Promoting Lifetime Plan Participation
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Movement of Assets from 401(k) Plans

As of December 31, 2013, 401(k) plans represented $4.2 trillion out of the $22.8 trillion of assets contained in the U.S. retirement system. But, as large as this number seems, it is significantly outweighed by the $6.5 trillion contained in IRAs that are viewed widely as a more expensive and less efficient way to invest retirement assets. According to some research, as much as 90 percent of these IRA assets is traceable to 401(k) and other defined contribution plans. Moreover, leakage of assets from the system through withdrawals, loans, and cash-outs has long been viewed as an impediment to retirement security.

The DOL's ERISA Advisory Council (Council) representing employers, employees, plan providers, and the general public recently issued a report whose underlying thesis is that participants would be better served if they consolidated all of their retirement assets in a single employer-sponsored plan, regardless of whether or not they remain employed by that plan's sponsor. The report suggests plan design features that can be implemented by plan sponsors and administrative actions recommended for adoption by the DOL that would facilitate so-called "Lifetime Plan Participation."

Addressing Plan Leakage

The report cited a number of plan features designed to address the perennial concern of preventing leakage of assets from the employer-based retirement plan system. For example, plan sponsors can disallow hardship withdrawals until all loan options have been exhausted. In addition, sponsors can ensure that participants understand when taking a hardship withdrawal, not only will their contributions stop for six months, but they will also lose matching dollars. Further, at the end of a six-month hardship suspension period, sponsors can reenroll participants automatically, subject to opting out, thereby addressing the inertia problem in a manner similar to automatic enrollment.

As suggested by Treasury official Mark Iwry, sponsors can address leakage from plan loans by adopting plan provisions that disallow matching contributions as a source for loans or withdrawals. However, the Council showed some ambivalence about loans, since it also recommended that sponsors consider allowing loans to continue after termination of employment as a way of encouraging employees to keep their money in the system. The Council also suggested sponsors consider permitting the initiation of new loans after employment termination. The Council acknowledged the difficulty of staying in touch with former employees and of administering plan loans made to them, but noted that automatic debit capabilities with a terminated employee's bank or credit card company could lessen the burden. A DOL representative appearing before the Council observed that loans to former employees are not prohibited transactions so that these loans do not need to comply with loan regulations in order to proceed.

Consolidating Plan Assets

As much as, and perhaps more than, the leakage of plan assets, the reason for the Council's concern about assets leaving the employer plan system was its view that participants enticed to roll over 401(k) assets into an IRA are getting a bad deal in the form of higher fees and the loss of ERISA fiduciary protection. This fear underlies DOL Advisory Opinion 2005-23A's holding that where a plan fiduciary discusses the advisability of a distribution or the investment of plan withdrawals, this advice is made in a fiduciary capacity and must be prudent, as well as consistent with ERISA's prohibited transaction rules. While the DOL has yet to take proactive steps to encourage retention of assets by retirement plans, the Council's report suggests techniques to make plans a more attractive retirement vehicle and to facilitate the consolidation of retirement assets in a single plan.

According to the Council, the first step for sponsors interested in this course is to let participants know they are welcome and encouraged to keep their assets in the plan after they retire or terminate. While a minority of sponsors have adopted this as official policy, it is by no means clear that a majority of them would welcome this approach due to expense and potential liability.

As for plan features to encourage plan retention of assets, the Council's suggestions focused on enhancing investments, distribution options that deemphasize lump sums, and techniques to encourage roll-ins. With respect to investment features, the Council proposed that plans provide a brokerage or mutual fund window as well as stable value fund options. Further, plans were encouraged to offer financial advice or assistance, although the DOL needs to do more to distinguish when this is mere investment education as opposed to fiduciary advice that creates liability exposure.

In the case of distribution options, plan features that could be added to keep assets in the plan include

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also resurrected the concept of “sidewalk” IRAs, authorized by EGTRRA in 2001, but seldom used. This is essentially an IRA option attached to a qualified plan through a master trust structure that enables access to the plan’s investment options.

**Recommended Agency Action**

The Council’s report is careful to avoid any suggestion that implementing the measures discussed above should be mandatory. Instead, it recommends that the DOL develop model notices and educational materials to encourage plan sponsors to offer lifetime income options and to guide participants in deciding what to do with plan assets when they change jobs or retire. The Council also believes the DOL should create uniform sample forms to facilitate plan to plan transfers and cooperate with other government agencies in developing standards that will foster the electronic transfer of funds and consolidation of accounts.

In 2008, the IRS issued proposed, but never-finalized, regulations that would have required participants receiving a plan distribution to be notified (as required by the Pension Protection Act of 2006) of any right to defer the distribution. Echoing GAO reports, the Council calls for this proposal to be updated and finalized so that the required notice includes an explicit disclosure that IRAs may have higher fees than investments in a plan. Further, the Council believes this notice should be required not only prior to receipt of a distribution, but also at any time a participant terminates employment.

**Conclusion**

It is clear that policymakers are concerned by the movement of plan assets to IRAs which is seen as not in the best interest of participants. It is not clear if the DOL Advisory Council’s proposals can stem the tide or if plan sponsors have any interest in doing so. If the trend continues, however, it would not be surprising to see restrictions on marketing or fees to keep these funds in qualified plans.

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