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The Retirement Advisor

"A Newsletter for Retirement Plan Sponsors"

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STONESTREET EQUITY, LLC

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Automate Your Plan

The stats are pretty clear. Too many employees don't take advantage of the opportunity offered by their employers' retirement savings plans — to the detriment of their future retirement security. What can you do to boost participation in your plan and help employees increase their account balances? Consider automating your plan in one or more of these ways.

Automatic Enrollment

With automatic enrollment, when an employee becomes eligible to participate in the plan, a set percentage of the employee's compensation is withheld (often 3%) and deposited in a 401(k) plan account for the employee. Some employers apply automatic enrollment only to new employees, but you could choose to automatically enroll all of your eligible employees. All employees must be given the option to decline participation.

(Cont'd on page 3)

Is it Time for a Self-Audit?

The IRS wants to learn more about 401(k) noncompliance so it can more effectively target plans for examination and bring them into compliance. In May, the Service mailed questionnaires to 1,200 401(k) plan employers randomly selected from the 2007 Form 5500 filings. It also issued a special edition of its *Employee Plans News* to provide an overview of the extensive questionnaire (*www.irs.gov/pub/irs-tege/se0510.pdf*).

Dear employer

The employers chosen to participate received a letter from the IRS with a password and personal identification number (PIN). The Internet-based questionnaire consists of 69 questions, many of which have multiple parts. The questions are about the 2008 plan year, although data must also be gathered from the 2006 and 2007 plan years. Employers were instructed to return the questionnaire within 90 days. The IRS stated that if an employer did not respond, the result would be further enforcement action, which will likely include an IRS examination of the plan.

What's next?

At recent conferences, IRS representatives have stated that when answers indicate that a plan is not in compliance, the plan will be subject to follow-up. The good news is that if an employer discovered a problem while responding to this questionnaire, the employer could still take advantage of self-correction or voluntary compliance programs to remedy the problem under EPCRS *before* the IRS follows up. The IRS indicated that future recipients will not have this option.

Once results are analyzed, they will be used as part of the examinations program. Plans under examination are not eligible to take advantage of voluntary correction. If significant errors are found, the plans are forced into closing agreements with much higher sanctions. The next wave of questionnaires (or other IRS examination projects) will be applied to a far larger base of 401(k) plans and, as already stated, will not provide time for employers to self-correct or enter the voluntary correction program.

A step ahead

Given these latest initiatives, this might be a great time for plans to consider conducting self-audits *before* the IRS arrives (in one way or another) for a real audit. The IRS has been promoting the idea of internal self-audit through the 401(k) Fix-It Guide, which can be found on its website at *www.irs.gov/ep*. Another good self-audit tool would be for employers to go through the 401(k) questionnaire with their plan professionals since there are a number of questions that may indicate noncompliance. The questionnaire (IRS Form 14146) is on the Internet at *www.irs.gov/pub/irs-tege/epcu_401k_questionnaire.pdf*. ▪

Focus on Target Date Funds

The Department of Labor's Employee Benefits Security Administration (EBSA) recently joined forces with the Securities and Exchange Commission (SEC) to publish an investor bulletin regarding target date funds (also known as life cycle funds). The guidance aims to give plan participants and other investors a better understanding of target date funds: what they are, how they operate, and how to evaluate them.

Plan sponsors will also benefit from this guidance. It can help them meet their fiduciary "prudent person" responsibilities by providing a better understanding of fund operations and a clearer picture of the risks involved.

Overview

Target date funds are long-term investments typically offered in retirement plans (although they are also available to investors outside retirement plans). Target date funds include a mix of investments, including equities, bonds, and other investments, designed to reduce overall risk. As a fund gets closer to its target date, the investment mix is changed, becoming more and more risk averse (i.e., more and more conservative).

This is fitting since a participant nearing retirement will soon need to withdraw money to live on and will have less and less time to recover from any losses that could occur in a volatile market. Ideally, the target date fund concept is a simple way to make professional portfolio management available to participants for the life of the retirement plan.

Same target date, very different funds

The EBSA/SEC bulletin stresses, however, that *participants should not rely on the fund's target date as the sole criterion for selecting the investment because funds with the exact same target date may have entirely different investment strategies, risks, returns, and fees.* Rather, individuals — and, we add, plan sponsors — are urged to evaluate the fund's underlying characteristics to determine whether it meets participants' needs. Further, the plan sponsor, in his or her role as plan fiduciary, must review the fund using the due diligence approach a prudent person would use and evaluate it in light of the goals stated in the plan's investment policy statement. If the fund meets the fiduciary's criteria and is approved as a plan investment, the individual participant will still need to consider whether it meets his or her needs.

The bulletin provides an example (see charts) of the extreme differences that can exist between two target date funds with an identical target date. When these two hypothetical funds reach their target date, the fund in Example 1 has an asset allocation of 60% stocks and 40% bonds. The fund in Example 2 holds 25% stocks, 65% bonds, and 10% cash investments, which is an investment mix one is likely to expect when the target date arrives. The investment mix in Example 1 leaves the investor heavily exposed to a market downturn right up to the fund's target date. This fund does not reach its most conservative mix of 30% stocks and 70% bonds until 25 years after its target date! *(Cont'd on pg. 4)*

Back to Basics: Record Retention

Retirement plans create a massive amount of paperwork. Retirement plan records include basic plan documents and adoption agreements, summary plan descriptions (SPDs), specific information about plan participants and beneficiaries, data needed to perform various tests, the tests themselves, governmental reporting, and contribution and distribution information.

The Employee Retirement Income Security Act (ERISA) provides rules for retaining retirement plan records. In addition, the U.S. Department of Labor (DOL) has issued regulations on keeping these records in electronic form. Keep in mind that the longer the paper trail, the easier it will be for a plan to respond to inquiries from a governmental agency or requests for information from plan participants.

Whose responsibility is it?

Generally, the burden of record retention falls on the plan administrator (the employer). However, it is possible that the job may be delegated to an outside service provider under the terms of its service agreement. Prior to changing service providers, employers should ensure that they receive copies of all necessary plan records from their current provider to alleviate future issues involving record retrieval. *(Cont'd on page 3)*

Quotes of the Quarter

"Retirement may be an ending, a closing, but it is also a new beginning."

Catherine Pulsifier

"The harder you work, the harder it is to surrender."

Vince Lombardi

"A man can't retire his experience. He must use it."

Bernard Baruch

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Automatic Contribution Escalation

Along with automatic enrollment, consider automatic contribution escalation. You can increase the automatic deferral percentage over time as long as the increases are made in accordance with a specified schedule. You must notify employees of the amount of the deferral increases and when increases will occur. Employees must be given the option to opt out of increases.

Automatic Rebalancing

Rebalancing may help cushion the impact of market downturns such as the one we saw in 2008. You may have several options for offering participants automatic rebalancing: Make automatic rebalancing an optional feature of your plan and encourage participants to use it; offer managed accounts; or choose a default investment option for your plan, such as a life-cycle or target-date fund, that automatically rebalances.

Retirement Saving Stats

▪ 19% of employees choose not to participate in the retirement savings plan offered by their employer.

▪ 58% of employees who don't participate have saved less than $10,000 for retirement versus 13% of those who do.Source: *2010 Retirement Confidence Survey*, Employee Benefit Research Institute, www.ebri.org ▪

Back to Basics: Record Retention Cont'd

How long must records be preserved?

Some plan records are retained for a fixed time period; others must be retained permanently. According to ERISA (Section 107), records used in the preparation of governmental reporting (such as Form 5500 and Form 1099-R) and participant disclosures (such as participant statements) must be preserved for at least six years from the date the report was filed (or should have been filed) or the disclosure provided. Note that retained reporting records must provide enough detail for the government to verify the accuracy of the report.

Plan records that must be maintained permanently include plan documents (including all adoption agreements and plan amendments), IRS determination letters, insurance contracts, SPDs, and board resolutions.

What about participant information?

As a practical matter, plan administrators may want to keep participant records longer than six years in case of legal action, such as participant divorce proceedings or dis-gruntled employee lawsuits. Participant information that should be retained includes:

▪ Determination of eligibility ▪ Hire and termination dates ▪ Beneficiary designations ▪ Notarized spousal consents and waivers ▪ Loan, hardship, and distribution documentation ▪ Hours worked for vesting and allocation purposes ▪ Compensation used for testing and allocations ▪ Elective deferral, matching contribution, and payroll records

How should plan records be preserved?

Proper and complete archiving of plan records is essential. Due to technological advancements, many transactions no longer take place on paper, which presents an added challenge. According to DOL regulations, electronic media may be used to comply with record retention rules provided the following requirements are met:

▪The recordkeeping system has reasonable controls in place to ensure the accuracy of the records.
▪The electronic records are maintained in reasonable order and in a safe and accessible place.
▪The recordkeeping system should be capable of indexing, retaining, preserving, retrieving, and reproducing the electronic records. (The retrieval issue becomes more interesting as equipment is updated and upgraded. For example, records retained on floppy disks may fail this test if no system drives are maintained to read that media).
▪The electronic records can be readily converted into legible paper copies.
▪The recordkeeping system is not subject to restrictions that would inappropriately limit access to the records.

With a few exceptions, original paper records may be disposed of after they are transferred to an electronic recordkeeping system, provided the system complies with these requirements. *The original may not be discarded* if it has legal significance or inherent value in its original form (e.g., notarized documents, insurance contracts, stock certificates, and documents executed under seal). ▪

Quotes of the Quarter

"Effort only fully realizes its reward after a person refuses to quit."

Napoleon Hill

"A culture of discipline is not a principle of business; it is a principle of greatness"

Jim Collins

"If you don't drive your business, you will be driven out of business."

B. C. Forbes

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Focus on Target Date Funds Cont'd

The market downturn of 2008/2009 had a surprisingly harsh impact on many of the target date funds that were being used as participants' retirement plan investment options. Many participants who were close to retirement were shocked that their target date funds lost so much value; they believed they were shielded from substantial loss by investing in a target date fund like the one in Example 2. It wasn't until the market downturn occurred that they learned — the hard way — that they were invested in a target date fund like the one in Example 1. They didn't expect a major loss so near the fund's target date (and their retirement), since they believed the fund should be providing a conservative, less risky mix of investments.

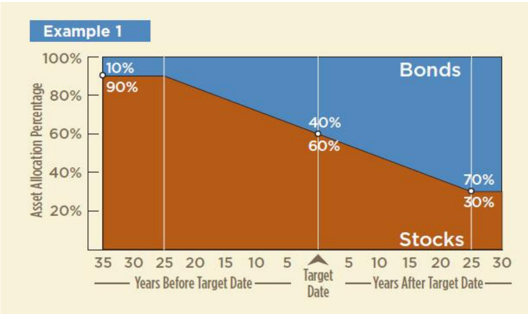
Tips for evaluating a target date fund

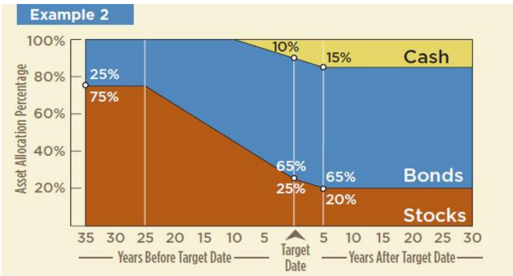
The bulletin provides a number of tips to help plan participants evaluate a target date fund before choosing it as an investment. In addition to the fund's target date, the bulletin advises participants to review the fund prospectus to find out the following:

- When does the most conservative mix of investments occur?
- What is the fund's risk level?
- How has the fund performed in the past?
- How does the asset allocation change over the life of the fund?
- What fees apply?

Guidance for fiduciaries

Since plan fiduciaries are responsible for the prudent selection of plan investments, the DOL will also be releasing guidance to assist them. A fiduciary compliance checklist will be published to help with the evaluation and selection of target date funds. ▪





Source: http://www.dol.gov/ebsa/pdf/TDFInvestorBulletin.pdf

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