristics of the group of employees as a whole, rather than each individual (for example, a balanced fund).

3. An investment service that allocates contributions among existing plan options to provide an asset mix that takes into account the individual's age or retirement date (for example, a professionally managed account).

4. A capital preservation product for only the first 120 days of participation. This eases administration, for example, in the case of workers that opt out of participation within 90 days. After 120 days the plan fiduciary must redirect the participant's investment into the above three QDIA categories (unless the participant opted out of the plan or redirected investments during the 90 days).

**As employees struggle to make their own retirement decisions, they depend on employers to sponsor retirement plans that can help them meet their financial goals. The five pillars outlined in this brochure can help you focus on and manage the priorities that are paramount to having a successful plan.**

# Plan Participation and Education

## Implement strategies that can help your employees meet their financial retirement goals.

With less support from Social Security and traditional pension plans than in years past, employees may be feeling more financial pressure than ever before. Workers are now being asked to assume greater responsibility for the planning of their retirement needs. As an employer, there are ways for you to structure your retirement plan to help your employees meet their financial retirement goals.

The ideal strategy for running a successful retirement plan is to take full advantage of the opportunities that the PPA affords and combine it with a high quality, thoughtful education program. The following actions can help maximize a retirement plan's effectiveness:

- Conduct a diagnostic on your company's retirement plan to determine its current status. Measure the plan's participation and deferral rates, along with the average number of funds each participant owns. Benchmark those results against industry averages. Your retirement plan consultant is able to assist you with this process.
- Implement automatic features: automatic enrollment, automatic deferral increases and QDIA.
- Work with your retirement plan consultant to design an education strategy that helps ensure your employees understand the value of the plan. If not properly educated, participants may never increase deferral rates or they may opt out of the plan after being automatically enrolled.
- Devise a participant investment advice strategy as offered through the PPA. Your retirement plan consultant can be the fiduciary adviser to plan participants and help them make informed decisions.

# Service, Technology and Day-to-day Administration

## Select a provider whose plan administration capabilities and level of service fits best with your organizational needs.

Your retirement plan should help minimize the burdens on your organization, not bog you down with day-to-day administrative issues. Exceptional customer service minimizes time spent administering a plan. Other administrative considerations:

- How much time do you spend managing your plan?
- Does your plan have central administration or is a third-party administrator involved?
- Do you have a dedicated, responsive client contact at your current provider?
- If participants have a problem or a question, will they call you or your plan provider first?
- How efficient is the payroll and loan processing?
- What planning tools do participants have access too?
- Are the fees you are paying for plan administration reasonable relative to other providers?

**We remain committed to staying abreast of the latest resources, trends and legislative developments so that we can help empower you and your employees to effectively plan and prepare for retirement.**

**Our goal is to provide you the tools and resources that can help you build and maintain a successful plan for your employees.**

August Benefits can answer your questions about cost, administration and service.
Call us at: 631-435-2701

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