Retirement Plan Solutions

SunTrust

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Retirement Adequacy — A Cause for Concern?

How many Americans are adequately prepared for the costs of their future retirement? Numerous studies over the years that have researched the issue of retirement adequacy have reached markedly different conclusions. Some predict that a significant part of the population is at risk for financial hardship in retirement, while others are more optimistic about retirement outcomes for much of the population.

Measuring and predicting retirement income adequacy is an important way for plan sponsors and employers to benchmark their plans with those of their competitors. A deeper understanding of the issue can help employers identify deficiencies in their own plans and take steps to realign them to better meet the needs of their employees.

Plan sponsors may be interested in a recent paper by the Society of Actuaries,® *Retirement Adequacy in the United States: Should We Be Concerned?,* 2018, that summarized the current research on retirement adequacy and clarified the differences in stakeholder perspectives, research objectives, empirical methodology, and model assumptions that have led to divergent conclusions.

On track or not?

According to the paper, current research shows that a large majority of Americans are on track to support a reasonably comfortable retirement. It further noted that the individuals at least risk of a financially difficult retirement are those in the highest income groups, who have many types of assets and income to support retirement, and those who have participated in employer-sponsored pension and retirement plans throughout their career. Those who face the greatest challenges are the disabled, widowed, unemployed, divorced, and individuals employed in industries or jobs that do not typically offer retirement benefits to workers.

Overall findings

The Society of Actuaries drew several conclusions from their review of major studies. They found that:

- The current system of voluntary employment-based retirement plans has been largely successful and constitutes an important pillar of the retirement system.

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- The Social Security system has done much to reduce poverty in old age.
- Households without access to employer retirement plans will receive a base level of lifetime inflation-adjusted income from Social Security. However, Social Security alone will not allow them to maintain their preretirement standard of living.
- More research needs to be carried out on the retirement challenges of vulnerable populations. Modifications to the social safety net or employer programs will be necessary.
- The different methodologies used in retirement adequacy research can make comparisons of results difficult. The Society of Actuaries' research noted that it was important to make distinctions based on assumptions in the models and that most studies:
    - Do not account for major unexpected shocks or expenses, such as poor investment performance, the cost of long-term care, the death of a spouse, and unanticipated medical expenses.
    - Assume the adequacy objective is to maintain the preretirement standard of living even though some retirees may be content with a lower level of spending. This assumption may understate the degree of adequacy in the system.
    - Assume that people retire at a "normal" retirement age.
    - Treat the issue of housing wealth differently. Overall retirement adequacy is higher if housing wealth is accessible to meet retirement needs.
    - Focus only on retirement adequacy of current or near retirees. Today's younger workers may encounter greater challenges in attaining retirement adequacy because of demographic issues, higher debt loads, lower likelihood of marriage and home ownership, shifts in employment, changes in the structure of employee benefit plans, and potential future reforms to Social Security.

Helping employees help themselves

A retirement plan remains one of the most attractive benefit options when it comes to attracting and retaining key employees. Plan sponsors should regularly evaluate their retirement plans to ensure that they continue to offer employees the potential to build adequate assets to ensure a financially secure retirement. ■

Decline in Household Spending by Age Cohort in the Health and Retirement Study, EBRI Analysis, 2013 dollars

	Age 65-75		Age 75-84		Age 85+	
Category	Mean	Median	Mean	Median	Mean	Median
Home	$18,720	$12,642	$14,732	$10,805	$13,111	$8,781
Food	$4,526	$3,982	$3,994	$3,228	$2,520	$2,152
Health	$4,383	$3,104	$4,624	$3,109	$6,603	$2,814
Transportation	$5,169	$4,025	$3,666	$2,794	$1,972	$1,241
Clothing	$1,311	$724	$950	$569	$888	$434
Entertainment	$4,300	$2,380	$3,277	$1,655	$1,609	$714
Other	$3,583	$1,148	$3,565	$1,034	$3,188	$734
Total	$42,805	$34,036	$35,315	$29,884	$30,610	$22,263

Source: *Retirement Adequacy in the United States: Should We Be Concerned?*, 2018

Protecting Employee Benefit Data

What plan sponsors should know

Retirement plan sponsors collect and hold a range of sensitive information, such as Social Security numbers, birth dates, and the addresses of plan participants. Typically, that information is stored in databases or the cloud and is frequently exchanged with third-party administrators, plan consultants, and investment management firms.

The potential for a security breach and the theft of sensitive employee data is a serious threat to participants, since criminals can use this type of information to steal an employee's identity. Plan sponsors should be aware of the dangers and the steps they can take to minimize the potential for a data breach.

The costs of such a breach can be significant. In addition to potential penalties and fines, there may be other costs to restore plan assets that were lost, inform participants whose accounts were impacted, and provide identity-theft protection.

Plan sponsor obligations

While federal laws exist that govern the use and the security of financial information held by the financial industry, they do not apply directly to retirement plans or to the sensitive information on participants held by those plans. However, U.S. Department of Labor (DOL) regulations impose an obligation on plan sponsors that distribute plan information electronically to ensure that the systems they use result in the actual receipt of the transmitted information and to protect the confidentiality of personal information relating to the participant's accounts and benefits.

In addition, DOL guidance requires that plan administrators who use a website to communicate investment information to participants take "appropriate and necessary measures reasonably calculated to ensure that the electronic delivery system protects the confidentiality of personal information."

Is cybersecurity a fiduciary responsibility?

An ERISA Advisory Council report issued by the DOL in 2017 did not directly address whether cybersecurity is a fiduciary responsibility. However, the report noted that further work was needed to clarify the extent of plan sponsor and vendor responsibilities to protect participant information. It also recommended that plan sponsors and fiduciaries consider cybersecurity in safeguarding plan data and assets and when making the decision to choose or retain a service provider.

SunTrust and cybersecurity

SunTrust's retirement plan recordkeeping platform is powered by Empower Institutional. SunTrust and Empower are committed to maintaining the highest level of online security and the protection of client information and accounts. We invest in systems and staff our team with experienced security professionals, and we employ multilayer processes to protect personal data. All systems are maintained under intense security protocols designed to stay ahead of the latest cyber threats and deliver the highest levels of protection to our clients and their participants. ■

Can Your Plan Pass the ADP Test?

Understanding the nondiscrimination rule

To encourage employers to offer retirement plans and employees to participate in them, the federal tax code confers tax-favored status on various types of employer-provided retirement plans. To retain that status, the plans must show that they do not discriminate in favor of highly compensated employees. Every traditional 401(k) plan must prove its nondiscriminatory status by carrying out an annual actual deferral percentage (ADP) nondiscrimination test. SIMPLE 401(k) plans and plans that have special "safe harbor" provisions are exempt from ADP testing.

The ADP test compares the average rates at which highly compensated employees defer salary with the average deferral rates for non-highly compensated employees. The differences between the averages for the plan's higher paid and lower paid employees must fall within a certain range.

The limits are:

- The ADP of the group of eligible highly compensated employees is not greater than 125% of the ADP of the eligible non-highly compensated employees, or
- The ADP of the eligible highly compensated employees is not more than two percentage points greater than — and no more than two times — the ADP of the eligible non-highly compensated employees.

Correcting excess contributions

There are two basic correction options for ADP test failures.

1. **Refund the excess contributions (plus allocable income).** While refunds can be made anytime within 12 months of the close of the plan year, a 10% excise tax applies to excess contributions not returned within two and a half months. For plans that include "eligible automatic contribution arrangements" covering all eligible employees, corrective contributions can be made up to six months following the end of the plan year without incurring the excise tax. Refunds will be taxable to the participants.

2. **Make additional employer contributions.** The other option is to make qualified nonelective contributions (QNECs) or qualified matching contributions (QMACs) for non-highly compensated employees. These contributions will be treated as elective contributions for ADP testing purposes until the plan satisfies the nondiscrimination test. ■

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