AdvisorFacts

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Helping 401(k) Participants Invest More Effectively

"Retirement readiness" and "participant outcomes" have not only become buzzwords over the last five years, they have become a key objective for many plan sponsors. Employers wanting to take a proactive approach toward helping employees prepare for retirement are learning that there is a great deal they can do to promote positive participant outcomes.

Advisors can play a critical role in helping sponsors identify concerns with current participant investment behavior and finding options for improving participants' chances of reaching their retirement savings goals.

Assess Asset Allocation

For existing 401(k) plan sponsors, a good first step is to evaluate whether participants' accounts are appropriately diversified. Plan advisors may want to help sponsors evaluate the current investment line-up.

- Is the investment menu sufficiently broad to allow participants to diversify their investment risk and adjust their risk exposure over time?
- Are there so many investments that participants with limited investment expertise are confused and overwhelmed by their investment responsibilities?
- Does the investment line-up meet the particular needs of the workforce demographic?

Provide Investment Education

With an assessment of participants' investment allocations, advisors can help sponsors develop an investment education strategy. Some participants may lack an understanding of very basic financial concepts, while others may be ready for more advanced investment topics.

Re-Evaluate Default Investment Options

In assessing whether the plan's investment menu is appropriate for the plan demographics, significant attention should be paid to the plan's default fund. Employees who are uncomfortable directing their own investments may rely on the default option chosen by the plan sponsor as plan fiduciary. Plans with an automatic enrollment feature may have a higher number of employees who don't take steps to select investments, increasing the number of participants who end up in the plan's default fund. In a study of participants who were automatically enrolled, only 17% changed from the default investment within the first few years of participation.[1]

With the creation of Qualified Default Investment Alternatives (QDIAs), most plan sponsors are now selecting default funds that meet the QDIA criteria. If the QDIA requirements are met, the plan sponsor will be relieved of fiduciary liability for the performance of the default investment.[2]

Consider Re-Enrollment

To proactively drive participants to more appropriate investment allocations, some sponsors choose to implement a re-enrollment strategy in an effort to move participants who were defaulted into an investment that is not appropriate for long-term savings or who have not been actively managing their assets to the plan's new default investment – typically a QDIA. Candidates that might benefit from a re-enrollment strategy include participants who:

- Were previously defaulted into or have chosen a very conservative investment
- May be invested aggressively for what is a typically acceptable risk/return level for their age
- Have not reviewed or adjusted their investment allocations since enrolling in the plan
- Have investment allocations that are generally viewed as problematic

Advisor Action Steps

- Help sponsors evaluate the plan's investment menu
- Assess the appropriateness of current investment
- Provide participant investment education
- Help sponsors monitor their default investments
- Educate sponsors about re-enrollment strategies

Footnotes

[1]Rand Labor & Population, Working Paper: Opting out of Retirement Plan Default Settings, Jeremy Burke, Angela A. Hung, and Jill E. Luoto, 2016,
https://www.dol.gov/sites/default/files/ebsa/researchers/analysis/retirement/opting-out-of-retirement-plan-default-settings.pdf

[2]Department of Labor (DOL) Default Investment Alternatives Under Participant Directed Individual Account Plans, October 2007,
http://webapps.dol.gov/FederalRegister/HtmlDisplay.aspx?DocId=13321&AgencyId=8&DocumentType=2

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