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Q1 2018

Qualified Plan News

March 2018 Capital Markets Review

	Period Ending March 31, 2018					
Index	**Qtr**	**Ytd**	**1 Yr Return**	**3 Yr Return**	**5 Yr Return**	**10 Yr Return**
S&P 500	−0.76%	−0.76%	13.99%	10.78%	13.31%	9.49%
Russell 3000 Value	−2.82%	−2.82%	6.81%	7.87%	10.71%	7.84%
Russell 3000 Growth	1.48%	1.48%	21.06%	12.57%	15.32%	11.31%
Russell 2000	−0.08%	−0.08%	11.79%	8.39%	11.47%	9.84%
MSCI ACWI Ex U.S.	−1.18%	−1.18%	16.53%	6.18%	5.89%	2.7%
Barclays U.S. Aggregate Bond	−1.46%	−1.46%	1.2%	1.2%	1.82%	3.63%
3-Month U.S. Treasuries	0.35%	0.35%	1.07%	0.49%	0.31%	0.31%

The U.S. equity market ended the first quarter down 0.6%, posting its first quarterly decline since the third quarter of 2015. January started the year off strong, as corporate earnings and favorable economic data supported the positive momentum following the tax reforms passed in December. The U.S. equity market fell sharply in February. Volatility spiked after U.S. wage inflation data showed signs of growth, indicating higher labor costs and raising the likelihood of further rate increases by the Federal Reserve. U.S. equities continued downward into March after the Trump administration announced it would be imposing import tariffs on select goods, raising the potential of a trade war with China. The Technology sector also dragged on the U.S. equity market in March due to privacy concerns, related to the use of data obtained from over 50 million Facebook profiles.

All capitalization segments of the market declined in the quarter, with large-cap stocks trailing both the mid- and small-cap segments of the market. Large-cap stocks continue to outperform the mid- and small-cap segments over the 1-year period. Growth stocks outperformed Value stocks by 4.3% in the quarter. The outperformance was due to the Consumer Discretionary and Technology sectors, which were the only two sectors to post positive returns in the period. REITs and Telecomm were the worst performing sectors in the quarter. Signs of a strengthening U.S. economy and rising wage inflation data increased the chances of further rate increases by the Federal Reserve, which sent REITs and Telecomm stocks down sharply in February.

International equities returned −1.2% in the quarter. In local currency terms, international equities returned −3.1% in the quarter. Despite continuing global economic growth, equity prices were negatively affected in many countries by fears of rising protectionism. Potential retaliatory trade restrictions against the U.S. and strong growth in other countries caused the value of the U.S. dollar to decline relative to most other currencies. Equity markets responded favorably to weaker-than-expected inflationary data from Europe and Japan, allowing their central banks to continue to provide accommodative monetary policy. Recent tensions with North Korea abated when Kim Jong-un agreed to meet with the presidents of both South Korea and the U.S. Emerging Markets overall posted a +1.4% return in the quarter as the weaker U.S. dollar and rising oil prices were supportive for equity prices, especially in many Latin American countries.

When Employees Retire Matters to Them…and to Employers

Americans pride themselves on making their own decisions, and when to retire is an important one. But it takes money to retire, and the shift away from traditional pension plans leaves many Americans ill-prepared to retire when they want to. Employees who struggle with their finances find it challenging to save enough to retire on their own terms.

But saving for retirement through 401(k) or other defined contributions plans has become an individual responsibility. Some would like to retire at 55 or 60, but must delay retirement until age 65 when they become eligible for Medicare. Others may want to retire at 65—the traditional age of retirement—but because of financial concerns have to wait to take the plunge until they reach full Social Security retirement age.

Without adequate resources, employees have less choice about when to retire.

Timing of Retirement is Important for Employers, Too

Employers have a stake in the timing of employee retirements. They, too, may suffer financially when employees are unprepared to leave the workforce on time. Of course, there are positive aspects to keeping older employees—experience, institutional knowledge, and a broader perspective, to name a few—employing older people who wish they were retired can have serious financial consequences. They may be distracted by financial concerns, less engaged in the company and their job, and less motivated than those who are happy to be working. They also reduce the company's ability to hire new talent, because of a lack of open jobs.

The Cost of Delay: Significant

A recent study found that a one-year delay in retirement for an individual can cost an employer $50,000. At that figure, it wouldn't take long for a 100-person company with 2 or 3 expected but delayed retirements per year to reach a significant level of expense.

To address the issue of delayed retirements, the study suggests adopting retirement programs with features that encourage appropriate financial behaviors. For example:

- **Saving**: Include an employer match to encourage more saving, and automatic enrollment and auto escalation to remove barriers to entry and increases in contributions.
- **Investing**: Offer quality investment alternatives for participants who prefer professional management of their account, and for those who fail to make an investment choice.
- **Withdrawing**: Including guaranteed lifetime income products among distribution options in a DC plan can reduce the level of assets needed for an individual to retire at age 65 by 36%, according to the study.

Education is critical to helping employees retire on time. Participants who are informed and confident often make better financial decisions, which can lead toward

Plan Sponsors Ask…

Question. From time to time an employee tells us they didn't know there were fees involved with the 401(k) plan. We are complying with the requirements to disclose the fees being paid, so it is surprising to us that some participants still don't know. Are we the only ones whose participants are not getting the message?

Answer. Unfortunately, your experience is not unusual. The National Association of Retirement Plan Participants, or NARPP, says that 58% of working Americans don't know they are paying fees on their workplace retirement savings accounts. That amounts to a staggering $35 billion dollars in fees every year, or $835 per investor. Even those participants who know they are paying fees are often unclear about how fees are calculated, with just 26% able to accurately explain. It's important to make sure the information provided to participants is clear, accurate and complete, because there is a strong link between fee transparency and trust from participants. NARPP found that 81% of participants would appreciate a standardized fee label on all retirement funds, similar to a food nutrition label. Visit www.narpp.org for more information on this and related research from NARPP.

long-term security. How much do employees know about saving for college while at the same time staying on track for retirement? Do participants know how much of their retiree medical expenses will be paid by Medicare? And do they understand how to maximize their Social Security benefits? Offering education on these and other important topics can get employees—and their employers—closer to the goal of on-time retirements.

Choosing a Retirement Plan That Maximizes Benefits for Owners and Key Employees

With the various restrictions and limitations on retirement plan contributions and benefits, small business owners and professionals may wonder whether it is possible to fund adequate retirement benefits for themselves using a tax-qualified plan. In many cases, it is—if the most appropriate plan design is chosen.

Why So Many Restrictions?

Many of the restrictions and limitations added to the federal tax code in the pension area have been aimed at making plans nondiscriminatory—i.e., making sure that the plan does not discriminate in favor of a firm's highly paid employees. In some cases, the perhaps unintended effect of the restrictions has been to dampen enthusiasm for retirement plans because business owners question whether the benefits they will receive justify the expense of maintaining a plan.

What plans should a business owner who is concerned about funding his or her own retirement consider? Several possibilities are discussed below.

Age-Based Profit Sharing Plan

One type of plan that may be appropriate for many small business owners and professionals is the age-based profit sharing plan. The plan combines the traditional benefits of a profit sharing plan with the ability to allocate employer contributions to participant accounts using factors that consider both compensation and age. In contrast, traditional profit sharing plans allocate contributions based only on compensation, with each participant receiving a flat percentage of pay.

If employee demographics favor the age-based approach, more of the annual profit sharing plan contribution is shifted to the accounts of the older owner(s) and key employees participating in the plan. In some instances, the total plan contribution can be lowered while allocations to the owner and the key employees remain at the same levels—or even increase.

Target Benefit Plan

This type of plan is a cross between a defined benefit pension plan and a money purchase plan. It uses actuarial assumptions—including assumptions about remaining years to retirement—in determining the amount to be contributed for each participant. As with an age-based plan, no more than $55,000 a year (in 2018) can be added to each employee's account, regardless of compensation or age. However, the plan is not as flexible as an age-based plan in that an annual employer contribution is generally required.

Defined Benefit Pension Plan

If the per-employee cap on additions to a plan account is a source of concern, a traditional defined benefit pension plan can often provide more lucrative benefits. With this type of plan, the closer a participant is to retirement age and the larger the promised retirement benefit, the higher the plan contribution, all else being equal.

Other Considerations?

Before deciding to implement any of these plans, the effect of the tax law's top-heavy rules should be analyzed. These rules generally are triggered when key employees hold more than 60% of the account balances or accrued benefits in all plans sponsored by the employer. When a plan is top heavy, every active participant must receive a minimum contribution or benefit (3% of pay for a defined contribution plan).

Qualified Plan News

Web Resources for Plan Sponsors

Internal Revenue Service, Employee Plans
www.irs.gov/ep

Department of Labor, Employee Benefits Security Administration
www.dol.gov/ebsa

401(k) Help Center
www.401khelpcenter.com

BenefitsLink
www.benefitslink.com

Plan Sponsor
www.plansponsor.com

Plan Sponsor Council of America
www.psca.org

Employee Benefits Institute of America
www.ebia.com

Employee Benefit Research Institute
www.ebri.org

S&P 500 is a commonly used measure of common stock performance. Russell 2000 is a commonly used measure of small capitalization stocks. Russell 3000 Value measures performance of U.S. equity universe broad value segment with lower price-to-book ratios and lower forecasted growth values. Russell 3000 Growth measures performance of Russell 3000 Index companies with higher price-to-book ratios and higher forecasted growth values. MSCI ACWI EX U.S. tracks 850 stocks traded in 22 world markets (excludes U.S. based stocks). Barclays U.S. Aggregate Bond Index tracks domestic investment grade bonds (including corporate, government, and mortgage-backed securities). Citigroup 3-Month U.S. Treasury Bill Index tracks short-term U.S. Government debt instruments. All referenced indices are unmanaged and not available for direct investment. Past performance is not a guarantee of future results.

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