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SUMMER 2013

The Pension Underfunding Threat

Can the states resolve the looming crisis in their teacher retirement systems?

Retirement Income Strategies

How Do I Move My Money?

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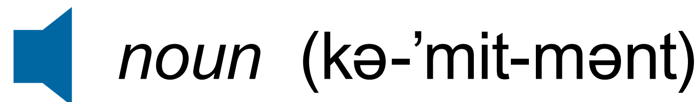

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403(b) ADVISOR

Summer 2013

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What are states doing to resolve the looming crisis in their teacher retirement systems?

STEVEN SULLIVAN

Cover:
Illustration by Robert Meganck

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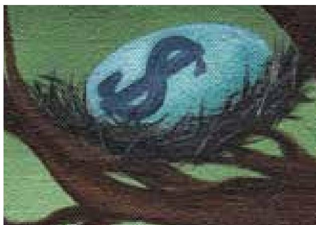

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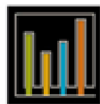
Participant Success Measures

Participant Success Measures refers to 10 recognized industry statistics that measure how well a plan helps participants prepare for retirement. This page lists each of these 10 statistics and compares them to the Benchmark Group. Few areas are more central to reviewing fees from the perspective of "what you get for what you pay." Here, small changes can make big differences for participants.

		This Plan's Participant Success Measures vs. The Benchmark Group							
Participant Success Measures	**% of Plans Measuring**	**This Plan**	**Low**	**Below Average**	**Average**	**Above Average**	**High**	**Difference from Average**
Plan's Current Participation Rate	81%	77%	46%	69%	77%	87%	98%	0%
Average Deferral Percentage for Non-Highly Compensated Employees	79%	6.1%	2.4%	4.2%	5.2%	6.1%	8.8%	0.9%
Average Deferral Percentage for Highly Compensated Employees	74%	7.1%	3.9%	5.6%	7.2%	8.2%	10.1%	-0.1%
% of Participants Maximizing Company Match	43%	56%	8%	36%	53%	69%	89%	3%
% of Plan Assets in Automatically Diversified Options*	96%	44%	2%	13%	22%	40%	74%	22%
% of Eligible Participants Making Catch-up Contributions	43%	42%	1%	3%	5%	15%	40%	37%
% of Participants Using Auto-Rebalance Option	32%	6%	1%	3%	7%	36%	74%	-1%
% of Terminated Participants NOT "Cashing Out"	43%	-	23%	47%	67%	82%	99%	-
% of Participants with a Personal Retirement Goal	2%	-	-	-	-	-	-	-
% of Participants On Track to Achieve That Goal	4%	-	41%	41%	48%	54%	54%	-

* Includes balanced funds, risk or target-based retirement choices, model portfolios, and managed accounts.
\- = N/A or not available.

# of Participant Success Measures Average or Better	0 for 10	1 for 10	2 for 10	3 for 10	4 for 10	5 for 10	6 for 10	7 or more for 10
Percentage of Plans in Benchmark Group	9%	23%	21%	21%	9%	6%	8%	4%



HOW DOES THE PLAN COMPARE
to the Benchmark Group with respect to these 10 important participant success measures?

- *This plan ranks average or better in **5 out of 10** categories*
- ***83%** of plans rank lower than this plan*
- ***11%** of plans rank above this plan*
- ***4%** of plans rank average or better in more than 6 categories*

BPAS offers a number of participant outcomes reports and strategies to assist our clients. For details, please call your BPAS Sales Representative.

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EDITOR'S LETTER

Good Ideas, for Free

Looking for some new ideas to add a little 'oomph' to your presentation? Need to reinvigorate an approach that may be getting a bit stale? How about trying something completely different to give your practice a little boost? Here are half a dozen ideas for you, totally free of charge:

- Now that school site visits are essentially a relic of the past, use a retirement saving toolkit as a way to get teachers out of the building to meet with you.
- Form your own "Director's Circle" — a small group of experienced, elite advisors you know. Get together on a regular basis, maybe twice a year, to share best practices and new ideas in a collegial setting.
- Think long term. For example, in 10 years, will 12b-1 fees exist? Will you still get commissions? Then reverse-engineer your practice to envision the best way to get from here to there — even if only as a thought experiment. They can be very helpful.
- Don't run away after you close a sale. Help with the plan; answer questions; assist participants; follow up to make sure all applicable ERISA and Code requirements are being met.
- Know who you're talking to. Sixty-one percent of people saving for retirement are more worried about running out of money than they are about dying. Forty-eight percent are interested in a guaranteed rate of return in exchange for a lower rate of return.
- Understand the "10/10/10 reality" of today's near-retirees: The 10,000 Boomers who turn 65 every day have seen 10 years of market volatility; and their life expectancy is 10 years greater than that of their parents.

I'm giving these ideas away, of course, because they're not mine in the first place. They came from the NTSAA 403(b) Summit held last month in Chicago. If you were there too, you can confirm just how great the conference was — from keynoters Bill Rancic, Dan Veto and Nevin Adams, to the expert panel discussions, the workshops, peer-to-peer roundtables, social events in the exhibit hall, a rousing NTSAA update from NTSAA Executive Director Chris DeGrassi, gracious MC-ing by Summit Chair Roxanne Marvasti and NTSAA President David Blask, and much more.

If you couldn't make it, look for my Summit wrap-up article in our next issue. And do yourself a favor: Make plans to join us at next year's conference in Washington, DC.

John Ortman, Editor

Correction

Our Spring issue included a special "thank you" to sponsors and exhibitors of the 2013 Summit. In the list of Summit sponsors, the logo of Lincoln Financial Group (which wasn't a sponsor) was included by mistake instead of the logo of Lincoln Investment Planning (which was). An updated "thank you" appears on page 45 of this issue.

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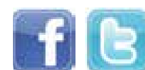

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GOVERNMENT IMPACT

Legislative Proposals Would Affect 403(b) and 457 Plans

BY MARK E. GRIFFIN

A trio of proposals affecting defined contribution plans have prompted reactions of varying degrees on and off Capitol Hill.

Congress' consideration of possible tax reform and deficit reduction measures has prompted Congress and others to examine the Internal Revenue Code for provisions that should be added, amended, or removed for various reasons. This examination has extended to the rules for tax-advantaged retirement plans — including Code Sections 403(b) and 457 — and the value of the tax benefits associated with them. This article identifies and briefly explains:

- a proposal by the Obama administration to limit the size of retirement plans;
- a proposal in the U.S. Senate to accelerate the distribution of amounts under such plans; and
- a proposal from the private sector that would consolidate certain retirement plans.

Limit the Size of Tax-advantaged Retirement Saving Plans

President Obama's fiscal year 2014 budget, released on April 10, 2013, includes a proposed new limitation — the "maximum permitted allocation" — on the aggregate value across tax-advantaged retirement plans and accounts, including 403(b) plans, 401(a) plans, IRAs and governmental 457(b) plans. The MPA would be based on the maximum annual benefit that a defined benefit plan may pay upon retirement under Code Section 415(b). Currently this limit (which is adjusted each year for increases in cost of living) is $205,000 per year.

The basic idea in applying Section 415(b) to the MPA is that an individual's aggregate value across all covered plans and accounts would be converted to an annuity payable at age 62 and in the form of a 100% joint and survivor annuity. The proposal is intended to limit an individual's total balance across covered arrangements to an amount sufficient to finance an annuity of not more than $205,000 per year in retirement (estimated to be roughly $3.4 million for a person age 62 retiring in 2013). However, because the MPA is based on actuarial assumptions tied to DB plan limits, the MPA likely will be far lower than $3.4 million if interest rates return to historic averages and for younger workers.

If an individual's account balances, aggregated across all covered plans and accounts, exceed the MPA, the individual would not be permitted to make additional contributions to covered retirement plans and accounts in the subsequent year. In addition, if the individual were still working, the individual would not be allowed to receive any additional employer contributions in a defined contribution plan or receive any additional accruals under a DB plan. The individual could resume making contributions if:

- the investment performance was such that the updated calculation of the equivalent annuity based on the individual's covered plans and accounts is less than the maximum annuity for DB plans;
- the maximum DB plan limit increases as a result of the cost of living adjustment, which would lead to an increase in the maximum permitted accumulation; or
- a decrease in interest rates led to an increase in the MPA expressed as an account value.

There are several complicating aspects to this proposal. To facilitate compliance, plan sponsors (and perhaps providers) would need to report each participant's account balance and contributions as of year-end, presumably to the participant/accountholder. Presumably, this notification would need to occur promptly after the end of the calendar year. Also, the IRS seemingly would need to publish annual tables showing the age 62 qualified joint and survivor annuity equivalent of different account balances to enable an individual to calculate if the MPA has been reached. Furthermore, individuals might need to report to their employers that the MPA has been reached and that contributions and accruals must cease. In addition, plan sponsors might be required to amend plans to preclude further contributions or accruals when the MPA is reached. It is unclear whether a plan sponsor could provide the missed contribution or accrual in another form (*e.g.,* as a cash payment or deferred benefit under a nonqualified plan).

Write On!

As advisors, we cannot sit by and watch our industry be changed by others. Instead, we need to be the agents of change, helping to ensure not only the retirement security of our clients, but of the next generation of advisors and their clients as well. Join us in this endeavor — help shape the future by contributing your thought leadership in *403(b) Advisor.* We're always on the lookout for articles submitted by NTSAA members like you. Please email John Ortman, Editor, at jortman@asppa.org for more information on how to contribute an article. Thanks!

Eliminate 'Stretch' Payments After Death

Last year, and again this year, a bill was introduced in the Senate which included a provision that would amend the required minimum distribution rules in Code Section 401(a)(9). These RMD rules apply to 403(b) plans, 401(a) qualified plans, 457(b) plans and IRAs.

The current RMD rules require that distributions from these arrangements must commence no later than the employee's "required beginning date" (*e.g.,* after the later of age 70½ or retirement in the case of a section 403(b) plan). If the employee dies prior to the required beginning date, the remaining interest either must be distributed within five years of the employee's death, or it can be "stretched" over the designated beneficiary's life or life expectancy, commencing within one year of the employee's death. If the employee dies on or after the required beginning date, distributions to the designated beneficiary must be made at least

Individuals might need to report to their employers that the MPA has been reached and that contributions and accruals must cease.

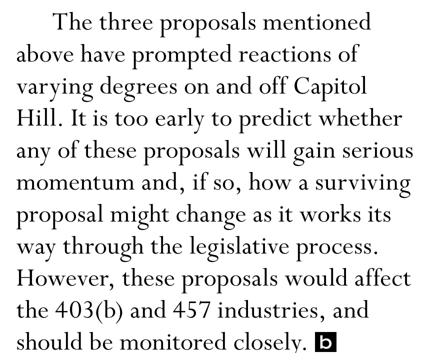
as rapidly as under the method of distribution being used on the date of death. Under this "at-least-as-rapidly" rule, the remaining interest generally can be "stretched" over the remaining life expectancy of the deceased employee or the remaining life expectancy of the designated beneficiary, whichever is longer.

The RMD proposal would require the designated beneficiary to draw down all assets in a 403(b) plan and other select retirement arrangements within five years, subject to exceptions for beneficiaries who are: (1) the surviving spouse of the deceased employee; (2) a child who has not attained the age of majority; (3) disabled; (4) chronically ill; or (5) not more than 10 years younger than the deceased employee. In the case of a child who has not attained the age of majority, the five-year rule would apply as of the date the child attains the age of majority. The new rule would apply regardless of whether the employee dies before or after the required beginning date.

Consolidate Retirement Plans

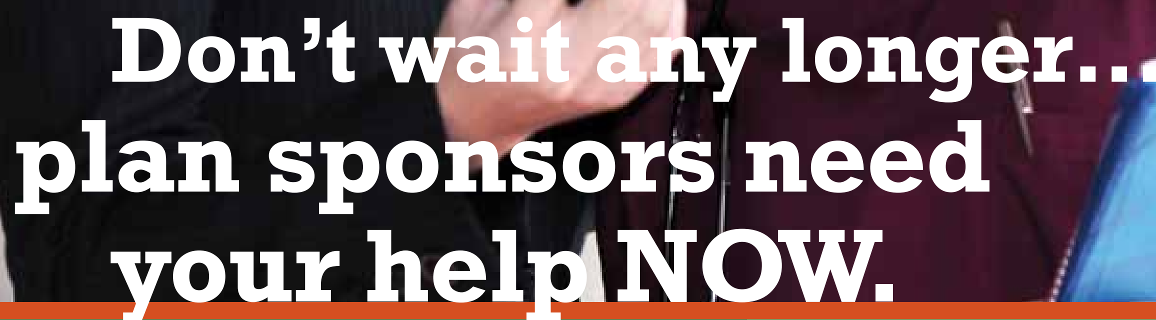
In a letter to the Pensions/Retirement Tax Reform Working Group of the House Ways and Means Committee dated April 11, 2013, the American Institute of CPAs (AICPA) suggested that Congress consider, among other things, a proposal to consolidate and simplify the multiple types of tax-favored retirement plans and the rules governing them. The letter describes the possible simplification measures as including the creation of a uniform employee contributory deferral type plan that would replace 403(b) plans, 457 plans, 401(k) plans and SIMPLE IRA plans. (Certain plan consolidation proposals were made in budgets by President George W. Bush.) The AICPA letter characterizes these plans as four variations of the same plan type, and states that having these variations causes confusion for many plan participants and employers. The letter does not specify the details of the proposed commutation.

Uncertain Outlook



The three proposals mentioned above have prompted reactions of varying degrees on and off Capitol Hill. It is too early to predict whether any of these proposals will gain serious momentum and, if so, how a surviving proposal might change as it works its way through the legislative process. However, these proposals would affect the 403(b) and 457 industries, and should be monitored closely. **b**

Mark E. Griffin is the managing partner at Davis & Harman LLP in Washington, DC and a member of the 403(b) Advisor *editorial advisory board.*



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—Christian Jachym, Director,
Non Profit Account Management team

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Simple Truths

This business is about doing the right things to help people make the best decisions they can, often under challenging circumstances. It's not about transactions.

BY CHRIS DEGRASSI

I had just walked through the side door to our house and stepped into the kitchen, back from a short trip to speak at a conference and meet with some NTSAA members. My youngest son, Colin — always most curious and talkative when he knows it's past his bedtime — wanted a full download on my trip. Where did I go, was the hotel nice, did I meet anyone famous and did I have anything in my bag for him?

In an attempt to take advantage of a teachable moment, I told Colin about the conference — the people I spoke with; how much I learned from the experience; the new

opportunities discovered and new business won. I attempted a response more meaningful than, "Daddy went on a trip."

Immune to the drone of my excellent parenting, Colin was busily looking through my briefcase, searching for the keychain I bought at the airport newsstand. Colin has quite a collection from various airports around the country. He hangs so many on his backpack that we can hear him jingling as he walks home from school.

"Cool!" The newest addition to his collection was a colorful surfboard on a silver chain. The keychain was a hit; the teachable moment lost, I thought.

"Well, you most likely didn't propose to Mom by telephone and she likely didn't respond to you by letter." My elder son, Michael, was looking at his Spanish vocabulary sheet, studying for an exam scheduled for the next day. True to form for a high school freshman, Michael had grunted to acknowledge my return home, but had not looked up from his studies. Or maybe it was the text messages on his phone that held his attention.

"What?" I asked Michael with a smile.

"I heard that in a movie once." Michael said, looking up at me. "It means that if you have something important to say to someone, you need to do it face to face." After a brief pause, he went on. "I mean, that's why you travel, right, Dad? You can't expect to build a business unless you get out and meet with people. Why would they want to do business and give you their money if they don't know you?"

Colin chimed in: "When I grow up I'm going to make a lot of money and help people." His ever-present grin grew bigger as he spoke. "And I'll have a Lamborghini to drive when I'm not driving my kids to soccer practice in my minivan."

The boys went on to argue the merits of driving a Lamborghini versus a Corolla. Michael focused on gas mileage, insurance costs and better things to do with your money; Colin was smitten with the thought

"When I look at the criticism directed at the financial services industry, I can't help but wonder if part of the problem is that the critics don't understand that being a financial advisor is a people business."

of going fast. I listened with a smile, acknowledging the valid points on both sides of the palaver, knowing that Colleen and I had two very special boys started on the right path in life.

I share this story because I'm a proud Dad, but also because it struck me how casually and clearly my boys had expressed very simple truths of life that we should all remember and apply to our business dealings. Life — and business — is all about people. And success is built through our relationships and the trust we earn by doing the right thing to help others.

In business-speak we sometimes refer to the ideal outcome as a "win-win" — the sweet spot where both parties benefit from a transaction. But our business — helping people prepare for and manage a secure and comfortable lifestyle beyond work — isn't about a transaction or a win-win outcome. Our business isn't about transactions at all, but about doing the right things to help people make the best decisions they can, often under challenging circumstances.

When I look at the criticism directed at the financial services industry, I can't help but wonder if part of the problem is that the critics don't understand that being a financial advisor is a people business. If your point of view is predicated on the notion that the financial services industry is a product- and transaction-focused business, then it stands to reason that you would focus on perceived deficiencies in products and transactions, and the regulatory regimens that govern them. The result is the commoditization of our industry. Or, as a colleague recently said, "We're turning our industry into concentrated frozen orange juice that babies buy and sell on smart phone apps from their cribs."

So as it turns out, the teachable moment was not lost after all. It's just that the lesson was for me! ■

Chris DeGrassi is NTSAA's Executive Director.

The ACA's New Rules for 501(c)(3) Hospitals

BY KIMBERLY FLETT

Advisors should be knowledgeable about the important new rules affecting their 501(c)(3) hospital clients under the Affordable Care Act.

The Affordable Care Act (ACA) affects many employers, including those in the nonprofit sector. Although there are numerous provisions under the ACA, this article focuses on one key area: 501(c)(3) hospitals.

Section 501(r) of the ACA requires 501(c)(3) hospitals to meet four general requirements:

1. establish a written financial assistance and emergency medical care policy;
2. limit amounts charged under the hospital's financial assistance policy for vital and emergency care;
3. before imposing aggressive collection policies, determine if an individual is eligible for financial assistance;
4. for tax years beginning after March 23, 2012, conduct a community health needs assessment.

The ACA imposes a new excise tax if these requirements are not met.

An organization qualifying as a hospital under 501(r)(2) of the ACA is defined as one that is required by a state to be licensed or that provides hospital care as its primary purpose and qualifies for exemption under 501(c)(3). The new requirements apply to each facility maintained by the hospital organization.

Financial Policy

The written financial policy requires the following:

- the criteria for establishing the need for financial assistance, including free or discounted care;
- the method used to calculate amounts charged to patients;
- the methods used to obtain financial assistance;
- publicity in the community; and
- collection methods.

A hospital must also have a policy for the method of providing care under emergency medical conditions, regardless of a patient's eligibility under the financial assistance policy.

Collection Methods

A hospital organization must not use extreme collection methods for payment until an assessment has been made whether the individual qualifies for assistance under the organization's financial assistance policy. These include lawsuits, liens, arrests or other aggressive policies. Furthermore, the organization must limit amounts charged for emergency medical care for those eligible for assistance and these amounts cannot exceed amounts billed to those with insurance coverage. The rates may equate the average of three commercial vendors or Medicare rates.

Community Health Needs Assessment

Every three years a hospital organization must conduct a community health needs assessment (CHNA). The purpose of this assessment is to determine community health needs and apply an effective course of action to ensure that health services are sufficient. Data should be collected from a variety of sources, including local public health agencies and not-for-profit organizations.

This information is required to be disclosed on Form 990 (see below), including the description of how the health needs are being addressed, and which needs are not being addressed and why. A $50,000 excise tax will be imposed on a hospital organization that fails to meet this requirement.

Schedule H Added

A new Schedule H was added to Form 990, "Return of Organization Exempt from Tax," for hospitals to report information under the CHNA requirement. These enhancements were implemented to Form 990 for the filing year 2010 and further updated for 2011. If a hospital is required to file Form 990, Schedule H, the most recent audited financial statements are required to be attached to the return.

Conclusion

For nonprofits, compliance issues affecting their medical plans can be just as important as those affecting their 403(b) and other qualified retirement plans. A good knowledge of the requirements under the Affordable Care Act will give practitioners knowledgeable insight into some of the important new rules affecting their clients. It is important that nonprofit clients consult with their legal, accounting and medical advisors to understand the full impact of the new issues created by the Affordable Care Act. **b**

For nonprofits, compliance issues affecting their medical plans can be just as important as those affecting their 403(b) and other qualified retirement plans.

Kimberly Flett, CPA, QPA, QKA, is the lead director of the retirement plan design and administration department of SS&G. She has served on several ASPPA boards, including the 403(b) Advisor *editorial advisory board.*

Playing with Distance

BY ART MARKMAN

Meet 'construal level theory,' which suggests that when people are far from something, they think about it abstractly, but when they are close to it, they treat it specifically.

When you're advising people about their retirement, you're constantly dealing with problems of distance. On the one hand, retirement is off in the future. It's hard for people to think clearly about what their needs will be at that stage of life. On the other hand, their current life is lived in rich detail. People know exactly how they would spend money that they have right now.

For the past decade, psychology researchers have explored construal level theory. This theory, which was first posited by Yaacov Trope and Nira Liberman, suggests that when people are far from something, they think about it abstractly, but when they are close to it, they treat it specifically. This theory points out that distance can be distance in space, time (events in the far future or distant past), or in social relationships (people are closer to themselves than to other people).

When thinking about retirement, this means that a person who is planning for their life a decade or more in the future is focused on general aspects of who they will be. They focus on broad necessities like housing, but not on all of the daily details like new clothes, birthday gifts, vacations and car repairs. However, these details become clear when thinking about present day life. One key reason why people have difficulty saving for the future is that it is hard to take money away from all of the specific needs that arise right now in order to provide for a vague and hazy future.

In your role as an advisor, it can be helpful to play around with people's perception of distance to help them prepare for the future.

Perhaps the most obvious thing you can do is to decrease the distance to the future. The best way to do that is to have people visualize specific days they will experience after retiring. Have them think about the activities

they want to engage in, the presents they want to buy, the vacations they want to take, and the cars they want to drive. Having people think about these details will draw them closer to their lives in retirement, and will help them to realize the kind of finances they will need to enjoy that future.

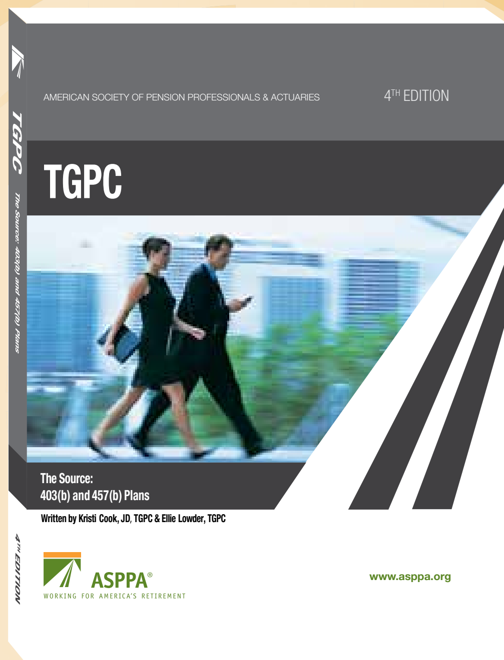
Less obviously, it can be helpful to increase people's distance from their own present. An easy way to do that is to have people imagine giving retirement advice to another person who is just like them. By thinking of themselves from this social distance, it becomes easier to gloss over all of the specific expenses that make people reluctant to invest in their retirement.

Another way to increase distance from the present is to have people think about the amount of money they would invest in their retirement in six months or a year. Even the distance of a year can get people to think beyond their current needs. Then have them actually commit to those investments.

> ***"When you find a discussion getting mired down in specifics, find a way to increase the distance to help people think more abstractly."***

The central lesson is that you should start to pay attention to the ways that distance affects how people talk about their lives. When you find a discussion getting mired down in specifics, find a way to increase the distance to help people think more abstractly. When people are not focusing on the fine details, try to bring them mentally nearer to the event. **b**

Art Markman, PhD, is a professor of Psychology and Marketing at the University of Texas and director of the program in the Human Dimensions of Organizations. He is the editor of the scientific journal Cognitive Science *and author of the books* Smart Thinking *and* Habits of Leadership.



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VALUE PROPOSITION

Add 'Estate Planner' to Your Toolbox

BY CLARK KENDALL

As a client ages and amasses wealth, estate planning becomes an increasingly important element of his or her overall wealth management strategy.

In today's rapidly changing retirement planning marketplace, 403(b) and 457 advisors should strongly consider adding the Accredited Estate Planner (AEP) designation to their list of credentials. In several key ways, becoming an AEP can add value to the services you provide to retirement plan participants at charitable institutions, school districts, and higher education institutions.

Before we get into the professional advantages of becoming an AEP, let's take a look at the two most significant new realities of retirement in the 403(b) and 457 marketplaces.

Greater Longevity

Increased longevity is by far the most significant new retirement reality. In our grandparents' generation, life expectancy was in the 70s. Now, for a married couple age 65, there is a 50% chance that one spouse will live past his or her 90th birthday. This stretches the time horizon for clients who are thinking about when to retire.

The Economy

The other new retirement reality is the fallout from the recent recession and sluggish economic recovery. Charitable organizations have been hurt disproportionately by the economic downturn, due to a sharp drop-off in charitable donations. Meanwhile, K-12 school districts and higher education institutions haven't been immune from economic hardship. University of Maryland professors, for example, haven't received a raise in three years.

An Added Skill

What does it take to become an Accredited Estate Planner? To obtain this designation from the National Association of Estate Planners and Counsels (NAEPC), you must be a Certified Public Accountant (CPA), Certified Financial Planner (CFP), Certified Life Underwriter (CLU) or an attorney. You also have to demonstrate at least five years of experience in estate planning. In addition, you must complete additional courses offered by NAEPC and take a cumulative exam administered by the association.

Why should a 403(b) or 457 advisor invest the time and money needed to become an Accredited Estate Planner? Because there is a critical intersection between estate planning and retirement planning. Estate planning isn't just about what happens after we die; it's also about what happens during our lifetime, especially if we have substantial wealth.

From a tax perspective, there are income, capital gains and estate taxes to consider. From a nonfinancial perspective, there could be many factors involved. For example, with today's increasing number of blended families resulting from divorces and second marriages, a client may have issues related to financial treatment of children from a second marriage.

Within a retirement plan, beneficiaries are separate from the ones listed in the client's will. Let's say that when your client fills out your 403(b) application, he or she lists children X and Y from a second marriage. But his or her will leaves the estate to children A and B from the first marriage. Guess which legal instrument takes precedence? The retirement plan.

But that's just the beginning. The relationship between retirement planning and estate planning can get even more complicated in blended families. For example, if your client dies and names his wife as the beneficiary of his 403(b), she can roll those assets into her IRA account that may name only her children. When she dies, all of your wealth goes to the beneficiaries she's listed — which may not include your client's children.

One of the key estate planning questions that ties into retirement planning is, "To Roth or not to Roth?" In other words, should a client be putting assets into a tax-deferred Roth IRA or not? What are the short- and long-term financial implications of deferring taxes on these assets?

Let's look at a specific example. I advise a husband and wife who are 80 years old and have accumulated a $2 million estate. They have $500,000 in an IRA account. For them, it made sense to convert the $500,000 IRA to a Roth IRA. Of course, they had to pay income tax on the $500,000, roughly $140,000, as if it were income. But once the money is in the Roth account, they no longer have to take the required minimum distribution that they would have had to take each year from the IRA (3.5% per year beginning at age 70).

As a client ages and amasses wealth, estate management becomes an increasingly important element of his or her overall wealth management strategy. By becoming an Accredited Estate Planner, you will better understand the retirement planning advantages of Roth IRAs and the estate planning implications of naming beneficiaries in retirement plans. Before your client checks any boxes, you can make sure that they fully understand the ramifications of those choices. ■

> ***"There is a critical intersection between estate planning and retirement planning."***

Accredited Estate Planner® Designation

The Accredited Estate Planner® designation is awarded by the National Association of Estate Planners & Councils to recognized estate planning professionals who meet special requirements of education, experience, knowledge, professional reputation, and character.

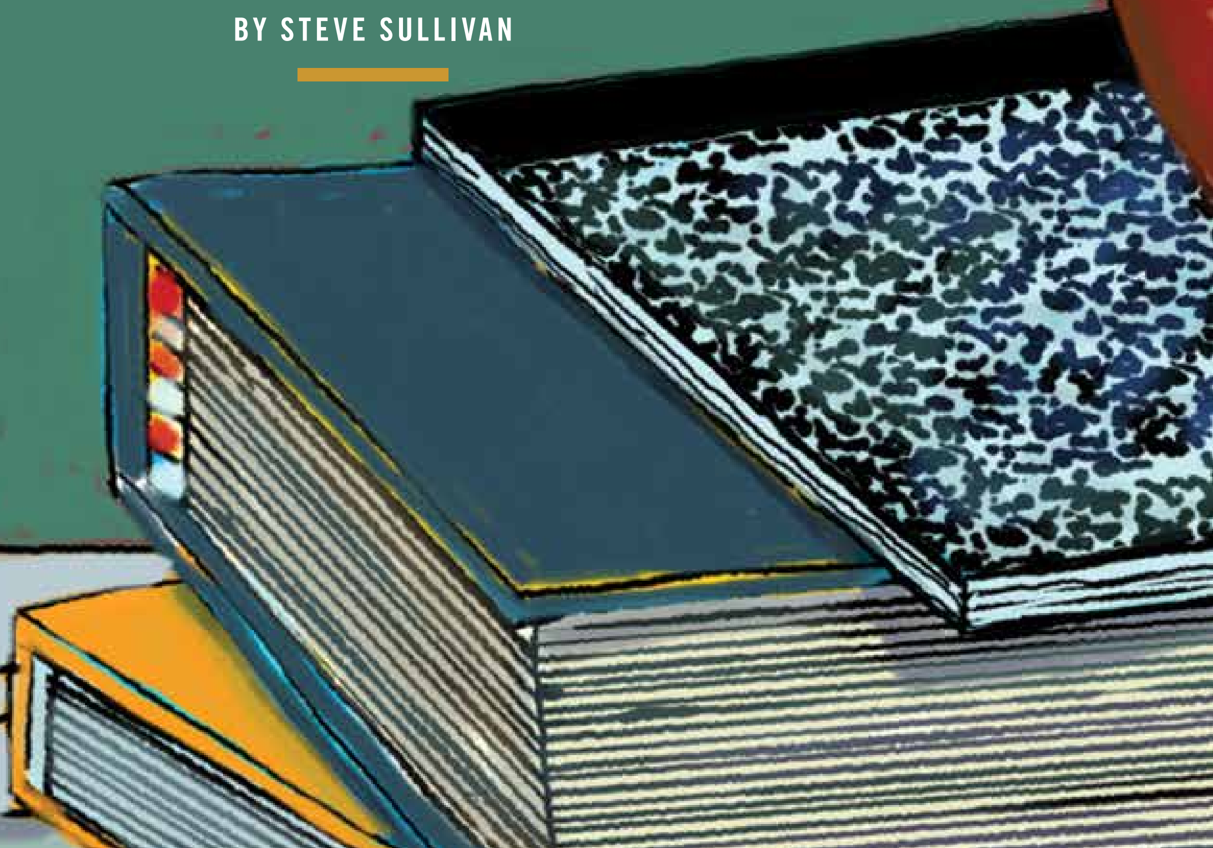
The AEP® designation is available to attorneys, Chartered Life Underwriters, Certified Public Accountants, Certified Trust and Financial Advisors, Chartered Financial Consultants, and Certified Financial Planners®. More information is available at http://www.naepc.org/designations/estate-planners.

Clark Kendall, founder of Kendall Capital Management in Rockville, MD, has more than 20 years of experience in investment management and wealth management strategies. He is one of a select few professionals in the world who has earned the triple designations of Chartered Financial Analyst, Chartered Financial Planner and Accredited Estate Planner.

State teacher retirement systems all across the country are in trouble. Advisors need to understand what their states are doing to fix the problem.

The Pension Underfunding Threat

BY STEVE SULLIVAN



These days, the three-legged stool is something that's more likely to turn up on an episode of "Antiques Roadshow" than it is to serve as a metaphor for comfortable retirement.

Not one of its legs is without a wobble: Defined benefit pensions are pretty much history. Social Security will start experiencing shortfalls at about the same time the number of retiring Baby Boomers reaches its peak. And private savings in 403(b)s and 401(k)s are subject to the vagaries of markets and the economy. No wonder that a National Institute of Retirement Security (NIRS) study released earlier this year found that 85% of Americans — not just teachers and government employees — are worried about whether they'll be able to retire.

Teachers have always been particularly fortunate. The mainstay of their retirement has been a usually generous defined benefit state teachers' retirement system (STRS) that they supplemented with defined contribution plans such as 403(b) and 457 accounts and personal savings. Now, even those defined benefits, at least in their traditional form, may not be there for many future public school retirees.

> *In states where pension funding is on the negotiation table, teacher demands for salary increases have often been countered with promises of better retirement benefits down the road.*

The reasons for this are varied and complicated. Since most STRS are DB plans, their funding is determined by complex actuarial formulas based on myriad facts and assumptions:

- How many people are in the system now?
- How many will there be next year, the year after that, and so on?
- Where will the money come from? How much will come from contributions? From investments?
- How will these investments perform?

That's a lot of uncertainty that has to be tamed by actuaries in order to provide a defined benefit.

Not surprisingly, recent economic downturns have taken a severe toll on all states' budgets, and not just their retirement plans. And even when times are good, states don't always fund their pension plans to recommended levels or take advantage of booms to build a financial cushion against the inevitable bust. After all, those obligations are long-term and usually way down the road. As long as states have enough money on hand to pay their current retirees, it's often tempting to use those funds that should be covering future retirees for something else more immediate and, perhaps, more politically attractive.

In states where pension funding is on the negotiation table, teacher demands for salary increases have often been countered with promises of better retirement benefits down the road.

Widening Gap

According to "Public Pension Pressure in the United States," a 2011 paper written by the Wharton School's Olivia S. Mitchell, "50 states together owed $117 billion to their pension plans in 2009 but in fact only contributed $73 billion. Contribution shortfalls of this nature have persisted because state DB plans follow rules set by their legislatures rather than by a centralized accounting authority; this permits politicians to adjust payment targets in times of fiscal stringency."

In 2012, the Pew Trust Center on the States updated a previous report, "The Widening Gap," that quantified the disconnect between what state pensions were promising and what their funding would allow them to provide. It reported the overall pension gap as $757 billion.

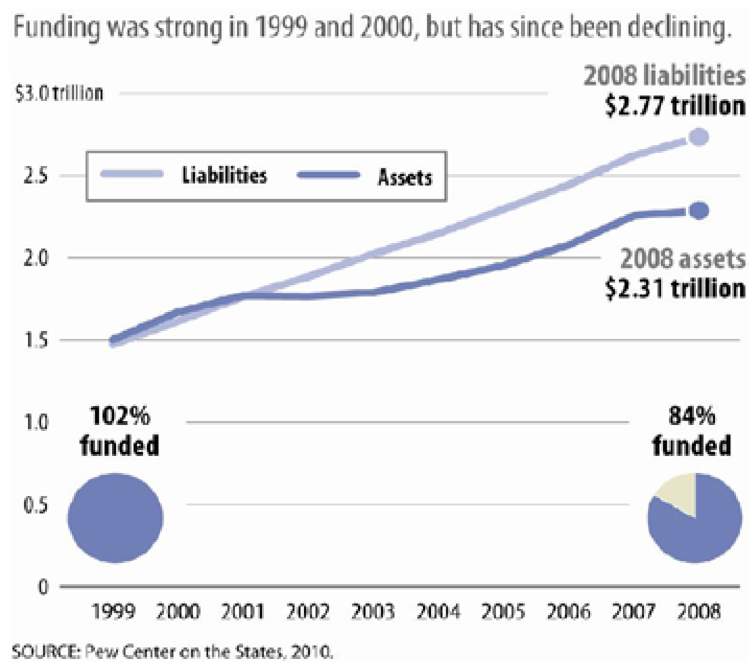
"States continue to lose ground in their efforts to cover the long-term costs of their employees' pensions and retiree health care," the report concluded, "due to continued investment losses from the financial crisis of 2008 and states' inability to set aside enough each year to adequately fund their retirement promises. States have responded with an unprecedented number of reforms that, with strong investment gains, may improve the funding situation they face going forward, but continued fiscal discipline and additional reforms will be needed to put states back on a firm footing."

The Pew report's scorecard (see Fig. 1) used the states' own actuarial assumptions — usually an 8% rate of return on investments — to evaluate their unfunded liability. Under those criteria, states such as North Carolina, South Dakota, Washington and Wisconsin were funded at 95% or better. Others at the bottom of the rankings were Connecticut, Illinois, Kentucky and Rhode Island, with funding below 55%. The majority of the states in between need improvement, the report concluded.

Many experts question, however, whether an 8% ROI is realistic in today's economic environment, preferring a more realistic 3.5% or 4% (see Fig. 2). But even a more moderate assumption of 6.25% can radically alter the results. New York, for instance, using an 8% assumption, projects a funding level of 101%, making it a star performer. Drop the assumption to 6.25%, however, and the Empire State is only 87% funded — better than most. But use the worst-case scenario and the ratio drops to 65%, putting it in the "needs improvement" territory.

The Pew report also assumes that a funding ratio of 80% represents a fiscally healthy plan. Not so fast, warns the American Academy of Actuaries. "A funded ratio of 80% should not be used as a criterion for identifying a plan as being either in good financial health or poor financial health," it said in an issue brief published last year. "No single level of funding should be

FIGURE 1: HOW DID WE GET HERE?



In 2000, nearly half the states were fully funded. In 2008, only four states could make that claim.

Source: The Pew Charitable Trust

FIGURE 2: RATE OF RETURN ASSUMPTIONS MATTER

State:	**New York**	Plans:	**ERS, PFRS**	
Return Assumption	**Assets**	**Liabilities**	**Percent Funded**	**Unfunded Liability**
8.00%	$148,861,000	$146,733,000	101.45%	-$2,128,000
6.25%	$148,861,000	$171,879,765	86.61%	$23,018,765
3.50%	$148,861,000	$229,732,022	64.80%	$80,871,022

State:	**Illinois**	Plans:	**SERS, SURS, TRS**	
Return Assumption	**Assets**	**Liabilities**	**Percent Funded**	**Unfunded Liability**
8.50%	$64,012,414	$117,391,324	54.53%	$53,378,910
6.25%	$64,012,414	$143,383,415	44.64%	$79,371,001
3.50%	$64,012,414	$191,644,211	33.40%	$127,631,797

Source: The Pew Charitable Trust

identified as a defining line between a 'healthy' and an 'unhealthy' pension plan. All plans should have the objective of accumulating assets equal to 100% of a relevant pension obligation, unless reasons for a different target have been clearly identified and the consequences of that target are well understood."

Accelerated Change

So what are states to do? They have options, but they're limited by a very important fact: Most state teacher pension systems are contracts, negotiated between school systems and teachers, usually through their unions, and ratified by state legislatures. "Once benefits are put in place, it's a contract and it's very difficult to work around it," says Dave Ellingson, research analyst at Trust Builders in Dallas, OR. "When there's an abrupt change in the situation — like the crash of 2008 — that does not negate a contract just because the STRS can't perform. The employer is on the hook for making up the shortfall."

So states and school systems can't just liquidate a troubled plan the way a private company can, leaving participants to be covered by the Pension Benefit Guaranty Corp. They have to either raise more money or cut benefits, and they have to do it by tinkering around the edges.

"Changes include reducing the percentage of crediting, trimming back early retirement ages so you're not able to retire at 55 with full benefits as you could before, and using more stringent actuarial valuations of the plan," says Edward Dressel, president of Trust Builders. Dressel's company creates software that helps advisors illustrate retirement benefits for more than 500 public pension plans across the country. He says that keeping up with the pace of change has created a couple of full-time jobs at his firm.

"When I bought the company in 2007 I could keep up with the changes pretty well," he says. "But because of what happened in 2008, I started seeing a lot of new changes coming in. In 2010 I hired a full-time person just to keep track of the changes and even he started falling behind. I hired another analyst in 2011. The volume of changes is overwhelming."

"State retirement systems across the country are making changes," concurs Ellie Lowder, TGPC, TSA Training and Consulting Services in Tucson, AZ. "Many of them are trying to move away from a defined benefit plan and substitute a defined contribution plan so the risk is on the employees rather than the employer." But even if they decide to do that, the contract won't allow the change to apply to participants already covered under the plan. They can apply only to new hires.

"Another option to reduce the unfunded liability is the cost-of-living adjustment (COLA)," says Ellingson, "which is usually controlled by the state legislatures. Most systems are tied to the consumer price index. So if you're a retired teacher with a $30,000 annual retirement benefit, let's say the COLA is 5%. Some systems grant a maximum of up to 3% but guarantee a minimum of 1%. That means retirees can depend on a COLA but it may not match the inflation rate in those years when it's high. But even in years when there is no inflation, they'll still get an increase of 1%."

No Easy Choices

However they deal with it, pension underfunding is an issue that states can no longer afford to ignore. But whatever they do usually ends up being politically unpopular and wildly controversial. In New York, Gov. Andrew Cuomo (D) has proposed a plan that would replace the traditional defined benefit plan for new employees with a defined contribution plan and reduce their benefits, bringing down the wrath of public employee unions.

According to the *Chicago Tribune*, Illinois' $96.8 billion STRS pension debt is the worst in the country. Gov. Pat Quinn's (D) plan to freeze the annual 3% cost of living increase for three years is drawing fire from politicians, unions and pensioners alike.

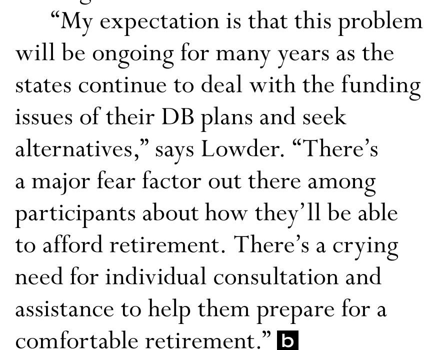
And in California, critics charge that Gov. Jerry Brown's (D) hard-fought pension reforms — increasing the retirement age for new employees, capping the annual payout at $132,120, eliminating numerous abuses of the system and requiring workers who aren't contributing half of their retirement costs to pay more — are too little, too late, and do nothing to solve the growing problem.

And similar controversies rage in other states that are trying to address the problem in their own ways.

Advisors Have a Role

Though 403(b) advisors can't do anything to solve the problems of underfunded STRS, they can and should understand how their systems work. Educating clients about what part of their retirement will be funded by their defined benefit pension (as well as Social Security and their voluntary contributions) is a big part of the service they provide. Vendors and providers can be good sources of this information, as well as the STRS themselves. Lowder suggests that advisors get a copy of the state system's employee benefits handbook and use it to gain a complete understanding of how the system works, including how to calculate a person's benefits.

Advisors should be aware, she adds, that if states shift from DB to DC plans for new employees, those state pension benefits will no longer be determined by the traditional actuarial formula, making them even harder to calculate.



"My expectation is that this problem will be ongoing for many years as the states continue to deal with the funding issues of their DB plans and seek alternatives," says Lowder. "There's a major fear factor out there among participants about how they'll be able to afford retirement. There's a crying need for individual consultation and assistance to help them prepare for a comfortable retirement."

Steven Sullivan is a freelance writer in Baltimore, MD, and former editor of 403(b) Advisor.

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An Overview of Retirement Income Strategies

BY STEVE HANSON AND RICHARD FORD

Guaranteed income, while very important, does come at a cost to the client. An analysis shows that these products provide much more value to the client when used as part of a customized income strategy than when used on a stand-alone basis.

With 10,000 Americans turning 65 every day, there is no shortage of potential clients asking for your help in determining if, when and how they will be able to retire. Sixty-one percent of Baby Boomers say they're more afraid of running out of money than they are of dying. While some who reach retirement age may be opting to continue working so they can rebuild savings impacted by the recession, many are looking to you to help them retire in the lifestyle they've worked so long for and desire.

Retirees are asking:

- Have I saved enough money to live the lifestyle I want?
- Will my money last as long as I live?
- How can I maintain control of my portfolio and make changes when I need to?

Advisors tell us they are concerned about:

- Increasing demand for their time, advice and personalized solutions.
- Not having the knowledge or customized solutions to meet client needs over an uncertain period of time.
- Growing their practice as retirees draw down on their savings, rather than contribute to them.

> *While the rankings can help advisors determine the relative overall effectiveness of the various strategies, there is no single strategy that is right for all clients.*

Making the transition from retirement accumulation planning to retirement income planning can be a challenge for even the most experienced advisor. While there is a nearly limitless list of strategies for providing income from a client's investments, there is a smaller number of retirement income strategies commonly utilized by independent financial advisors. This article compares some of the more commonly used strategies, including:

- Variable Annuity with a Guaranteed Lifetime Income Rider (both a "standard surrender" variable annuity and a "short surrender" variable annuity)
- Fixed Indexed Annuity with a Guaranteed Lifetime Income Rider
- Time-Segmented Income Strategy
- Market-Responsive Withdrawal Program
- Customized Income Strategy that combines: (1) an immediate lifetime income annuity with a market-responsive withdrawal program; and (2) a variable annuity with a guaranteed lifetime income rider (both "standard surrender" variable annuity and a "short surrender" variable annuity) with a market responsive withdrawal program.
- Longevity Insurance Strategy that combines a market-responsive withdrawal program with a deferred lifetime income annuity.

Utilizing financial market and other economic data dating back to 1926, we tested each scenario using both back-testing and Monte-Carlo simulation methodologies. We then compared the relative advantages and disadvantages of these strategies from the perspective of both the client and the financial advisor and ranked the strategies based on key criteria to produce an overall report card on each strategy. Key considerations of a retirement income program from the client's perspective are:

- Amount of income generated

> **61%** *of Baby Boomers say they're more afraid of running out of money than they are of dying.*

- Amount of income guaranteed for the client's lifetime
- The residual value of the account at the end of the desired timeframe (legacy)
- The liquidity of the assets throughout the income time horizon

The financial advisor's primary goal, of course, is to ensure that the client needs relative to the factors mentioned above are met. That being said, no matter how effective an income strategy may be, it will not gain acceptance in the advisor community unless the advisor can implement it efficiently and be fairly compensated for the services that they provide the client. Therefore, the following additional factors must be considered by the financial advisor:

- Ease of implementation (both initially and ongoing)
- Income generated by the strategy for the financial advisor (both up-front and overall)

Following are descriptions of these strategies.

Variable Annuity with a Guaranteed Lifetime Income Benefit (GLIB)

There are many flavors of variable annuities with lifetime income riders, but most of them provide a guaranteed rate of growth to the "benefit base" prior to the client taking income and then guarantee income equal to a percentage of the benefit base even if the client's account value should fall to zero. These contracts typically also have a "step-up" provision that allows the benefit base to increase if the contract value exceeds the benefit base. These contracts have been very popular in recent years and account for a very large portion of variable annuity sales.

The two forms of contracts included in this analysis are the "standard surrender" contract and the "short surrender" contract. The standard surrender contract generally has a longer surrender period (typically seven years) and lower contract expenses as compared to the short surrender contract. Also, the standard surrender contract will typically pay a higher upfront commission and either no asset-based trail or a lower asset-based trail than the short surrender contract.

Fixed Indexed Annuity with a Guaranteed Lifetime Income Benefit (GLIB)

This is very similar to the variable annuity strategy, but the funding vehicle is a fixed indexed annuity rather than a variable annuity. We did not perform simulations for this strategy — mainly due to the difficulty of modeling FIA caps, spreads and/or participation rates. These mechanisms are an integral part of determining the return on the contract, but they are not tied directly to any index or asset class that can be modeled. While, generally speaking, caps, spreads and participation rates are related to current interest rates and market volatility, they are ultimately set at the discretion of the insurer.

That being said, the results of the variable annuity products can be used as a proxy for the results of the FIA products. FIAs have a lower upside and a lower expected return than VAs, but they also don't have as much of a downside. Thus, one would expect the income and residual account balance for the FIA to be lower than the variable annuity for the median and 75th percentile cases and equal to or better than the variable annuity for the 25th percentile cases.

Time-Segmented Withdrawal Strategy

This strategy was developed to address one of the key issues with a traditional systematic withdrawal program — sequence of returns risk. In this strategy, the client divides their assets into segments (typically with 5, 10, 15, 20, and 25-year time horizons). As the time horizon of each segment is increased, so is the risk profile of the segment. At the inception of the strategy, the client invests enough money into a five-year SPIA or a money market fund to provide them with five years of income. Every five years, a segment is liquidated and the proceeds are used to purchase another five-year SPIA or money market fund, thus providing an additional five years of income. The theory is that the more aggressively invested segments have longer time horizons and are, thus, more likely to produce returns equal to their long-term historical averages.

Market-Responsive Withdrawal Program

This strategy is an adaptation of a traditional inflation-adjusted withdrawal strategy. The client invests their assets in a moderate asset allocation portfolio and takes systematic withdrawals from the portfolio. Each year, the client's withdrawals are automatically adjusted upward or downward based on the performance of the account in accordance with the predetermined rules. By implementing these rules, the initial withdrawal rate can be dramatically increased as compared to a traditional systematic withdrawal program without decreasing the probability of success.

Customized Income Strategy

The Customized Income Strategy combines a Market-Responsive Withdrawal Program with a source of guaranteed lifetime income (either a Lifetime Income Annuity or a Variable Annuity with a Guaranteed Lifetime Income Benefit). The primary tenet of this strategy is that every client should establish a "floor" of guaranteed income to meet their essential income requirements. To the extent that this floor is not covered by Social Security, pensions or other guaranteed sources, the guaranteed income product (either an immediate lifetime income annuity or a variable annuity with a guaranteed lifetime income benefit rider) is used to fill the gap. For the client's non-essential income, a market-responsive withdrawal strategy is utilized.

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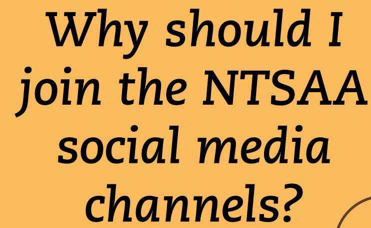

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Longevity Insurance Strategy

The Longevity Insurance Strategy is designed for the client who is reluctant to commit a significant portion of their retirement assets to a guaranteed income product due to liquidity or expense factors. In this strategy, the client initially generates all of their income from a Market-Responsive Withdrawal Program. However, the client also allocates a small portion of their assets to a deferred lifetime income annuity that will begin paying the client a stream at some point in the future (typically 20 years later). Because the client has a guaranteed income stream that they know will commence in 20 years, they can confidently withdraw more income from their Market-Responsive Withdrawal Program than they would otherwise. Also, the cost of the deferred income annuity is significantly less than the cost of an immediate income annuity.

Testing Results

Variable Annuity with a Guaranteed Lifetime Income Benefit (GLIB)

The stand-alone variable annuity with a guaranteed income rider ranked fairly low in terms of its ability to generate income for the client over the long term. This is due to the fact that compared to the non-guaranteed solutions that were tested; there is a relatively high cost to implement such a strategy due to the variable annuity contract and rider expenses. These expenses eroded the client's purchasing power over time in our simulations. For similar reasons, this strategy ranked in the lower third for liquid account value and residual account value. The primary appeal of such a solution is the ease of implementation, due to the fact that it is a "single application" solution. Also, the potential up-front compensation to the advisor was the highest among the alternatives, though total income to the advisor over the client's lifetime was actually the lowest.

Time-Segmented Withdrawal Strategy

The time-segmented withdrawal strategy ranked in the top third of the strategies tested in terms of total purchasing power provided to the client; however, this strategy provides little in the way of guaranteed lifetime income. Residual account value and liquid account value were low due to the fact that a large portion of the account value is initially invested in a period-certain income annuity to provide for the first five years' worth of income. Every five years, another substantial portion of the account is liquidated and used to purchase another period-certain annuity, further eroding liquid account value and residual account value. From the advisor's perspective, this strategy ranked the lowest in terms of ease of implementation and up-front compensation, though it was in the middle of the pack in terms of total advisor income over the life of the client.

Market-Responsive Withdrawal Strategy

The market-responsive withdrawal program ranked very high in terms of the purchasing power provided to the client, though it does not provide the client with any guaranteed lifetime income. Because it is a relatively inexpensive strategy to implement and the assets remain in accounts that are free from withdrawal penalties, this strategy ranked highest in terms of residual account value and liquid account value. While this strategy requires an annual review process, it still ranked relatively high in terms of ease of implementation. The primary downside from the advisor's perspective is that it provided little up-front compensation, but it did rank highest in terms of overall income to the advisor over the life of the client.

Customized Income Strategy

The customized income strategies, whether the guaranteed portion of the client's income was provided by an income annuity or a variable annuity with a lifetime income rider, performed similarly in our tests. They ranked in the lower half in terms of total purchasing power — again attributable to the additional costs associated with providing guaranteed income. For that additional cost, the customized income strategies did provide a high level of guaranteed lifetime income that was "customizable" to meet the specific client's needs. These strategies also ranked high in terms of residual account value and liquid account value because only a portion of the client's assets was tied up in products with surrender restrictions and higher costs. The customized strategy is somewhat more difficult to implement, as it does require the sale of multiple products, but it is less complex than the time-segmented withdrawal strategy. Finally, these strategies ranked in the upper half in terms of initial and total advisor income — indicating that the advisor is fairly compensated for the services being provided.

Longevity Insurance Strategy

The longevity insurance strategy provided the most total purchasing power and ranked in the middle of the pack in terms of guaranteed lifetime income. It also ranked in the middle in terms of residual and liquid account value, ease of implementation and initial and total advisor income.

Strategy Report Card

The report card shown in the chart summarizes the results of our testing based on the following criteria:

- *Purchasing Power* — the amount of income that the strategy can reliably provide the client
- *Guaranteed Lifetime Income* — the amount of guaranteed lifetime income the strategy produces
- *Residual Account Value* — the residual value of the account at the end of the desired timeframe (legacy)
- *Liquidity* — how easy will it be for clients to access their money should the need arise during the income time horizon
- *Ease of Implementation* — a measure of the ease with which an income strategy can be implemented (both initially and ongoing)

The strategies were ranked (1st through 8th) based on each of the criteria and provide an average overall ranking for each.	Purchasing Power	Guaranteed Lifetime Income	Residual Account Value	Liquid Account Value	Ease of Implementation	Advisor Income (Up Front)	Advisor Income (Total)	**Average Ranking**
Market-Responsive Withdrawal Program	2	7*	1	1	3	7	1	**3.14**
Customized Income Strategy with Variable Annuity (Standard Withdrawal)	5	2*	2	2	6*	3	3	**3.29**
Customized Income Strategy with Variable Annuity (Short Withdrawal)	6	2*	3	3	6*	4	2	**3.71**
Longevity Insurance Strategy	1	4	5	4	4*	5	4	**3.86**
Customized Income Strategy with Lifetime Income Annuity	4	1	4	6	4*	6	6	**4.43**
VA with GLIB – Standard Surrender	7	7*	6	5	1*	1	8	**5.00**
VA with GLIB – Short Surrender	8	5*	7	7	1*	2	7	**5.29**
Time-Segmented Withdrawal Strategy	3	6*	8	8	8	8	5	**6.57**

*Tied

- *Advisor Income (Up Front)* — compensation received up front for the work done to ensure that clients have income streams that meets their needs
- *Advisor Income (Total)* — cumulative compensation received for the work done to ensure that the client has an income stream that meets their needs given a time horizon

Conclusions

While the rankings in the previous section can help advisors determine the relative overall effectiveness of the various strategies, there is no single strategy that is right for all clients. Also, just because a strategy has a high overall ranking that does not necessarily mean that it will be appropriate for any given client. For example, the stand-alone Market-Responsive Withdrawal Strategy — despite its high overall ranking — would not be appropriate on its own for a client with a need for guaranteed income. Conversely, a Customized Income Strategy that includes a guaranteed income component would not be appropriate for a client who has enough guaranteed income coming from Social Security or pensions.

One point that is clear is that guaranteed income, while very important, does come at a cost to the client. It will be very rare to find a situation that justifies putting all of the client's assets into a guaranteed income product such as a variable annuity with a guaranteed lifetime income benefit — the cost of the benefit is just too high. As shown in our analysis, these products provide much more value to the client when used as part of a Customized Income Strategy than when used on a stand-alone basis.

When implementing a Customized Income Strategy, the choice of the guaranteed income component (lifetime income annuity versus variable annuity with guaranteed lifetime income benefit) has little effect on the outcome for the client. The Lifetime Income Annuity, in general, will provide slightly more guaranteed income but with less liquidity. The shorter surrender period variable annuity is likely to produce less total income for the client than the standard surrender variable annuity or the lifetime income annuity.

In the end, the choice of income strategy will come down to the advisor's preferences and the client's needs. Regardless of the strategy you select, look for products and planning resources to help you effectively implement the strategy. **b**

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FEATURE STORY

How Do I Move My Money?

Navigating the Minefield of Contract Exchanges, Plan-to-Plan Transfers and Rollovers

BY MICHAEL WEBB

Though the 403(b) final regulations became effective nearly three years ago, rampant confusion remains with respect to moving one's money into and out of plans and between vendors within a 403(b) plan. In fact, to this day, I have seen plan sponsors and participants consistently attempt one type of transaction (rollover, exchange, or plan-to-plan transfer) when another transaction type would have been far more appropriate.

This article will attempt to demystify the regulations that govern participants' movement of 403(b) (and 457(b)) assets, and will address some common misconceptions about the differences between these three very distinct types of transactions.

Rollovers Out of Plans

The good news: Rollovers were unaffected by the final regulations.

Plan-to-plan transfers can be used to move assets between similar plan types, but beware of the significant restrictions that apply to such transactions — especially with respect to ERISA plans.

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The bad news: Many participants did not understand the rollover rules in the first place!

Understanding a rollover is grounded in the two principles:

- One may only roll over an eligible rollover distribution, which means that an individual must be eligible for a distribution under a retirement plan.
- A rollover is the only one of the three transaction types (ignoring the limited exception for transfers to purchase service credits under a governmental defined benefit plan) whereby assets can move between different types of plans (such as 403(b) to IRA, or a 403(b) to 401(k), etc.)

The first principle is the most misunderstood aspect of rollovers. If there is no distributable event (*e.g.,* with respect to elective deferrals, an in-service employee who is not at least 59½ years of age wishes to move assets), there can be no rollover.

As a reminder, in-service distributions of elective deferrals prior to age 59½ are generally only available in the event of financial hardship, and hardship distributions are not eligible for rollover. If the plan is even more restrictive — for example, if all in-service distributions are prohibited — then rollovers for current employees out of the 403(b) plans of their current employer would not be possible.

Distributions on certain types of employer contributions (as opposed to elective deferrals) may be less restrictive; but these are often more restrictive than the restrictions on elective deferrals. Thus, most active employees are not in a position to use rollovers out of the 403(b) plan of their current employers.

The rules are similar for governmental 457(b) plans. However, for 457(b) plans of private tax-exempt entities, rollovers are not permitted.

The second principle involves an important distinction, within the context of the first one. Let's take the example of an individual who wishes to move assets from a 403(b) plan to an IRA. Since different plan types are involved, it is clear that the only allowable transaction is a rollover. Thus, we would ascertain whether the employee is active or has had a severance from employment. If the employee has experienced a severance, and is no longer an employee of the plan sponsor, a rollover may be completed, with a rare exception when distribution of certain plan assets cannot be withdrawn until actual retirement. If the employee is active, chances are he/she cannot complete a rollover, unless another distribution eligible event (*e.g.,* attainment of age 59½, if the plan permits), has occurred. No distribution means no rollover.

> ***Rampant confusion remains with respect to moving one's money into and out of plans and between vendors within a 403(b) plan.***

Any rules that would apply to ordinary distributions, such as spousal consent to waive a QJSA for ERISA plans, would apply to rollovers as well. Lastly, 403(b) information sharing agreements (ISAs) are not required for rollovers out of a 403(b) plan.

Contract Exchanges

Two types of transactions arose from the ashes of Revenue Ruling 90-24 transfers, which were eliminated under the final 403(b) regulations. They are contract exchanges and plan-to-plan transfers.

Unique to 403(b) plans, and unlike rollovers, contract exchanges may be made prior to a distributable event, such as severance from employment. Thus, for in-service employees, contract exchanges are much more viable. The disadvantage is that contract exchanges are only permitted within a plan that permits exchanges, so assets cannot be moved outside the plan in this fashion.

Thus, contract exchanges are only utilized in plans with multiple approved providers. Such providers must be specifically listed in the plan as being approved in order to receive a contract exchange of assets.

Approved providers are generally providers to which current contributions are being made, although it is possible to list "exchange-only" providers in the current plan document. Such providers would not be eligible to receive current contributions, but could receive exchanges. That actually occurs relatively rarely in non-ERISA plans. ERISA plans often, however, contain "inactive" plan vendors that are required to remain part of the plan under ERISA.

In addition to the requirement that the plan must permit exchanges, there are two other requirements for contract exchanges:

- The accumulated benefit after the exchange must equal the accumulated benefit prior to the exchange. (Note that the application of surrender charges would not violate this requirement.)
- The distribution restrictions in the new contract must be as stringent as those in the prior contract, and the new contract issuer must agree to provide the employer with information necessary for compliance with the final 403(b) and other tax regulations for transactions like loans and hardship distributions.

It should be noted that the second requirement does not necessarily call for the execution of a separate information sharing agreement, since all providers receiving ongoing contributions would be required in their written plans to share information. An information sharing agreement would only be necessary for the "exchange-only" recipient providers described above.

Finally, rules that would apply to rollovers, such as spousal consent to waive QJSA for ERISA plans, would not apply to contract exchanges. In that case, a distribution is not involved, and, moreover, assets remain within the plan.

Plan-to-Plan Transfers

The third method of moving assets is via a plan-to-plan transfer, which is permitted in both 457(b) and 403(b) plans, but with differing restrictions.

As the name of this type of transaction indicates, it is used to transfer assets between plans, as opposed to within a plan, where the contract exchange would be the appropriate transaction.

Unlike a rollover, a plan-to-plan transfer is permitted only between plans of the same type (*e.g.,* 403(b) to 403(b), 457(b) to 457(b), etc.). However there is a limited exception to this same-plan-type rule for transfers to purchase service credits under a governmental defined benefit plan (see below).

Unfortunately, 457(b) plans involve a further complication: plan-to-plan transfers are not permitted between 457(b) plans of governmental and tax-exempt entities. In addition, plan-to-plan transfers are further restricted by plan type. For governmental plans, an active employee may transfer his/her current 457(b) plan assets to another 457(b) plan maintained by his/her current employer; transfers are not permitted to plans of prior employers.

The final 457(b) regulations limit transfers between plans of tax-exempt entities to those employees who have incurred a severance of employment from one plan sponsor and subsequently wish to transfer assets to the 457(b) plan of their current tax-exempt employer; active employees of tax-exempt entities may not transfer plan assets. Such 457(b) plan-to-plan transfers, while permissible, are relatively rare, and thankfully so, since the rules are so convoluted.

Plan-to-plan transfers are likely to be only slightly more commonplace for 403(b) plans, since rollovers will be available for many employees who are eligible for plan-to-plan transfers. However plan-to-plan transfers will be permitted in two situations where rollovers would not be permitted, assuming the employee was not eligible for a distribution.

Specifically, the final 403(b) regulations permit transfers by an active employee from his/her current 403(b) plan to that of a prior employer or to another 403(b) plan of his or her current employer.

Several caveats do apply. One major issue is the requirement that both the receiving plan and the current plan permit such transfers. In other words, the current plan must permit transfers out, and the receiving plan must allow transfers in.

Having seen completed plan documents of various plan sponsors, I can state that it may be difficult to find both a plan that permits transfers out, and a receiving plan that permits transfers in. Many plans restrict transfers out, due to vendor contract restrictions, while a number of plans also limit transfers into the plan, out of concern that any defects associated with transferred assets under the prior plan could carry over to the current 403(b) plan.

The IRS's model plan language emphasizes this concern, requesting confirmation that the transferor plan is a plan that "satisfies section 403(b) of the Code."

In addition, for ERISA plans, certain sections of the Code and ERISA essentially conflict with the plan-to-plan transfer provisions. Though those fiduciary and other provisions are beyond the scope of this article, consider the following example of one such conflict.

Suppose a plan contains a QJSA provision whereby spousal consent is required for loans and any distributions that are not in the form of a QJSA. Imagine a participant whose assets are currently in an ERISA 403(b). If there is a non-ERISA 403(b) plan, which is also maintained by her current or prior employer, she could circumvent the spousal consent provisions by simply completing a plan-to-plan transfer of assets to a non-ERISA plan, where spousal consent would not be required for future loans/distributions. This example explains only one of many reasons that ERISA plans would not permit individual plan-to-plan transfers out of their plans.

Information sharing agreements are not required for plan-to-plan transfers. As with contract exchanges, rules that would apply to rollovers would not apply to plan-to-plan transfers, since a distribution is not involved.

Finally it should be noted that there is a special subsection of the plan-to-plan transfer provisions that permits 403(b) plan assets to be transferred to a qualified governmental defined benefit plan for the purpose of purchasing permissible service credit in the defined benefit plan. This is the sole example of where a plan-to-plan transfer can be made between different plan types (a 403(b) plan and a 401(a) defined benefit plan, in this case).

Conclusion

If one is attempting to move assets between different plan types (*e.g.,* 403(b) to IRA), one will need to be eligible for a distribution from the plan one wishes to move assets from, since only rollovers are permitted in such a scenario. Plan-to-plan transfers can be used to move assets between similar plan types, but beware of the significant restrictions that apply to such transactions, especially with respect to ERISA plans.

In summary, when transferring assets between plan providers within a 403(b) plan, contract exchanges are the transaction of choice.

Please note that this article is for general informational purposes only, and is not intended to be taken as legal advice or a recommended course of action in any given situation. Readers should consult their own legal advisor before taking any actions suggested in this article. b

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Audit Concerns for 403(b) Plan Sponsors: Year 2

BY STEVEN P. KJAR AND
EMILY POWERS

Most 403(b) plan sponsors have now completed their second round of governmental filings and independent plan audits under the regulations that went into effect on Jan. 1, 2009. Since these requirements are still relatively new, plan sponsors continue to run into questions and issues.

In the Winter 2010 issue of *403(b) Advisor,* we published "Audit Concerns for 403(b) Plan Sponsors," which highlighted issues uncovered during the first year of the new regulations and provided solutions to help plan sponsors mitigate risks in the future.

Now that Year 2 of the new requirements is behind us, we thought a follow-up article focusing on common audit issues uncovered during the most recent plan audits would be a helpful tool for plan sponsors. We'll discuss the audit issues that CapinCrouse, an independent accounting and auditing firm specializing in not-for-profit organizations, saw most frequently during audits performed for its clients. We'll also provide Lockton Retirement Services' suggestions for correcting these issues. These suggestions are based on our work as an independent retirement plan consulting firm, specializing in providing solutions to retirement plan sponsors.

AUDIT CONCERN	SUGGESTED SOLUTIONS
Definition of Compensation • Contributions to a 403(b) plan are based on the definition of compensations found in each plan document. The most recent audit results indicate that many plan sponsors administered their plan using a definition found in the plan document. This is especially true for plans that were drafted for the first time in 2009. • For example, many 403(b) plan documents define compensation as "gross income." Historically, 403(b) plans have excluded overtime and bonuses from the definition of compensation. Housing allowances are also commonly excluded. Plan sponsors are required to administer the plan using the correct definition of compensation. If you are using "gross income", exclusion of compensation is an error and will be noted in your audit results.	• Define your objective for the definition of compensation. • Review your plan's definition of compensation and compare it to your payroll procedures. If they don't match, you need to either change your payroll processing for plan contributions or amend your plan document. • Your retirement plan consultant, your retirement plan vendor or an ERISA attorney can assist you in this.
Discrimination Testing • Under the universal availability requirements, your plan must now be available to all employees. The latest audits found that many plans — especially those adopted for the first time in 2009 — include blanket language stating that all employees are eligible to participate, but in operation, certain classifications of employees are excluded from participation. This is a violation of your plan provisions.	• Plan sponsors can "exclude" certain employees from the universal availability requirements. • Your plan must be expressly written to exclude these employees. Plan sponsors must operate a plan in compliance with the plan document. • Common classes of employees improperly excluded: temporary employees, part-time employees and student employees. • Review you plan provisions and check with your Human Resources department to determined how you currently administer plan eligibility.
Incorrect Calculation of Distributions • Plan administrators did not calculate the correct vesting percentage, tax withholding or both.	• Most plan sponsors rely on their third-party plan administrators to calculate and distribute funds. • Consider requiring the plan administrator to review and sign before a withdrawal is approved. • Consider implementing 100% immediate vesting in all contributions.

AUDIT CONCERN	SUGGESTED SOLUTIONS
Hardship Withdrawals and Participant Loans • Some plan documents do not allow for hardship withdrawals or participant loans. Many third-party administrator (TPAs) are equipped to process these requests without plan sponsor direction. Typically, participants request loan or withdrawals directly from the TPA, and the plan sponsor is unaware of the transaction.	• Plans that use multiple vendors are especially vulnerable to this problem. • Many plan sponsors have adopted a single vendor to control these types of issues. • Some plans require the plan sponsor to review and approve loans and withdrawals. • Discuss plan provisions with your vendors, communicate your specific objectives in writing, and make sure vendors follow them. • Retirement plan consultants specialize in vendor management and in making sure the plan is administered according to the provisions of the plan document.
ERISA Fidelity Bond • If you have an ERISA retirement plan, you are required to have an ERISA fidelity bond for those individuals with access to plan assets. Note that fiduciary liability insurance is not the same as an ERISA fidelity bond.	• Review Field Assistance Bulletin 2008-04, Guidance Regarding ERISA Fidelity Bonding Requirements. • Contact a broker who can help you secure the appropriate bond.
Lack of Plan Governance • Many plan sponsors are unaware of regulatory compliance requirements and their responsibility for oversight of the plan.	• Plan sponsors are required to have a process to evaluate plan investments, fees, services, revenues and compliance. • A best practice for plan sponsors is to establish a retirement plan committee that implements a process for regular oversight of your plan.

The overriding cause behind these issues is the fact that many 403(b) plans are not being administered in accordance with the written plan document. Plan administrators are required to follow the provisions of the written plan document, and plan sponsors are responsible for making sure the plan is written according to their specific objectives and then administered as written.

As we noted in last year's article, help is available. Consultants specializing in 403(b) retirement plans are available to help plan sponsors navigate these issues. Attorneys and auditors can also provide compliance support for your plan.

It is very important for your plan to be administered correctly and in accordance with your specific objectives. The audit process can help you define areas for improvement and provide the opportunity to obtain assistance in complying with the law, your plan document and your specific objectives. ■

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RMDs and the 21st Century 'Grandparent's Delight'

BY FRANK OWEN, III

A new twist on an old idea may be a good way to turn RMDs into an unexpected legacy for a client's grandchildren.

As Dickens wrote in his classic novel, *A Tale of Two Cities*, "It was the best of times; it was the worst of times…" Of course, he was writing about the economic and political unrest in London and Paris in the late 18th century. I am no literary scholar and this is no political essay, but I think the beginning lines of that book seem appropriate to what today's retirees face — especially the educational retiree. The best of times because they have in most cases a secure pension and Social Security check each month, yet the economic uncertainty still exists.

They hear daily about the looming federal debt, the uncertainty of entitlements, looming inflation, a low interest rate environment and political gridlock in Congress. As uncertain

Do you have a systematic program to discuss legacy planning ideas with your retiree clients, or does the check just go out and away?

as things may be, most of my clients don't have to worry about losing a job or foreclosure on their homes, so life, while it could be better, is still pretty good.

But worry they do, because they know that the future their children and grandchildren face may not be as secure as theirs was 40 or 50 years ago. Politically they may feel helpless in correcting that problem. Financially they have enough to live on, but not an excess of assets to leave as an inheritance. So it is also the worst of times to them.

Blast from the Past

I entered the financial services profession in 1978. As a young insurance agent I was introduced to the phrase, "grandparent's delight." You may remember it too. Upon the birth of a grandchild, the grandparents bought a life insurance policy on the child that would provide an immediate death benefit, future opportunity to buy more insurance without proving insurability and a buildup of cash values that could be used later in life.

While writing this article I Googled "insurance policy on grandchildren" and it led me to the Gerber Life Grow-Up Plan. Not much has changed in 35 years.

I think the two biggest differences between today and 1978 are the uncertainty of the times and the sophistication of the buyer. Not that these policies were bad, but I think more importantly they did not really allow grandparent to leave a legacy for their grandchildren.

RMD = Outflow

Now let's look at it from today's perspective and reality. Most advisors who practice in the 403(b) environment have done an excellent job helping their clients accumulate assets for retirement. Despite some of the discussion about fees and markets, most of our clients would say that the most important thing to them was to have a secure financial retirement and someone they could trust to help them sort out all of their options. For the large part, most 403(b) advisors have succeeded in that effort.

Many of my clients have been able to retire with their state pension and Social Security as their primary income sources. The 403(b) assets have become an inflation hedge or cash access for emergencies or opportunities. As a matter of fact, many of my clients would prefer not to take money out but at 70½, they have no choice.

They do have a choice on what they do with those withdrawals, however. Last year we finally realized that more than $1.5 million a year was flowing out of our clients' accounts for required minimum distributions (RMD) and we had no plan to help redirect it.

How about you? Do you have a systematic program to discuss legacy planning ideas with your retiree clients, or does the check just go out and away?

Focus on RMD Income

Almost all retirees are parents and grandparents. Many of them believe the next generation's retirement will not be as secure. That's a sad statement but a widely shared perception. This means we have the perfect opportunity and obligation to help our retired clients address that concern for their heirs.

Some advisors have already addressed this by focusing on using the RMD income to fund a long-term care contract to make sure that assets are not depleted and are still there to pass on to the next generation. Others have discussed survivorship life to allow parents to spend the inheritance but leave it tax free after their death.

Those are all worthwhile discussions, but I remember years ago a client of mine retired and said his focus would be on the "4Gs" of his life: Grandma, gardening, God and grandkids. His eyes really lit up when he said "grandkids."

Most retirees will say that they are worried about what will happen to their grandchildren, or maybe they are concerned that if left to the children it will get spent. So why not offer a solution? Most grandparents help with the education of their grandchildren; can you imagine the legacy and impact of providing something to a grandchild when they reach retirement?

Many people are worried about how the world will look 50 years from now. Will their children and their families enjoy the same standard of living? Do they worry how they will help resolve that concern since they won't be here 50 years from now?

Possible Solution

So here's an idea that might be a useful planning tool. Today's life insurance products are much more flexible and innovative than they were 35 years ago, with computers generating

Most retirees will say that they are worried about what will happen to their grandchildren, or maybe they are concerned that if left to the children it will get spent. So why not offer a solution?

illustrations in minutes. In 1978 it took weeks to get an illustration. But speed needs to be tempered with letting clients see the advantages, disadvantages and uncertainties that can occur.

Why not have the grandparents purchase a policy on the life of a grandchild? Making sure they comply with all of the issues regarding guideline premium tests. Consider using a universal life product and an income benefit rider. As you know, the devil is always in the details and it's important to stay within those guidelines.

Let's look briefly at an example using a 9-year-old granddaughter. The grandparent funds the policy at $1,000 per year for seven years. In exchange, a death benefit is created for $100,000 on the grandchild. No further payments are made or required beyond that point in time. The death benefit is simply a byproduct of the strategy because we are focusing on income in the future.

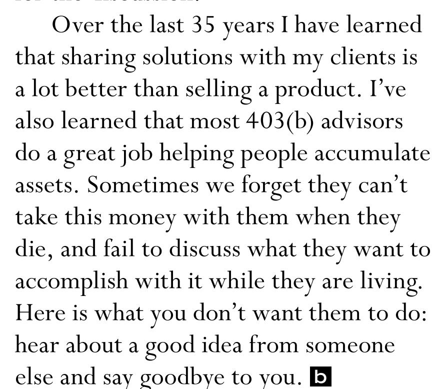
The policy is left to accumulate value until the grandchild reaches age 65. Contract performance is unknown and markets are uncertain, but for this example let's assume the S&P averages 5% per year for the next 56 years. At age 65 the accumulated cash value would generate $33,487 annually in guaranteed income through policy loans not currently subject to taxes, for the life to the grandchild. Of course, income payments are based on the insurer's ability to pay.

You can imagine the compounding effect on the internal build-up of value — and you can imagine the skeptics' concerns about not knowing what the future holds. There are a lot of unknowns; and there will always be critics. I can hear them now: Will the grandchild keep the policy that long; will the S&P grow at 5% each year; will the company be in business when they retire; what about tax law changes; and will inflation offset the value of these dollars?

We know this: Assuming a 3% inflation rate each year, the purchasing power of $33,487 is the equivalent of about $6,000 today. Inflation will certainly affect the numbers, but would $6,000 per year help a grandparent today to supplement their lifetime of saving? But even beyond that, the biggest unknown is this question: Will my grandchild's future be as secure as mine?

Solving Beats Selling

If you have clients receiving an RMD each year that they don't need for their income, why not have this discussion? Maybe instead of leaving a legacy of love for the next 50 years, some will decide to put it in a college savings program to help save for college. Maybe they purchase long-term care coverage or buy a survivorship life policy to pass it on. Maybe they do nothing but thank you for the discussion.



Over the last 35 years I have learned that sharing solutions with my clients is a lot better than selling a product. I've also learned that most 403(b) advisors do a great job helping people accumulate assets. Sometimes we forget they can't take this money with them when they die, and fail to discuss what they want to accomplish with it while they are living. Here is what you don't want them to do: hear about a good idea from someone else and say goodbye to you. **b**

Frank Owen III is president of FR Owen & Associates in Charlotte, N.C. He is a member of the editorial board of 403(b) Advisor *magazine.*

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- Important changes to the determination letter process
- Form 8955-SSA guidance
- New IRS practice rules in Circular 230
- Latest guidance for 403(b) plans
- Guidance for governmental plans
- Latest court cases and IRS/DOL/PBGC guidance

No Lemons

BY YANNIS P. KOUMANTAROS AND
ADAM C. POZEK

Lemon Wallet • [www.Lemon.com]

This cheap tech won't necessarily help you earn more bread, but it could save your bacon. Lemon Wallet is part Passbook and part CardStar, mixed together and improved. Basically, it allows you to use your smartphone camera to store pictures of your ID, credit cards, membership cards, rewards club cards — heck, even your library card. For some, it recreates the barcode for easier scanning; for others, it enhances the photo to show a clear image of all the information on the face of your cards. With bank-level security and encryption, your data is safe.

A few weeks ago, I was headed out of town and arrived at the airport only to realize I had left my wallet at home. Although the images I had stored in Lemon Wallet were not enough to get me past the TSA, the airline used the picture of my driver's license to rebook me on a later flight. I was able to use the picture of my Visa to re-charge my Starbucks card so that I could grab breakfast and coffee while I waited for my wife to arrive with my wallet. (She only gave me a little bit of grief for it.)

The basic version of Lemon Wallet is free, but you can upgrade to the premium version for $39.99 per year to link directly to your banks' websites to manage your accounts, export transaction data to Excel or, in the event your actual wallet is ever lost or stolen, have Lemon Wallet automatically cancel and replace all of your credit cards for you.

CreditKarma • [www.CreditKarma.com]

My guess is that you have a pretty good idea what your current credit score is, right? Us too. However, do you really know how certain elements of your day-to-day life affect your credit score, and what factors drive your score up or down?

CreditKarma entered the marketplace for one solid purpose — accessing all of your finances, all in one place, all for free. Sponsored by advertisers, all of us as consumers get this application for free! The premise is simple — CreditKarma pulls a soft inquiry from the credit bureau every time you log in, runs an algorithm on historical data and makes an educated guesstimate — accurate to about 99% — of your credit score.

The free credit monitoring is a huge bonus because you can actually have CreditKarma push notifications to you anytime someone pulls a hard inquiry on your credit or opens up a new account, or when you hit a certain threshold on your credit utilization percentage. This application really hits a home run, and should be downloaded on all smartphones.

FlipBoard • [www.FlipBoard.com]

There's a lot of information out there on the Interwebs these days. Some of that info would be great to pass along to plan sponsors or participants if only there was a way to package it to look a little more polished than simply forwarding a link or copying and pasting the text. Behold, we give you FlipBoard.

After starting out as a social newsreader, FlipBoard evolved to allow users to create their own electronic magazines from content they curate from around the Internet. Create as many magazines as you want on as many different topics as you want. You choose the content. Need some editorial assistance? No problem. FlipBoard's "Invite Contributors" feature lets you, well, invite others to contribute to your magazine.

Once you've created your masterpiece, simply click a button to share via Twitter or Facebook. You can also grab a URL to share via text message or email, or to copy and paste anywhere you want. Like, say, an article on Cheap Technology — at http://flip.it/7h8h3 — created in about five minutes. And oh, yeah … it's free!

JoliDrive • [www.JoliCloud.com]

There's cloud storage; there's social media; there are myriad other online locales where you might have to sweep away the virtual dust bunnies to find your information lurking. But before you can think about sharing any of it, you have to be able to find and manage it. That's where JoliDrive comes in. Via their website, you can manage accounts and access data from across the Internet.

Cloud storage? Yep. JoliDrive includes preconfigured links to DropBox, Box.net, Google Drive, SkyDrive and SugarSync, just to name a few. Social media? Check. There are links to Facebook, Google+, YouTube, Instagram and Flickr. Need more? Try SlideShare, Tumblr, Scribd and Instapaper.

Simply click the icon for the service you want to add, enter your login credentials and presto — you have a mission control dashboard that would make NASA jealous. And one of the best parts is that it won't cost you a penny.

Adam and Yannis are always on the lookout for new and creative mobile applications and other technologies. If you have any tips or suggestions, please email them at adam.pozek@dwcconsultants.com and yannis@spectrumpension.com.

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Conversion Communication in a Commoditized World

BY SARAH SIMONEAUX

Plan conversion, no matter how we thin-slice it, is a detailed and complex process. Don't underestimate the importance of communication in it.

"Facebook me," he said, in answer to my question about the best way to reach him. I stared in astonishment. This was not my college sophomore son, but my 80-year-old father. Seeing my wide eyes, he went on: "Look, you know I've never liked talking on the phone. I reserve email for my students, and I keep Facebook open on my iPad so I can chat with my grandchildren. Facebook is the way I like to communicate."

While I was surprised, his answer made sense. As a law professor, he was used to dealing with Millenials and their electronic communication preferences. I had just never thought to ask him about how he wanted me to communicate with him, and it explained why he was slow to return my calls.

How does my octogenarian Gen Y-loving father figure into the retirement services profession? All I had to do to get him to respond to me was to ask how he wanted to

be communicated with. And the answer he gave me was not what I expected. Think about how often that happens in our business: We fire off emails or leave voicemails requesting information, asking detailed questions and delivering complex information without ever asking how our clients want to receive that information.

Takeover plans — which represent a large part of our business these days — are especially vulnerable to communication missteps. Service providers ask for list after list of required items and then hand the plan off to another staff member who may or may not be aware of what has happened in the initial conversion process. It's a recipe for turning a consultative service provider into a commodity. Meaningful communication and teamwork should be at the core of our business, especially when clients first encounter the services staff with their takeover plan.

First Contact

The first impression of a service firm is the key to winning and keeping clients. Malcolm Gladwell, in his book *Blink*, describes how people use "thin-slicing," or quick first impressions, to form lasting opinions of others. Gladwell profiles Dr. John Gottman of the University of Washington, who is able to predict with 90% accuracy whether or not a couple will stay married for the long term by watching their conversation about a mundane topic — for less than one minute.

Clients and advisors will be forming lasting impressions of services staff in this first minute of communication. Which question would leave a better impression of the company: "We need your signed plan document, last year's testing reports, this year's census and your employees' enrollment forms" or "Before we get involved in your plan's details, how would you like us to communicate with you?" Listen to the answer and then stick to that communication method. Don't assume what the answer might be — remember my Facebook-loving dad's response to me.

Troubleshooting

What do you do when you find the requested way of communicating isn't working? First, apply the "rule of two." If you have to send two emails about the same topic, pick up the phone. If you have to call a second time, ask when would be a convenient day and time to set up a call.

Second, ask a question rather than reciting a list: "What can we do to help you provide this information?" These tips may be intuitive to salespeople and business owners, but conversion specialists and administrative staff are likely not to have been trained in these important communication techniques.

Regardless of how intuitive or well-trained everyone is in communicating, things will go wrong. Ross Shafer, a keynote speaker a few years ago at The ASPPA 401(k) SUMMIT, points out in the book *The Customer Shouts Back* that 88% of customers would stay with the firm after being badly treated if they felt that their complaints were heard and problems were fixed.

Foster Communication Skills

Malpractice insurance companies will give premium discounts to doctors who go through communication training. Why? Their research shows the highest probability that a physician will be sued is not for making mistakes, but instead when they have poor relationships with patients and staff. A services firm should foster an environment where employees can face reality and take responsibility without placing blame on others, as well as having the freedom to suggest changes to improve flawed processes and bad customer service.

Knowing how to communicate well with clients and advisors should be a key skill for takeover plan associates. However, these employees are often put in this position because of their attention to detail and their qualified plan knowledge, and they may have limited customer service skills. They may also be struggling to balance conversion with a caseload. As a result, curt and rigid client communication is likely to be the first impression of the company. While soft skills training can help break the communication logjam, consider adding a conversion team member with a limited or no caseload who can build relationships among clients, providers and advisors.

> "Meaningful communication and teamwork should be at the core of our business."

Remember that successful communication strategies have these five ingredients:

1. Find out how people want to communicate and stick to that method.
2. Use the "rules of two."
3. Remember that you are building relationships and not just gathering data.
4. Train everyone on "soft skills."
5. Make sure you are communicating the values and objectives of the firm.

Effective communication fosters human connections in an increasingly technological and commoditized retirement services world. ■

Sarah Simoneaux, CPC, is president of Simoneaux Consulting Services in Mandeville, LA, and a principal of Simoneaux & Stroud Consulting Services. She is a former president of ASPPA and previously served on the Education and Examination Committee as a Technical Education Consultant. She is the author of the textbook, Retirement Plan Consulting for Financial Professionals, *which is used for the PFC-1 course in ASPPA's QPFC credentialing program.*

TAKEAWAY

The IRS Wants to Know: How Effective is the Opportunity to Participate?

BY ELLIE LOWDER

> *Reports have included audits of plans where only 18-20% of employees actually participate in the plan.*

IRS field examiners are asking employers to share their employee education plan when participation rates in the 403(b) plan are low — causing the IRS to question whether the rules governing the universal availability requirement are being met.

In reports of recent IRS audits of 403(b) plans, we're learning that IRS field examiners are asking employers to share their employee education plan when participation rates in the 403(b) plan are low. Reports have included audits of plans where only 18-20% of employees actually participate in the plan. Those low participation rates are causing the IRS to question whether, in fact, the rules governing the universal availability requirement are being met.

As a Senior Staff Specialist in the IRS audit area said, "The field examiners are being provided the actual participation rates of an employer where an audit is planned, and that is raising red flags. The examiner is intent on discovering whether, in fact, an "effective opportunity" has been given to employees to not only enroll in the plan, but to continue to make contributions, and increase contributions over time."

In a telephone interview with the IRS Staff Specialist, I asked the staff member to define what is meant by "effective opportunity" — or in simpler terms, "What is the makeup of a good education plan?" The answer? "The educational activity must be diverse to fit the needs of a wide range of employee types — and, the annual meaningful notice of the right to participate and make changes should be followed up with year-round activity." Those activities include:

- frequent educational workshops
- financial advisors to provide face to face enrollment and counseling services to employees
- online tools for those employees comfortable with seeking out and acting upon retirement savings information online. (Note: In a recent report from the Census Bureau, we learned that roughly 30% of the population either does not have a computer (16%) or, if they have a computer, does not have Internet service (14%).)
- Written communications designed to reach all eligible employees to include specific details to make it easy to gather information leading to enrollment, or changes in contribution levels, or approved product providers.

Financial advisors (and TPAs) will want to begin discussions with these employers and offer assistance to them, only so that an effective opportunity to participate in the 403(b) plan is provided. This will provide a double win for employers that set up an employee education program:

- the program will increase employee satisfaction with the benefit provided by the employer; and
- employees who participate in saving their own retirement dollars are more likely to retire at normal retirement ages, leaving room for employers to save budget dollars when those departing employees are replaced with new employees starting at the lower end of the salary scale. b

Ellie Lowder, TGPC, writes frequently for 403(b) Advisor. *She is a consultant with TSA Training and Consulting Services in Tucson.*

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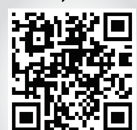

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