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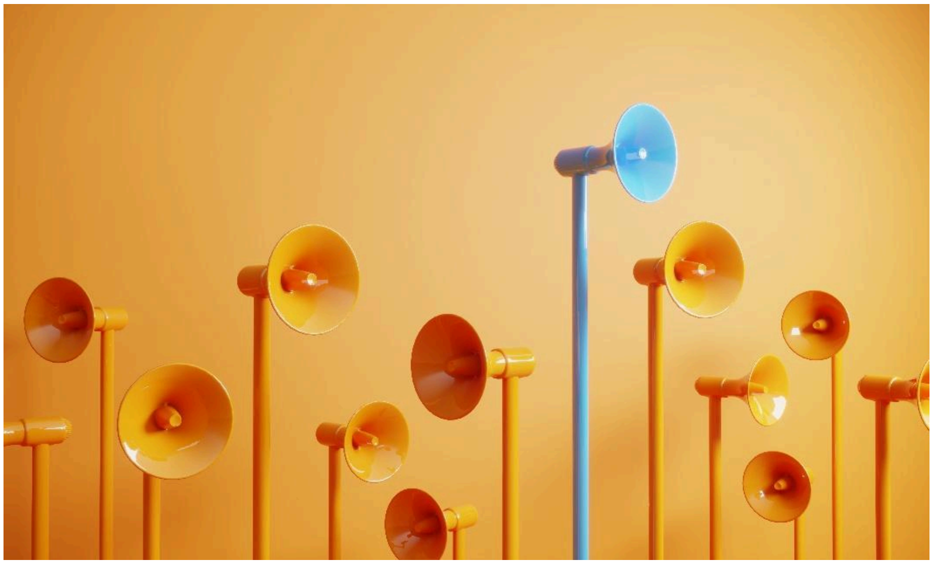
Managed Accounts Offer a More Personalized Approach



Target-date funds have long played a vital role in giving American workers access to professional help when establishing and maintaining a diversified investment portfolio. However, the glide paths — the balance of stocks, bonds, and cash — that serve as the foundation for these platforms has traditionally been based on a single consideration: the participant's projected date of retirement.

To be fair, target-date funds have played an important role in helping millions of novice (and even expert, but busy) retirement plan savers invest in broadly diversified portfolios overseen and rebalanced on a regular basis by professional investment managers. But the allocation of those investments between investment classes — the glide path — is still often based on that one demographic factor. Still, it's no more precise than a broad five- or 10-year time frame that approximates a traditional retirement age — which may, or may not, apply.

That means, of course, that those investment allocations can be oblivious to key demographic considerations like gender (women tend to live longer), marital status (ditto married individuals), race, and health, as well as investment risk appetite and other means of retirement income support. In short, they can overlook the kind of things that would be considered if there were an opportunity to sit down in a one-on-one conversation with a financial advisor.

Enter managed accounts — a solution that considers an expanded array of personal considerations like those noted above. These accounts craft a more relevant, personalized portfolio based on individual variables that can have a huge impact on how a retirement investment portfolio is designed. Traditionally, this was done via a one-on-one interview with an individual. But these days much of this data can be found in payroll systems and/or may already be maintained in recordkeeping platforms — or fields present in standard wealth management programs.

The Potential Impact

A Morningstar study found that after using managed accounts, 72% of participants who were off-track in saving for retirement increased their savings rates. At median, this represents a 33% jump from what they were contributing previously, or about 2% of their salaries on average. Additionally, a larger number of off-track participants (12%) started contributing enough to receive the full employer match.

The study also found that after using managed accounts, participants' assets were placed into portfolios that were more risk-appropriate. Moreover, the researchers noted "improved expected annual returns both in nominal and risk-adjusted terms."

The Bottom Line
Managed accounts can provide retirement savers with a more personalized asset allocation — but not every managed account platform provides the same depth and level of customization. Additionally, that level of personalization comes at a price. Plan fiduciaries should carefully consider the cost, quality, and composition of those designs. They should also document how and why services were evaluated, selected, deemed necessary — as well as compensated — when adding a managed account option to their lineup.

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Don’t Take Forfeitures for Granted

Retirement plans have long subjected employer contributions to vesting schedules, rewarding tenure by increasing the participant’s ownership in those contributions in proportion to their years of service.

However, several law firms have recently challenged this long-standing and common practice, arguing that using forfeitures to offset employer contributions is not in the best interests of participants or beneficiaries, as ERISA requires.

What Are Forfeitures?
“Vesting” in a retirement plan means ownership, according to the IRS. More specifically, this means that workers vest, or own, a certain percentage of their account in the plan each year, depending on a timeline established by the plan. Amounts that are not vested — earned, by virtue of their hours or service — may be forfeited by employees when they are paid their account balance. Vanguard reports that more than half of the plans it administers impose vesting requirements on employer contributions.

Now, when a worker leaves prior to becoming 100% vested in those contributions, those “forfeited” account balances may, according to established regulatory guidance, be either (1) used to offset employer contributions, (2) applied to reduce plan expenses, or (3) reallocated to the remaining participants in the plan.

Committee Considerations
The litigation filed thus far has alleged that the decision on how to reallocate plan forfeitures by the plan fiduciaries was a fiduciary decision and not in the best interests of participants — even though the IRS allows plans to make this decision. In fact, this practice has been common among retirement plans for decades.

While these cases are still working their way through the courts, in view of how many plan committees routinely make decisions on the disposition of forfeitures, careful consideration on those determinations going forward would be prudent. As a result, retirement plan fiduciaries may want to consider the following:

1. Review the plan document to confirm how/if it says forfeitures are to be reallocated (some of the suits have alleged that plan committees have not followed the terms of the plan document).

2. If the plan document leaves the decision to the plan committee, in consultation with an ERISA attorney, consider amending the document to remove that decision from plan fiduciaries — either by spelling out a specific order of reallocation, or by leaving that decision to those not affiliated with the plan (say, the board, as a plan design decision).
3. Consider immediate vesting for eligible participants. Note that this has cost and communication implications. Recent research by Vanguard finds that vesting does not provide a systematic retention benefit, though there is a 2.5% recovery of employer contributions for the average plan.

In short, don't take forfeitures for granted.

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Basic Fiduciary Obligations for New Plan Sponsors

Threats of financial penalties and legal liabilities heighten the need for proper compliance with the Employee Retirement Income Security Act of 1974 (ERISA). Let’s go over the basics of what it means to be a fiduciary in an organization’s retirement plan.

What is a Fiduciary?

In basic terms, a fiduciary is a person or group in a company that is responsible for the retirement plan and does what is best for the participants in the plan. There can be three different kinds of fiduciaries in a plan:

1. Named Fiduciary: This person or group is named specifically in the plan rulebook. There can be multiple people to handle different tasks such as investments and reporting.
2. Appointed Fiduciary: A named fiduciary is allowed to assign fiduciary responsibilities to another person such as an investment manager to handle monetary decisions.
3. Functional Fiduciary: This is someone that isn’t appointed as a fiduciary on paper, but steps into the role. Even if they aren’t officially listed on the plan rulebook, they legally become a fiduciary.

Fiduciary Obligations

According to ERISA, there are 4 main duties of a fiduciary:

1. Acting in the best interest of the retirement plan participants, not the fiduciary’s or company’s.
2. Making careful and knowledgeable decisions involving retirement plans.
3. Don’t put your eggs in one basket. Spread out investments to reduce risks.
4. Follow the plan rulebook unless it goes against federal guidelines.

In addition to these main duties, there are additional tasks assigned to plan fiduciaries. Reporting, keeping records, and handling claims are large responsibilities that can result in major penalties if not completed correctly. To begin, fiduciaries need to annually file a Form 5500 with the government to be transparent with plan performance. Failing to do this can include up to $2,670 per day from the Department of Labor as well as IRS penalties. Keeping records related to the plan as well as sharing these records with participants will be important for any potential legal disputes that arise. Any claims made by participants about their retirement plans must also be handled by the plan fiduciary.

Plan fiduciaries carry a big responsibility, and it's important to operate fairly for the sake of the plan participants as well as know the regulations to mitigate any future liability issues.

Source
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PARTICIPANT CORNER

Saving in Your 20s, 30s, 40s and Up… What Changes?

No matter how old you are, it's never too early (or late) to save money for retirement. Each decade comes with different goals, investment types, and risk factors, but understanding the difference can help you be prepared for when your retirement comes around.

Entering the Workforce: Your 20s
Your early career is going to be the most important time to save money in your retirement. With compound interest, that money that you put in your account in your 20s has about 40 years to accumulate, giving you a large return on your initial investment. Understandably, contributing a large portion of your paycheck is not attainable for most participants, but any contribution is better than none, and always aim to maximize your company's match (it's free money!).

Level Up in Your 30s and 40s
You've already started your career; you've moved up and began earning more money than in your 20s, which means it's time to increase your contributions. Bump up your percentage, and, if feasible, turn on auto-escalation to increase your contributions year after year. If you are still working on repaying loans such as auto or student loans, revisit your investment options annually and re-evaluate your options.

Close to the Finish Line: Your 50s and Early 60s
The time has finally come to start planning your retirement, but not so fast! You still have time to boost those savings before you fully retire from the workforce. After 50, you have the opportunity to contribute catch up contributions up to $7,500 (as of 2025) on top of the $23,500 usual limit for a total of $31,000. As a bonus, if you are 60-63, you can access an even higher limit of $34,750 for a "super" catch-up contribution. If you maximize that extra bump, that is an extra $15,000 which could mean having an extra $100 per month for over 12 years.

No matter what age you are, saving for retirement is important for securing a financially stable future. Don't know where to start? Reach out to your retirement plan's representative for help!

For more information, please contact The 401K Shop at (979) 865-0660.

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