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Just out of Reish: Automatic Piloting

There is a need to improve the retirement benefits provided by 401(k) plans. This column focuses on benefit improvements for the one-half of the private sector employees who are covered by 401(k) plans; however, my first point addresses the issue of improving overall coverage (The first part of this two-part series is at [Just out of Reish: 'Equal' Time?](#)).



Every employer should be required to sponsor an automatically enrolled deferral-based retirement plan, though start-ups could be given two or three years before they have to do so. The minimum initial deferral rate should be at least 3%, automatically increased each year up to at least 12%. Employees could elect to not make deferrals (or to cap their deferrals at any level).

The programs should, unless an employee elects otherwise, initially invest employee accounts in a qualified default investment alternative (QDIA) under the DoL's regulation. The programs also should include one or more "safe" investments, a money market fund and/or stable value. If well-selected and reasonably priced, the employer would have a fiduciary safe harbor for any and all employee investments.

Further, the plan sponsor would not be required to offer any other investments, but could do so. If they chose to, the employers would not be responsible for them as a fiduciary—if the lineup were robust (e.g., a mutual fund window) and if the employer disclosed that it was not responsible for those additional investments.

All employees, including part-timers, would be covered and enter the plan no later than the first day of the quarter following three months of employment.

Employers could transfer the fiduciary responsibility for the operation of their plans—both investment and administration—to specified entities. The entities could include the types that can serve as fiduciary advisers—for example, banks, trust companies, insurance companies, broker/dealers, mutual fund companies, RIAs, and so on. In other words, plan sponsors should be able to transfer all of the fiduciary responsibility, except for that for selecting that fiduciary that is the retirement plan administrator (RPA).

The RPA would have responsibility for selecting the investments, administering the plan, calculating benefits, making distributions, and so on. The fiduciary responsibility rules would be tightened to reflect higher expectations due to their full-time, professional status, and that they would need to have level fees or to satisfy an exemption that would permit them to receive variable compensation under strict limits and controls.

Service providers, including RPAs, would be required to report all of the plan costs, as well as their fees and revenues, as dollar amounts to employers and participants within three months after the end of each year.

Plan sponsors or RPAs would be required to educate employees about the concept of benefit adequacy. Participants would be given regular updates of the retirement income that is likely to be produced by their 401(k) accounts in combination with Social Security, and, if a participant is not on course for adequate benefits, he should be told the amount he needs to increase deferrals to get on course. Finally, plans should be required to provide participants with calculators to make reasonable retirement estimates, including the impact of different deferral rates and investing styles and of later retirement.

Plan sponsors or RPAs should be required to educate employees on how to withdraw their benefits in a manner that has a high probability of lasting for their lifetimes—even if they live beyond their expectancies (since, by definition, about half do). Employees also should have access to calculators that allow them to calculate the probability of the exhaustion of their benefits under a variety of scenarios.

Plans should be required to offer, as a primary—and default—alternative, a guaranteed form of retirement income for life. The guaranteed benefit should last for the life of the participant and the participant's spouse, unless the participant elects otherwise and the spouse consents.

With those changes, I believe that 401(k) plans would be better retirement plans. To accomplish that goal—and to avoid greater government involvement—employers will have to accept a higher level of responsibility for the results produced by their plans.

Fred Reish is Managing Director and Partner of the Los Angeles-based law firm of Reish Luftman Reicher & Cohen. A nationally recognized expert in employee benefits law, he has written four books and many articles on ERISA, IRS and DoL audits, and pension plan disputes. Fred has been awarded the Institutional Investor Lifetime Achievement Award and PLANSPONSOR's Lifetime Achievement Award. He is also one of the 15 individuals named by PLANSPONSOR magazine as "Legends of the Retirement Industry."

Fred Reish
editors@plansponsor.com