RAYMOND JAMES

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State Sponsored Retirement Plan Initiative 2019

Across the globe, more and more people are realizing a major retirement problem looming: retirement insecurity. This has been one of the side effects of the shift from DB to DC plans as the primary retirement savings vehicle. This issue has come to the forefront not just in the United States, but globally. Since 2012, there has been a dramatic increase in the number of stakeholders looking for a solution to this problem. While there are many private-sector solutions in development, this article will focus on the efforts of state regulators to expand retirement savings for private sector employees.

Since 2012, 43 states have taken steps to study, implement, or consider legislation that would establish state-facilitated retirement savings programs. As of the end of 2018, 11 states and 1 city have enacted new retirement savings programs and 2019 looks to continue this trend. However, we may only be in the early innings of the state-facilitated retirement plan movement; of these 11 initial states, only one is fully operational and the remainder are in pilot programs set to launch in 2019-2020. There have been four models these plans have followed so far: Auto-IRA, Multiple Employer Plan (MEP), Marketplace, and Voluntary Payroll Deduction IRA.

Auto-IRA: States currently utilizing this structure are California, Connecticut, Illinois, Maryland, Oregon, and the city of Seattle.

Multiple Employer Plan (MEP): States currently utilizing this structure are Vermont and Massachusetts.

Marketplace: States currently utilizing this structure are Washington and New Jersey.

Voluntary Payroll Deduction IRA: New York currently utilizes this structure.

In 2019, we have already seen state and local governments taking steps to implement state-facilitated plans. The mayor of New York City recently announced a proposal that would require employers with five or more employees to offer a retirement plan or auto-enroll employees into the city plan with a default Roth IRA contribution of 5%. Participants in the plan would have a limited investment menu of low-cost funds and ongoing costs would be funded by fees charged to participant accounts.

Two bills have been introduced in the Virginia House of Delegates since their new session began on January 9. H.B. 2431, which is modeled after Oregon's OregonSaves plan, and H.B. 2432, which would create a marketplace similar to what Washington State offers. Both proposals aim to expand

retirement savings, but H.B. 2431 would make it mandatory for all private-sector employers, sole proprietors, and the self-employed to participate, while H. B. 2432 would create a voluntary exchange. The exchange under H.B. 2432 would allow access to plans offered by financial services firms at a low-cost.

IFS believes that increasing access to retirement savings is an important first step. However, there is still a lot of room for improvement. Oregon recently released some interesting statistics on their own plan, called OregonSaves. Over the final six months of 2018, the plan added 1,659 employers and more than doubled in assets. The average employee saved $1200/year with an average savings rate of 5.2%. Compare this to data from Fidelity's Q3 2018 *Building Futures* report, which tracks various retirement plan metrics, and the room for improvement is apparent. In Fidelity's report, the average employee saved 8.7%, which equates to $6,830 of their own deferral and received $3,930 in employer match for a total average contribution of $11,150 (nearly 10 times more than OregonSaves' average savings).

The Rehabilitation for Multiemployer Pensions Act

On January 9th, the new Chairman of the House Ways & Means Committee, Richard Neal (D-MA), introduced a bill designed to help multiemployer pensions (not to be confused with Multiple Employer Plans, or MEPs) meet their liabilities. Currently, the backstop for a failed plan is the Pension Benefit Guaranty Corporation (PBGC), which would only provide participants pennies on the dollar from what they were promised. It is estimated that the PBGC trust fund that provides these payments will be depleted by 2025.

This proposal would create a new agency within the Department of the Treasury, the Pension Rehabilitation Administration (PRA). The PRA would have the authority to issue bonds in order to finance loans to plans in a "critical and declining" status, plans that suspended benefits, and some plans currently receiving assistance from the PBGC. The loan would be used to meet the plan's obligations in one of three ways: annuity purchase, a portfolio of investment grade bonds that match cash and duration needs, or "Some other portfolio prescribed by the Secretary of the Treasury in regulations which has a similar risk profile as Cash Matching and Duration Matching and is equally protective of participants' and beneficiaries' interests." The loan terms would require the plan to make interest payments for 29 years with a final interest and principal repayment in year 30.

The Importance of Having a Prudent Process – *Wilcox v. Georgetown University* [1]

Georgetown recently received a ruling in favor of the university's motion to dismiss claims similar to what was brought in *Sacerdote v NYU*. As a recap of the NYU lawsuit, the following has been reprinted from our Q3 update:

> *"Since 2006, we have seen an increase in the number of lawsuits filed against 401(k) plan sponsors for breach of fiduciary duty. But it wasn't until a decade later that similar lawsuits*

[1] Wilcox v. Georgetown Univ., D.D.C., No. 1:18-cv-00422-RMC, 1/8/19.

have begun targeting large university 403(b) plans. At IFS, we believe the best defense against litigation is to have a thorough and documented prudent process, and we encourage all plans to establish such processes. In the first 403(b) fee case to go to trial, Sacerdote v NYU, demonstrates the importance of having a prudent process. In this case, the plaintiffs alleged that the retirement plan committee members that oversee two NYU plans breached their fiduciary duties by failing to monitor investments and by allowing the plans to pay excessive recordkeeping costs. The argument is similar to many of the cases brought by Schlichter Bogard & Denton LLP, the law firm that has been successful in litigating private employer ERISA fiduciary breach lawsuits."

The Georgetown lawsuit was also brought by Schlichter, Bogard, & Denton LLP, but the arguments were rejected by the judge for failing to recognize basic facts about the way annuities work and their role in 403(b) plans. The court also called into question whether the plaintiffs have standing to sue, due to not showing fiduciary breaches that impaired account values (i.e., damages). These claims are reviewed below.

Claim: Using multiple recordkeepers resulted in excessive fees; the participants argued that the committee could have consolidated recordkeepers and negotiated lower costs.

> **Judge's Ruling:** The complaint alleges participants should pay only $35/year per participant for recordkeeping services for the three recordkeepers offered. However, the court ruled that plaintiffs provided no factual support for their assertions, cited no example of any non-TIAA entity recordkeeping TIAA annuities, nor showed any evidence that the investment platforms – TIAA, Vanguard, and Fidelity – would agree to continue the same offerings at a lesser price. The court stated, "the mere allegation that Georgetown could continue to offer the same Plans and the same associated services for $35/year has no factual support, is entirely speculative, contrary to case law and common sense, and does not warrant discovery."

Claim: The fiduciary committee retained underperforming funds (TIAA Real Estate fund and CREF Stock fund) that should have been removed from the investment menu.

> **Judge's Ruling:** The plaintiffs argued that the TIAA Real Estate fund was too expensive and compared it to the Vanguard REIT fund. Over the time period in question the TIAA fund performed better. The court ruled that because the plaintiff was invested in the better performing TIAA fund over the relevant time period, he did not experience loss or injury from the investment. Regarding the underperformance of the CREF Stock fund, the court found, "a fiduciary is not required to select the best performing fund. The CREF Stock Account, with its deliberate mix of foreign and domestic investments, may not have performed as some purely domestic accounts with different investments does not indicate imprudence on the part of Defendants."

The cases filed against universities underscore the importance of following a documented prudent process. Of the lawsuits targeting university 403(b) plans, those that have been able to demonstrate their prudent process have generally obtained pre-trial dismissals (University of Pennsylvania, Northwestern University, Washington University in St Louis, and Georgetown University) or won at trial (New York University). Those that have not followed a prudent process have generally resulted in settlements. IFS believes that all employer-sponsored plans should have a documented process in place and aligns with the firm's commitment to acting as a fiduciary.